



Teachers Financial Planning

Windfalls: Making the most of the unexpected

This article looks at the common kinds of windfalls that people receive, their tax treatment and strategies for utilising them.



Personal Planning UPDATE

When it comes to money and effectively utilising finances to achieve your goals, the starting point is always a solid and well thought out plan. A good plan can't, however, guard a household or a business against every possible occurrence.

Just as sometimes external market forces or some previously unseen internal dynamic can rear up and lay waste to the best laid plans, sometimes a windfall can seemingly drop from the sky and open up a whole new range of possibilities.

As tempting as it is to blow your whole windfall on the holiday of a lifetime, financial opportunities of this nature don't come around very often. While often unexpected, a windfall is a chance to take a leap towards your goals.

The most common types of windfall that people receive are:

- inheritance
- bonuses
- tax rebates

- selling assets or shares
- lottery, competition or gambling winnings.

There's no rush

It is important to take your time and not rush into anything. A windfall does not inherently change your priorities or your financial obligations. History is littered with examples of people who let the irrational exuberance of a sudden influx of money cloud their judgement.

The first step is deciding where to put the money while you consider what you are going to do with it. Do you want to open a separate savings account for the windfall so that you can benefit from interest while you make your decision? Some accounts and ISAs give better rates if you are willing to lock your money away for a number of years.

It is also always wise to keep a portion of your windfall ticking over in an easy access savings account in case of emergencies.

Contact us today to talk
about your savings strategy.



Windfalls and tax

Bonuses

While an employer providing bonuses has a range of reporting and tax obligations to fulfil, the person receiving the bonus should have their PAYE and national insurance deducted by the time they get the money. This is because the bonus is considered to be income.

Christmas bonuses are slightly different, and are exempt if the person is given goods that can't be resold for cash and they earn less than £8,500 a year. Otherwise they are also treated as income.

Inheritance

Like bonuses, any inheritance tax (IHT) on your payment should have been deducted by the time it gets to you. However, you may need to pay income tax if your inheritance generates an income and you could be liable for capital gains tax (CGT) as well if you dispose of the inherited asset and it has increased in value since the person died.



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Capital gains

CGT is charged on the profit made from the disposal of most types of asset, so if your windfall has come from selling something for a profit you are going to be liable. The difference between what you paid for the asset and how much you sold it for (the 'gain') is what is liable for tax (though there is an annual exemption to reduce potential CGT liability).

For certain kinds of windfall gains there is a windfall gains tax rate that applies, although this pertains to certain kinds of development land sold between a certain period. We will be able to show you if this applies to you.

Lottery and gambling wins

Lottery and gambling winnings are not considered to be income and are therefore not taxed. It is how you use the money that will then make you liable, such as giving gifts or making capital gains.

Talk to one of our team about your tax obligations today.



Windfall strategies

Now that you have figured out where you stand in relation to tax, you can get down to the serious business of figuring out what to do with your money.

The options open to you are potentially endless, the only constraints being the size of the windfall itself and the law. Here are some of the more popular choices.

Save it for the future

There are always going to be big purchases and ongoing financial obligations coming over the horizon, so why not keep some of your windfall tucked up in a high interest account or an ISA until such an occasion arrives?

If you have children who will be going to university, you could save them having to take on a significant debt. Or if you have elderly dependents who are likely to need ongoing care later in their life, you could help them financially. Of course, you could leave the money until you retire and use it as a tax-free boost to your income.

Gifts

If you want to share the windfall around, you can arrange to give it away to individuals or organisations as gifts. There are no direct taxes on gifts and a person can make tax-free gifts of up to £3,000 in each financial year. On top of this, up to £3,000 is available tax-free if they have not used up last year's allowance.

While gifts themselves are not taxed, they could eventually be liable for IHT if the gift giver dies within 7 years of giving the gift and their estate exceeds the IHT exemption threshold. In this instance the value of the gifts will be added to the estate.

Debts

Another important action to consider is using the windfall to pay down your debts. Mortgages are usually the big focus here. If clearing your debt will provide a boost in your regular income then this can be seen as a great long-term strategy.

Investing

A popular choice for people who receive windfalls is to invest the money. Investing in property is an option that many people with large windfalls consider because by renting or renovating it and then selling it on, property can be a long-term productive asset. Becoming a landlord is a financial and managerial commitment and anyone who invests will need to keep actively involved.

Alternatively, a person can invest in stocks and shares, although again this is a big commitment and one that carries a number of potential risks. The old advice of spread your risk, invest in the long-term and stay calm in the face of market fluctuations remain relevant because many people tend to forget them.

Whatever you decide to do with your windfall, we can help you make sure that you do it in a way that works for you. Life is all about making results out of the opportunities that you are presented with and our expert team has a lot of experience in helping families and businesses use their finances to achieve their goals.

Important Notice

The way in which tax charges (or tax relief, as appropriate) are applied depends upon individual circumstances and may be subject to change in the future. ISA eligibility depends on personal circumstances.

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