Chartered Financial Planners

BreedElliott

happiness through sensitive financial planning

Newsletter: May 2021

Intergenerational wealth transfer – Part II

Last month, we considered how we might motivate the Smith family grandparents to look to transfer some of their wealth to their own children and grandchildren during their lifetimes, rather than waiting for the funds to be passed down the generations when they die.

As financial planners, we feel that we can add value in two key ways:

1. Grandparents will undoubtedly be reticent about transferring wealth if they think there is any chance that they might need this wealth themselves during their lifetimes.

   We aim to help our clients to think deeply about their future lifetime ambitions and to conduct a thorough analysis of what their future income and capital needs might be. Only once this exercise has been completed can the grandparents start to feel comfortable that they can afford to transfer (effectively, give away) some of their wealth.

2. There is a strong chance that grandparents will also feel uncomfortable transferring wealth because they may worry about having little or no control of the money and may be concerned that family members may squander it.

   In this situation, we would suggest to the grandparents that they involve children and grandchildren in their financial planning. In this way, rather than future generations simply receiving an inheritance, with little or no idea about the thinking behind the gift, they will be actively involved with and be able to understand the grandparents wishes.

In this newsletter, assuming that we have been successful in motivating the grandparents to embark on an intergenerational wealth transfer strategy, we consider how wealth transferred might be best used by the next generations.

The Smith family grandchildren's objectives

For 20 to 30 year-olds, the common reasons for saving might include: accumulating a rainy-day fund; paying off a credit card or repaying a student loan; saving for a holiday or a new car; saving for a deposit on a first home.

As the grandchildren grow older, their savings objectives may become focused more on the longer term, such as saving for their own children, saving for their retirement and saving for paying off a mortgage.

The Smith family parents' objectives

If any of the second generation of the Smith family have already retired, we can realistically assume that they are financially independent and, therefore, may not need to inherit. However, they are likely to have strong views about their parents transferring wealth to their children.

Assuming that the Smith family's parents' generation is aged over 50 but not yet retired, they are likely to still be accumulating wealth with a focus on attaining financial independence. Their ongoing savings objectives might include: continuing to accumulate a retirement fund, including building their pension fund; saving to pay off their mortgage; saving to support their young adult children.

Coordinating the Smith family's objectives

The grandparents are likely to have opinions and views as to which of these various savings objectives they feel happy to contribute towards. For example, they may feel very comfortable helping with a deposit on a new home but not so comfortable in helping to repay a credit card liability.

In order to make an intergenerational transfer of wealth work for all, it would seem sensible to communicate between the generations to determine a strategy where both donor and donee feel comfortable with the outcome.

Possible solutions

On the assumption that we are successful in encouraging the three generations of the Smith family to formulate a wealth transfer strategy, let us now consider how any gifts made by a grandparent (the donor) to the parents or the grandchildren (the donees) might be managed.

- For objectives where money is required by the donee immediately, e.g. repaying a credit card liability, the solution would be simple: an outright gift from the donor.

- For objectives where money is likely to be required in the relatively short-term, e.g. where a grandchild is saving up for a deposit on a first home, the donee is unlikely to want to expose the gift from the donor to any form of risk. Therefore, they may look to buy Premium Bonds or to deposit the gift into a cash ISA.

- For objectives where money is unlikely to be needed in the short term but where it would be useful to have a fund in the medium to long term, e.g. to repay a mortgage, the donor may suggest to the donee that they invest any gift into a stocks and shares ISA. The degree of investment risk within the ISA could be determined based on the donee's risk profile.

- For longer term objectives, such as accumulating a retirement fund, which is likely to provide for the donee for the remainder of their lifetime, a natural solution would be to invest any gift received into a pension plan. The added benefit to this solution would be that the gift into the pension plan would be eligible for tax relief, thereby elevating the value of the gift.

Trust and trusts

Clearly, all of these solutions are dependent upon a degree of trust between the donors and the donees. It would be fairly straightforward, in most situations, for a donee to ignore the donor's wishes and, potentially, to squander the gift. However, the risks of this happening are mitigated to a large degree by the whole family being actively involved in formulating the plan.

If keeping control of any wealth transfers is an important consideration for the grandparents, they could choose to settle any gift into a trust, where the trustees would have control on any distributions and the timing of those distributions from the trust fund. However, this can become complicated and involve additional costs.

Also, for families where the grandchildren or great-grandchildren are minors, the grandparents would have the ability to make gifts into investments such as Junior ISAs, where the child's parents would have control of the funds until the child reached age 18.

The next steps

The idea of intergenerational wealth planning has been embraced by extremely high net worth families for many years. In a way, they were forced to in order to ensure that key assets remained within the family.

However, with the enormous levels of wealth due to be passed down the generations over the next two or three decades, it makes sense for more than just the extremely high net worth families to think seriously about formulating an intergenerational wealth transfer plan.

If you think this could be a sensible idea for your family to explore, please do not hesitate to contact us and we will also raise the subject with you at our next review meeting.

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Market data

Market	Value at start of 2020	Current situation	Comments
Interest Rates (BOE base rate)	0.75%	0.1% at 30/04/21	The official bank rate is 0.1%.
House Prices (Nationwide)	House prices increased by 7.3% in 2020	House prices up by 2.1% in the month to 30/04/21	Annual house price growth 7.1%.
UK Share Prices (FTSE 100)	7542.40	6969.81 at the close on 30/04/21	The FTSE 100 rose by 242.31 points in April.