

Need a Gift for a College Graduate?

Consider a Roth IRA

By Gleba & Associates

With time (and compound interest) on their side, a Roth IRA might be the perfect graduation gift for the college grad in your life.

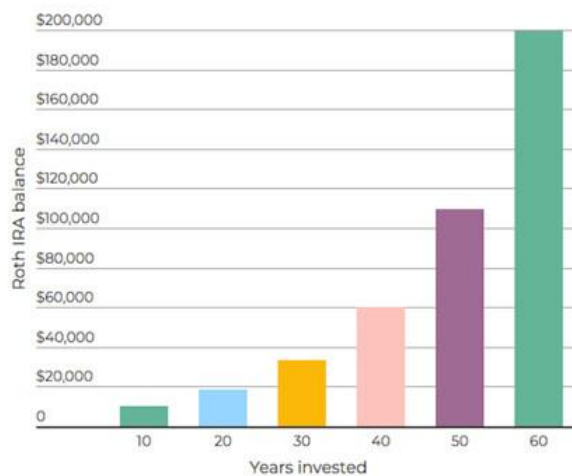
While there are plenty of material things on the wish list of your college grad, consider giving them a Roth IRA as a graduation gift. Sure, it may not be as “fun” as an Apple watch, but they may be thanking you over and over a few decades from now.

Why a Roth IRA?

So why consider a Roth IRA for a graduation gift? Because young adults have the power of time and compound interest on their side. Roth IRA investment earnings will grow tax-free. Putting money away and making regular contributions before the age of 30 will allow their portfolio to grow considerably, even if the contributions slow down from there.

In order to qualify for a Roth IRA, the graduate must have income from work this year. Either a job or a freelance gig like babysitting will qualify. The maximum annual contribution is \$5,500. Here’s an illustration of how a single Roth contribution can grow over time:

How \$5,500 becomes \$200,000



Methodology: One-time contribution of \$5,500, compounded over 10, 20, 30, 40, 50 and 60 years. Includes 6% average annual investment return and monthly compounding; not adjusted for inflation.

Not just a handout

As opposed to a check, giving a Roth contribution will help your college grad start to think about saving and investing. Worried they won't be incentivized to contribute? Consider offering a match, where you put in \$1,000 for every \$1,000 they put in (up to the \$5,500.)

Also, sit down and open the account with the grad. Rather than an electronic funds transfer, consider writing a check, so it is clear that the account is going to be opened and funded.

More of a “nudge” than a “gift”

Technically, there is no way to “gift” a Roth IRA, since the account must be opened by the grad themselves. Once it is opened, you can then give them money to contribute to the Roth. Now, in this context, contributing to a Roth IRA generally means investing. “Don't worry too much about the complex ins and outs at this point,”

“For people just starting out, a low-cost target-date mutual fund, which offers a diversified portfolio, can work — some charge fees as low as 0.2% or less.”

Rules to watch for

- The college grad must have money earned from work this year; that could be a freelance gig or a part-time job.
- The maximum amount the college grad — that is, whoever owns the account — can contribute in a year is the lesser of these two options: \$5,500 (\$6,500 if 50 or older) or their earned income.
- There are income limits on Roth IRAs. For single people, the maximum contribution amount starts to phase out at modified adjusted gross income of \$120,000.
- The grad has to set up their own Roth account. You can write a check directly to the custodian where the account is located or to the student.

Examples are hypothetical and for illustrative purposes only. The rates of return do not represent any actual investment and cannot be guaranteed. Any investment involves potential loss of principal.

Much of the information in this article, including the graphic, originated from an article published by Andrea Coombes on NerdWallet

<https://www.nerdwallet.com/blog/investing/best-gift-for-your-college-grad-a-roth-ira/>