



Loans to family members; should I put it in writing?

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Date: Tuesday June 9, 2020

There are a lot of reasons why you might enter into a loan arrangement with a family member. Parents loan money to their children, grandparents to their grandchildren and even siblings to siblings. If the loan arrangement is documented appropriately, then this arrangement can be of great benefit to all parties involved. Likewise, if you don't put family loans in writing, there can be dire consequences.

There seems to be a false sense of security that nothing can go wrong with a loan arrangement with a family member and it is viewed with rose coloured glasses. No one thinks it will end badly.

But we see the other side of it. When loan arrangements have not been documented properly, it can lead to disagreements and falling outs between family members.

When there is a loan arrangement between family members, there is even more reason to document it thoroughly and properly. Dealing with it at the outset when everyone is on good terms is much easier (and less costly) than trying to fix the problem later down the track.

How do I document a loan to a family member?

The type of document required to deal with family loans will depend on what lengths you want to go to in order to protect the money and ensure it is repaid under the terms you all initially agreed to.

Documenting a family loan in a written agreement and having all lenders and borrowers sign the agreement, is an important step.

However, there is an array of circumstances that may mean that your loan needs to be documented in a more formal way to ensure your protection – especially if the loan document is challenged.

Can a family loan document be challenged?

A loan document may be challenged.

The most common circumstances where a loan document may be challenged are the following:

1. If the borrower was made bankrupt and you are one of the creditors expecting to have your loan repaid;
2. The borrower's relationship with their partner breaks down and you would [like your loan repaid as part of the property settlement](#) ;
3. The borrower predeceases you and you expect the loan to be [repaid from their estate before their estate is distributed](#);
4. The loan is not enforceable due to the statute of limitations and your time to enforce the loan against the borrower has run out.

What do I need to include in the family loan document to protect my money?

This will always depend on your individual circumstances, the reason for the loan and your expectations for repayment.

It is important that the document be properly drawn and accurate, so [we suggest you engage a lawyer to assist with this](#). The borrower should also consider getting their own independent legal advice regarding the loan.

The most common inclusions in a loan deed

- Background and intention of the loan;
- The amount of the loan;
- Are there interest payments?
- Are there regular loan repayments?
- The period of the loan;
- If there is to be security for the loan, such as a mortgage or caveat registered onto the title of the borrower's property;
- When the loan must be repaid;
- The parties to the loan – should it include the borrower's partner?

Sometimes more detailed clauses are required to protect the lender

Depending on the circumstances and your need for repayment (especially if the loan document is challenged), the loan document may need to be more detailed.

It may need to look more like a loan that is on terms you would see from a commercial lender. Some of the common inclusions in a loan deed (as detailed above) may no longer be optional if you want to ensure you are protected if challenged.

For example, quite often family members do not wish to charge the borrower interest or require regular repayments of capital. But to prove that your loan is a genuine commitment and must be repaid if challenged, you may need the loan document to require interest payments and regular repayments.

The conduct of the lender and the borrower is also important. If the loan document calls for interest payments and regular repayments, then the parties to the loan will need to prove that those payments have actually been made.

If you want to ensure your loan is repaid if the loan document is challenged, then [we suggest seeking legal advice to draw up a loan document](#).

Also, it's worth ensuring you understand specifically [how to protect your loan if the borrower goes through a divorce](#).

Are there any other considerations I should have to reduce my risk?

1. We suggest seeking advice from an accountant. There are income tax considerations for you as lenders in relation to when interest payments are due and are made.

2. [We suggest looking at your Will](#) as giving money to a family member may affect the intended distribution of your assets.

- Is the loan to be forgiven on your death?
- Have you gifted money to one child but not to another and this needs to be evened up when your estate is divided between your children?

1. Advice from a financial advisor should be sought before entering into any family loan agreement, to ensure you can afford to provide the borrower with money, especially if in a worst-case scenario that money is never repaid by the borrower.

2. We suggest you look into insurance policies if you intend to be repaid the money.

- What if the borrower dies and they did not have the assets to repay the loan?
- Should you have a life insurance policy on the borrower's life for the amount of the loan so you can ensure you are repaid if the borrower dies?
- What if the borrower loses their job or is unable to work due to injury or illness and cannot make repayments?
- Should you have insurance in place to cover your repayments in this instance?

1. Are you entering into a loan with a family member for the right reasons?

- For example, a lot of parents are tempted to loan funds to their child as the interest repayments from their child are more than what they would receive from a bank if the funds were in a term deposit.
- There are certain considerations to have in respect of a loan for this purpose.

How can E&A Lawyers assist?

Family loans and loan agreements is a complex and ever-changing area of law. We are always willing to assist to ensure your money is protected and you understand the risks associated with providing money to family members.

E&A Lawyers is a team with lawyers specialising in different areas – this is certainly a topic that can cross over some different areas of law.

[Our estate & trusts lawyers](#) can assist you with advising on loan agreements, ensuring you consider your Wills in the context of the loan and ensuring you understand how the loan may be treated on your death.

[Our family lawyers](#) can assist you with understanding the implications of a loan if the borrower has a relationship breakdown.

[Our property lawyers](#) can assist you with creating security for the loan, such as registering a caveat or a mortgage on the title of the borrower's property.

Get help from a family lawyer

Contacting E&A Lawyers

For more information or to arrange a consultation with a lawyer, you can call or email us.

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