

## TIPS ON LENDING MONEY TO FAMILY AND FRIENDS



Money is an emotionally charged issue that has torn apart many a relationship. Family Foundations offers the following suggestions when deciding whether to lend or not to lend to a loved one:

- **Just like in Vegas, don't risk more than you can afford to lose.** Loaning money to friends or family is a gamble, so never make a loan if it's going to put your own financial situation on the skids. However well-meaning the individual is, none of us knows what tomorrow holds. Only loan the money if you're comfortable with the idea that you'll never see it again.
- **Do not dip into your retirement account.** Loaning money is not a good idea if it means that you have to risk your retirement savings. Protect this nest-egg as though you were the mother hen, and don't let any of your chickens touch it.
- **Involve your spouse/partner in the decision.** Communication could not only save you money, but could save your marriage or relationship. If you and your spouse don't agree on making the loan, it could result in significant stress on your relationship.
- **Evaluate the impact the loan will have on other family members.** If you loan money to one child, you're setting a precedent. What if other children are not as responsible, thus the risk of them repaying a loan is greater? Be prepared to deal with the potential strife such a situation could create within the family.
- **Consider the reason the borrower needs the money.** Do they want the loan because of an emergency like loss of job or unexpected medical bills, or because they made poor spending decisions? Will it be used for something that will improve their life, like a down payment on a home or education?
- **Don't be an enabler.** If the borrower is engaged in a destructive lifestyle, and is habitually in financial hot water, be emotionally supportive rather than financially supportive. A better use of your money would be to pay for professional counseling to get to the root of the problem, as bailing them out of their current crisis won't address the underlying issues.
- **Treat the loan as a business arrangement.** After all, you've now become the banker, and bankers take things seriously. Once you have agreed on the amount of the loan, discuss the interest rate, term, payment due date, and late fees. To figure out monthly payments, including interest, consider using a loan calculator, such as the one available at [www.bankrate.com](http://www.bankrate.com).

- **Put all the terms of the loan in writing.** Many Web sites offer free promissory note forms. One such site is Internet Legal Research Group at [www.ilrg.com/forms/promisry.html](http://www.ilrg.com/forms/promisry.html), where you can find promissory note forms for each state. Consider having the documents notarized, as this will give you more legal standing if the borrower defaults. While putting it in writing is smart because it makes the borrower more accountable, be aware that it won't guarantee you will be repaid. It's simply another layer of protection.
- **Be forthcoming about any legal steps you will take to collect an unpaid loan.** Jointly reviewing a worst-case scenario in advance of the situation can go a long way to preserve a relationship if things start going south.
- **Divorce yourself from making judgments on the borrower's spending decisions.** When someone owes you money, it's difficult not to watch how they spend their money, particularly if they're behind on payments to you. Fixating on their frivolous spending can drive a wedge between the two of you. Inquiring about their plans to get back on track with payments is justified, but resist the urge to grill them over where the money has gone.
- **Think long and hard before agreeing to co-sign a loan.** When you co-sign a loan, you are agreeing to repay the loan even if the lender defaults. And, you may not be notified until the loan is several months delinquent. Such a delinquency will negatively affect your credit rating, as well as that of the primary borrower.
- **Consider requiring collateral for large loans.** If you are lending money for a car, insist that you be listed as the lien holder on the title. If the loan is for the down-payment on a house, have the loan drawn up with you listed as the second mortgage holder. If the borrower defaults, any equity remaining after the primary lender is repaid will go toward paying off your loan. If you are going to require collateral, it is wise to have the loan handled by an attorney.
- **Check on possible tax consequences.** The IRS frowns on loans that charge little or no interest and may require you to pay a gift tax. Before loaning more than \$10,000, talk to your tax accountant to ensure you are protected. If the borrower defaults on the loan, document your attempts at collection so you can write-off the loan.
- **Consider what will happen if you die before the loan is paid back.** In your agreement, include a statement covering such circumstances. Will the loan be forgiven, or will it still be owed to the estate? Do the same repayment terms remain in place? If it is owed to the estate and the borrower is an adult child, will the amount be subtracted from your child's share of the inheritance?

**Family Foundations** stands ready to help. To reach us, call (904) 396-4846 or go online to [www.familyfoundations.org](http://www.familyfoundations.org).

#### **About Family Foundations**

You don't have to solve your financial problems alone. Family Foundations has

trained and certified credit counselors who offer financial management and debt reduction services. Family Foundations is a nonprofit, community-based organization and a Member of the National Foundations for Credit Counseling (NFCC). For more information on Family Foundations, call (904) 396-4846 or visit [www.familyfoundations.org](http://www.familyfoundations.org).