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HELPING YOUR CHILDREN SAVE FOR THE FUTURE

CONSIDER A CUSTODIAL ACCOUNT

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Clients often ask me for ideas on how to help their children save for the future. While a piggy bank can be handy for petty cash, there are better options for saving more significant amounts of money. A great place to start is with a custodial account, which is an account opened for a child by an adult. There are several different types of custodial accounts that can help you save for your child's future.

1. Custodial bank account – A great time to start saving is upon the birth of a child, as this is often when friends and relatives give cash gifts to the new parents. You can use this cash to establish a bank account in your child's name with an adult listed as the custodian. The custodian is tasked with managing the funds until the child reaches the age of majority (age 18 or 21 based on your state's guidelines).

   Options for such an account include a UTMA (Uniform Transfers to Minors Act) or UGMA (Universal Gifts to Minors Act). Both types of accounts allow you to transfer assets to a minor without establishing a trust. Any assets added to the account are considered irrevocable; in other words, the child has full access to spend the money as he or she wishes upon reaching the age of majority.

2. Custodial investment account – Once a custodial bank account is established, you may consider establishing a custodial investment account. As of April 2021, interest rates on bank accounts are low (not much more than you'd earn in that piggy bank). If you have a time horizon of five to seven years or more and are willing to take on a bit more risk, you may want to consider a custodial investment account.

   Custodial investment accounts are very similar to custodial bank accounts, but they also provide an opportunity to invest in stocks, bonds, mutual funds and exchange-traded funds (ETFs). You can also link your custodial investment account to your custodial bank account so when your bank account accumulates enough assets, you can transfer them to the investment account.

3. Custodial Roth IRA – Once your child starts working and earning money (babysitting, mowing lawns, refereeing soccer games, etc.), he or she becomes eligible to contribute to a Roth IRA. There is no minimum age to establish a custodial Roth IRA, and these accounts are subject to the same rules of ownership as the custodial accounts mentioned above. Custodial Roth IRAs are also subject to the same contribution limits and withdrawal parameters as a normal Roth IRA. Imagine the potential of starting a Roth IRA at age 12, adding to it every year and realizing the growth of assets over 47 years until reaching age 59 ½!

In addition to helping you save for your child's future, custodial accounts offer a great opportunity to teach your child about saving, investing and the power of compounding interest. As your statements arrive, you can review the accounts with your child to help him or her understand these important financial concepts.

If you have any questions about custodial accounts or their potential tax implications (kiddie tax), or if you would like assistance establishing a custodial account, please contact us. We look forward to helping you save for your child's future.

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