ESTATE PLANNING

Leaving an Inheritance?
Is It Better to Give to Kids Now or Later?

Retirees should secure themselves first, and if you're all set there, then consider a few other things, such as the impact on the kids and tax issues.

(Image credit: Getty Images)

Flying off on a recent family vacation, I was sitting next to my 4-year-old and had my 8-month-old on my lap. Thank goodness it was a short flight! Before takeoff, as always, the flight attendant told us, "In the event of emergency, secure your own oxygen mask before helping your kids." It's a statement that we have become almost numb to, but my guess is, it would be hard to follow through on. When it comes to giving your kids their inheritance now or after you die, my advice is the same as the flight attendant's: Make sure you secure yourself first. That is: Do you have enough money that you can afford to give it to your kids or anyone else?

The biggest unknown in this projection is undoubtedly long-term-care expenses. Most certified financial planners with a decent piece of software or calculator can answer this for you. Assuming you check this box, and there is enough to go around, consider the impact on your kids.

Will Giving an Inheritance Early Have a Positive Impact?

Money can be a rope or quicksand depending on the amount and the recipient. Think about what your kids have done in the past when they have received more money than they are used to. Did they use it to cover expenses? Did they invest it? Did they show up at the next family gathering in a nicer car? If your money went toward a flashy vehicle, you may want to reconsider.

In all seriousness, the beneficiary of the funds often matters more than the amount or vehicle for the gift. This is one reason revocable trusts are such a popular estate planning tool. They allow you to control how and when the beneficiary spends their new money.

Consider the Kid's Age at the Time of the Gift

Let's say you're 65 years old and you had twins at the age of 30. Your life expectancy is about 85. So, you are essentially deciding whether you should give money to your kids in the next 20 years, or in 20 years. In 20 years, your Millennial kids will be 55 and likely in their peak earnings years. Their kids will be graduating from college. They will be entering the period where the gap between their earnings and expenses is largest. Said differently, they don't need the money then.

On the opposite end of the spectrum, when expenses may actually be larger than expenses, is the period when the kids are young. Childcare expenses paired with the possibility of only one working spouse means this may be the period of greatest financial need.

What About Taxes?

While your kids may benefit from your funds most during this period, it may not be the optimal time to give from a tax perspective. Due to the large gift tax exemption, I would not worry about the gift tax when giving, unless your estate is larger than about $12 million. You should, however, consider capital gains and income taxes.

Sometimes we recommend giving stock to kids when they are in school and have very little income. That's because there is a tax arbitrage opportunity. If you sell the stock, you're likely to pay 15% in capital gains taxes. If someone in the lowest two income tax brackets sells the stock, there is no tax.

I know, I know, I haven't gotten to the negative part. If you leave a stock at death in a non-retirement account, there is a "step-up" in basis. That means your child won't have to pay any taxes on the gains accumulated during your lifetime. So, if you're one of the lucky (maybe smart) ones who bought Apple stock in the '90s, it's probably best to leave those funds at death.

This step-up in basis applies to all capital assets, including real estate. It can be a powerful way to avoid large tax bills on investment properties and your home.

So, capacity to give has to come first. A serious talk about the impact is next. Then, put together an efficient plan to execute your wishes.

NYSUT NOTE: The ins and outs of estate planning – like leaving an inheritance – can be complicated. Which is why working with a professional is crucial. And as a NYSUT member, you have access to the NYSUT Member Benefits Trust-endorsed Legal Service Plan. Provided by the law firm of Feldman, Kramer & Monaco, P.C., this plan offers NYSUT members, their spouses and even retirees access to a national network of attorneys that deal with numerous personal legal matters. Learn more about the features of this plan or enroll by visiting the website today.

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