September 2021

wealth management

# Leaving an inheritance **vs** gifting during your lifetime

0113 224 2800

info@truewm.com

Thinking about passing on wealth can be difficult. However, it’s important to consider how you will pass on money and other assets to those who are important to you. This is why inheritance and gifting should form part of your wider financial plan.

These considerations may influence how you use your wealth during your lifetime, what you write in your will, and other decisions you make. Traditionally, people have left their loved ones an inheritance. Yet, for a variety of reasons, more families are passing on wealth during their lifetime. Depending on your goals and circumstances, this can make sense financially, as well as aligning with your wishes.

Does leaving an inheritance or providing gifts now make sense for you?

## Why financial gifts are on the rise

Leaving an inheritance is still a popular way to pass on wealth.

According to research from the Institute for Fiscal Studies, wealth passed through inheritance plays a key role in long-term financial security. The thinktank estimates the median inheritance for those born in the 1980s will be £136,000. This is around 14% of lifetime earnings for this age group.

Inheritances can provide security later in life, so why is a shift towards gifts occurring?

Many young adults are facing financial challenges. As wage growth has stagnated, many are finding it difficult to keep up with day-to-day expenses and the cost of reaching traditional milestones. Buying a first home is a good example of this. Rising property prices mean your children or grandchildren may be struggling to save a deposit or secure a mortgage. As a result, parents and grandparents are increasingly providing some form of gift to help young adults step onto the property ladder.

Half of first-time buyers under the age of 35 receive some financial support from family, according to Legal & General research. A gift to purchase a home can provide long-term financial security and improve wellbeing.

As well as buying a home, you may want to provide a gift to help with things like education costs, day-to-day expenses, or even paying for a once in a lifetime experience. A gift during your lifetime could do more to help loved ones achieve financial security than an inheritance later in life.

A gift also has the benefit of allowing you to see the advantages and security your wealth offers. Gifting can be an attractive way to pass on wealth, but, as with leaving an inheritance, there are some things you need to consider carefully first.

If you're not sure whether an inheritance or gifting is right for you, read on to find out more.

## Leaving an inheritance

Leaving an inheritance is the traditional way to pass on wealth. It can provide your loved ones with a lump sum when you pass away that could be used to help them reach goals later in life.

However, just because it's traditional, this doesn't mean there aren't things you need to think about. If you plan to leave an inheritance, here are three things to consider.

### 1. What wealth will you leave behind?

One of the challenges of understanding how to pass on wealth is calculating what your assets will be. You may have an idea of their value now, but how will that change over time? Some assets may increase, such as your investment portfolio or property, while others may fall, like your pension if you're drawing an income from it.

With so many different factors to consider, it can be difficult to have confidence in what the value of your estate will be. In turn, this can mean you're not sure how you want to distribute your assets.

Financial planning can not only help you understand the value of your assets now but how they'll change in the future. Based on your goals, lifestyle, and some assumptions, such as how investments may perform, we can forecast your wealth. This means you're in a position to make decisions about inheritances. Please contact us if you'd like to discuss how the value of your assets could change.



## 2. Does your will reflect your wishes?

The only way to ensure your wishes are carried out when you pass away is to write a will.

Without one, your assets will be distributed according to intestacy rules. This could be very different from your wishes. As a result, writing a will is something everyone should do. You can use a will to name beneficiaries, including family members, friends, or charities.

A will can also help speed up the probate process as there are less likely to be disputes if your wishes are clear.

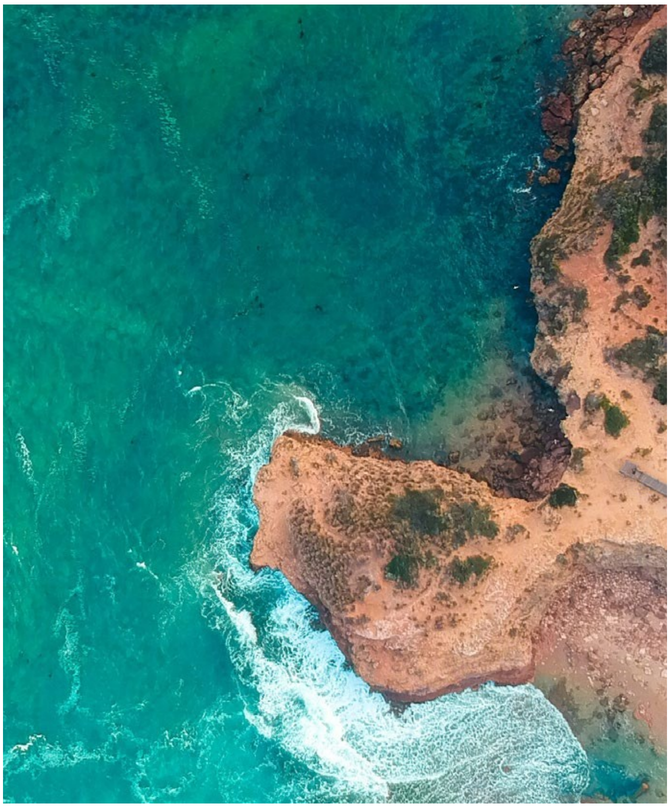
You can write and register your own will. However, it's often advisable that you seek legal advice. This can remove mistakes and help you understand how to split your estate in a way that suits your goals.

To make sure your will is legally valid, you must:

- Be 18 or over
- Make it voluntarily
- Be sound of mind
- Make it out in writing
- Sign it in the presence of two witnesses, who must be over 18
- Have it signed by your two witnesses in your presence.

It is possible to witness the signing of a will remotely, such as via video conference. If your will is not legally valid, the instructions may not be followed.

Once you've written a will, don't forget about it. Your wishes and circumstances may change over time, so you should review your will regularly and make updates where necessary.



**Updating your will**

If you need to make changes to your will, you have two options:

1. Amend your will**.** A codicil is an official alteration to a will. Codicils must be witnessed and signed in the same way as a will. There is no limit on how many codicils you can add to a will. However, to minimise confusion, they should be used for minor changes only.
2. Make a new will. For major changes to your will, you should write a new one. This should state that it revokes all previous wills and codicils, and you should destroy copies of your old will.

### 3. Do you need to consider the impact of Inheritance Tax?

If your estate could be liable for Inheritance Tax (IHT), being proactive can minimise the bill your loved ones will face. Taking some time to understand if your estate may be liable for IHT could mean you're able to pass on more wealth to loved ones.

For the 2021/22 tax year, the nil-rate band threshold is £325,000. If the entire value of your estate is below this figure, no IHT will be due. If you're passing on your main home to children or grandchildren, you can also make use of the residence nil-rate band, which is £175,000 for 2021/22. For most people, this means they can pass on £500,000 without having to worry about IHT.

If you're married or in a civil partnership, you can pass on any unused allowance from the nil-rate band and residence nil-rate band to your partner. So, as a couple, you can pass on up to £1 million without IHT being due.

The standard rate of IHT is 40%, so if you exceed the thresholds, it can drastically reduce the amount you leave behind. There are often things you can do to reduce, or even eliminate, an IHT bill but these steps must be taken while you're still alive.

**What is your estate?**

Your estate includes all your assets. This may include your savings, property, and material goods.

Remember to consider how the value of your estate will change. You may not be liable to IHT now, but could rising property prices push you over the threshold?

Among the steps you can take to reduce IHT are:

1. **Writing a will:** Writing a will is the only way to make sure your wishes are carried out. It can also be used to reduce an IHT bill. For instance, leaving your home to your children means you're able to make use of the residence nil-rate band.
2. **Reducing the value of your estate by spending:** Spending more of your wealth to bring the value of your estate under the IHT thresholds can eliminate the bill while helping you reach your lifestyle goals.
3. **Making gifts to loved ones during your lifetime:** Giving away some of your wealth during your lifetime can reduce an IHT bill. However, keep in mind some gifts will still be considered when calculating IHT; find out more in the gifting section of this guide.
4. **Using a trust to remove assets from your estate:** A trust can be a useful way to remove assets from your estate to pass on to loved ones. In some cases, you can still benefit from the assets while they're in a trust, such as receiving an income from investments. Trusts can be complex, and you should take financial and legal advice.
5. **Leaving at least 10% of your estate to charity:** This will reduce the rate of IHT from 40% to 36%, while also supporting a good cause.

There may be other things you can do too. If you'd like to discuss how you can minimise IHT, please contact us.

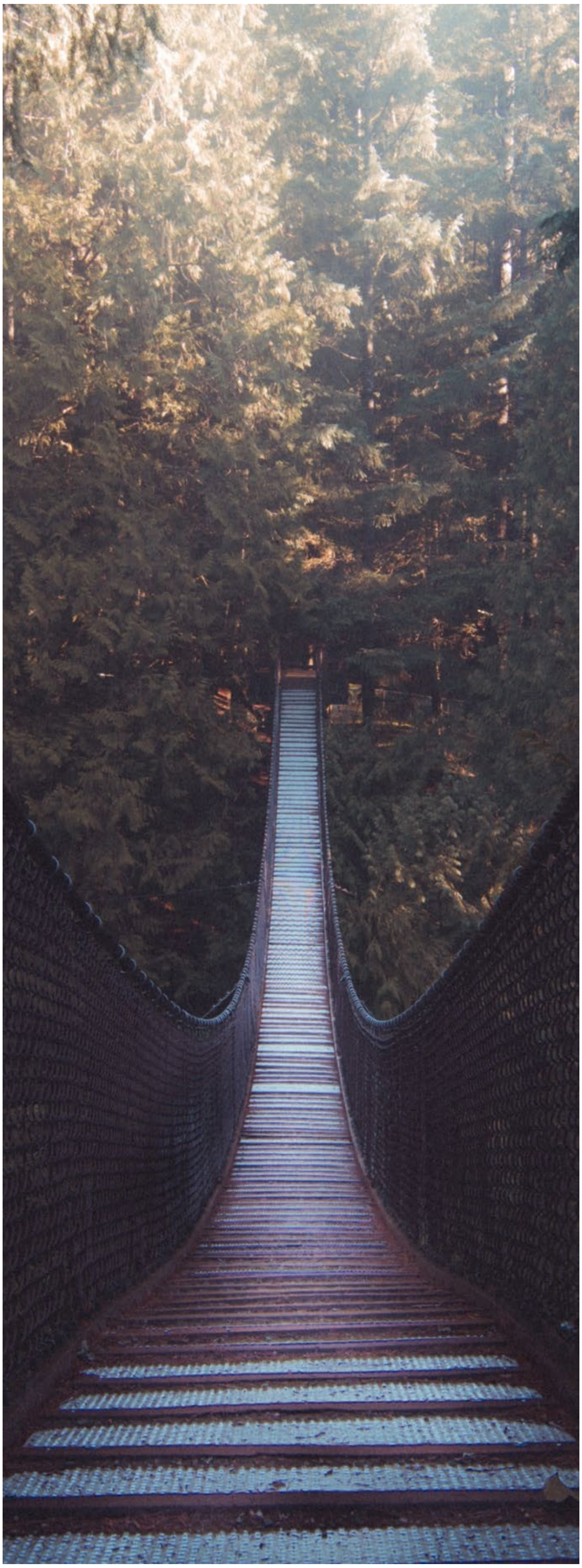
## Your pension and Inheritance Tax

Your pension may be one of your largest assets, but they are usually exempt from IHT charges.

If you have a defined contribution pension and die before age 75, your beneficiary may be able to take a lump sum without facing any tax. After the age of 75, or if they prefer to take a flexible income, the withdrawals may be liable for Income Tax depending on individual circumstances.

So, if you have other assets you can use to create an income in retirement, leaving your pension untouched can make financial sense.

You should also note that your pension is not covered in your will. Instead, you must complete an expression of wishes with your pension provider. If you have more than one pension, you should do this for each scheme.



## Providing financial gifts

Increasingly, parents and grandparents are providing financial gifts to family members and friends during their lifetime. It can be an attractive option, but you also need to consider the long-term impacts. Here are three questions to answer if you plan to pass on wealth through gifts.

### 1. Could gifting affect your financial security?

One of the most important things to do before gifting is to understand how it could affect your financial security.

Would taking a lump sum out of your estate now mean you're unable to meet goals later in life? Assessing the short- and long-term impact of giving gifts means you can have confidence in the decisions you make.

It's also important to note that the unexpected can happen. Often in retirement, spending decreases. However, if you were to need some form of care, your expenses can rise rapidly. After gifting, would you still have a financial buffer to ensure you had access to the care and facilities you needed? We can help you understand the impact gifts could have.

### 2. When will you provide gifts?

If you plan to provide gifts to loved ones, it's also worth setting out when you intend to do this and your reasons behind it. Do you want to provide a regular financial gift? Or a one-off gift under certain circumstances, such as when your child is buying a home?

Setting this out can not only help you include gifts in your financial plan, but means you can talk to loved ones about the financial support you'd like to offer. Your plans may influence the decisions they make and could provide peace of mind.

Understanding the value of gifts and when you'd like to give them can also ensure your wishes are carried out. You may, for instance, hope to provide a house deposit for each of your children, but they may be ready to purchase property at very different times. As a result, you may need to update your will to reflect this.



### 3. Could the gifts still be considered part of your estate for Inheritance Tax purposes?

Gifting during your lifetime can be a useful way to reduce the value of your estate so that it falls under IHT thresholds. However, not all gifts are considered outside of your estate immediately for IHT purposes. In some cases, gifts may be included in your estate for up to seven years.

These gifts are known as "potentially exempt transfers", which means they will only be outside of your estate once seven years have passed. If you die within seven years of gifting, they may still be considered when calculating IHT. The amount of IHT paid on these gifts reduces over the seven years but it could still leave your loved ones with an unexpected IHT bill.

It's important to consider this when thinking about making gifts during your lifetime, as well as your potential IHT liability. If your estate exceeds IHT thresholds, there are some gifts that you can make that are considered immediately outside of your estate. These include gifts:

- Up to £3,000 each tax year, known as your "annual exemption"
- Up to £250 per person each tax year
- Up to £1,000 as a wedding or civil ceremony gift, rising to £2,500 for grandchildren and £5,000 for children
- Made from your income that do not affect your standard of living
- To help with someone's living costs, such as children or an elderly relative.

**Inheritance Tax taper relief**

If you provide a gift and pass away within seven years, the amount of IHT due on the gifts will depend on the time that has passed:

Less than 3 years: 40%

3 to 4 years: 32%

4 to 5 years: 24%

5 to 6 years: 16%

6 to 7 years: 8%

7 or more: 0%

These gifting rules can be complex, and you should keep a record of the gifts you make. If you'd like to discuss how you can use gifts to reduce IHT, please contact us.



## Gifting and leaving an inheritance

For many people, passing on wealth won't mean choosing between gifts and an inheritance; a hybrid approach will suit some.

You don't have to decide between the two options, but it is important that your wishes are included in your financial plan. This can ensure you remain financially secure throughout your life and that your wishes are carried out when you pass away. It can be difficult to plan how your assets will be distributed, but it's a step that can give you confidence in the future and provide security for those who are most important to you.

Whatever you decide to do, you should also think about discussing your decision with your beneficiaries.

This can help them put a long-term financial plan in place that provides financial security and avoids misunderstandings.

Previous research suggests many are overestimating how much money they'll receive through inheritance. 2019 figures published in Money Age show, on average, UK adults are expecting to receive a windfall of £132,000 from their parents. In reality, the average figure passed down is £50,000. The gap could leave some people with an unexpected shortfall.

Financial planning can help you and your family understand how wealth will be passed on, and how to make the most of it.



## Which option is right for you?

There's no one-size-fits-all approach to passing on wealth. You should first consider what your wishes and goals are, as well as the situation of your loved ones. Understanding the impact you want your wealth to have can help you make the right decision for you.

If you'd like to discuss your options and put a plan in place, please contact us:

0113 224 2800

info@truewm.com

**Please note:** This guide is for general information only and does not constitute advice. The information is aimed at retail clients only.

The Financial Conduct Authority (FCA) does not regulate estate planning, tax planning, or will writing.

A pension is a long-term investment. The fund value may fluctuate and can go down, which would have an impact on the level of pension benefits available. Your pension income could also be affected by the interest rates at the time you take your benefits.

The tax implications of pension withdrawals will be based on your individual circumstances, tax legislation and regulation, which are subject to change in the future.