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Roth IRA's for Minors

by Julie Lobaza

Did you know you can open a Roth IRA for a child at a young age? Parents, grandparents, and other family members can help jumpstart their loved one's retirement savings by contributing to a Roth IRA; allowing them to begin taking advantage of tax-free growth, while also teaching children the importance of saving.

These accounts hold all the same benefits as a regular Roth IRA but require an adult to serve as a custodian to control the assets and assist in the investment decisions. Custodial Roth IRAs are maintained by the adult until the child reaches age 18 (in Michigan). At that point in time, the account is transitioned to a regular Roth IRA solely in the child's name.

If your child has earned income, they may automatically qualify to make contributions. You could reward a child for doing choirs, or even setup a match to entice them to make contributions of their own. Income from a job can be from their own business, their parent's business, or any employer. The requirements for income received must be from reasonable work performed, at the going market rate; and the total contribution cannot exceed the child's income for the year or $6,000. When tracking a child's earnings, it is a good idea to keep an accurate record. Ideally, a child would receive a W-2 or Form 1099 to assist in tracking. Jobs such as babysitting, or dog walking don't traditionally require a W-2 or 1099. In those cases, you need to keep detailed records of work performed and amount earned to support any contributions made to their Roth IRA.

When it comes to utilizing money from a Roth IRA, you would normally have to wait on withdrawing the "earnings" until age 59 ½. However, the account owner may be able to take out up to 100% of the original "contributions" at any time without taxes or penalty.

Note that there are a couple of situations which allow for early withdrawals if the account has been opened for at least 5 years. You could make a federal and state tax-free withdrawal up to $10,000 of earnings if used for a first-time home purchase. You can also withdraw money for qualified educational expenses without paying the 10% penalty, but you would still incur taxes on the earnings.

Investing even small amounts at an early age can make a significant difference over time. Meanwhile, a Custodial Roth IRA can be great tool to help your child learn about saving, preparing them for financial stability in the future.

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