When Friends or Family Ask for Money

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How do you respond to a friend or relative who asks to borrow money or asks you to cosign a loan? Lending money is a business transaction with financial risks. Lending money to family and friends, in addition to being a business transaction, is a personal transaction and affects relationships that are very important to you. At its best, lending money to a friend or relative is a way to help someone you love. At its worst, lending money to a friend or relative destroys a meaningful relationship.

Before lending money to a friend or relative, consider the entire situation—your situation and the situation of the person asking for money. Will the money solve the problem of the person asking for help? How will giving financial assistance affect your present and future financial situation?

Is money the problem or the symptom?

When a person asks for a loan, he or she thinks money will solve his or her problem. And, sometimes it does. For example, when a person has had unexpected expenses or reductions in income, your loan helps that person through the temporary crisis. You may even prefer to make a gift rather than a loan.

However, money may not be the problem, but rather the symptom of the problem. Lack of money may be caused by chronically living beyond one’s means.

When spending continually exceeds income, the only solutions are to increase income or decrease expenses. Life changes are necessary to increase income and/or decrease expenses.

Money problems also may be caused by drug, alcohol, and/or gambling addictions. If the money problem is a symptom of one of these, your loan, rather than solving the problem, allows this person to continue to ignore or deny the real problem.

Some clues that money is a symptom of other problems are:

- The person has borrowed from you or other friends or family members before and not repaid as promised
- The person asking for money is vague as to why he or she needs the money
- The person doesn’t want you to tell other friends or family members he or she has asked for a loan.

Taxes on gifts

Gift taxes are not a concern for modest gifts. You may give up to $10,000 per person per year to as many people as you wish without paying federal gift taxes. This is called the annual gift tax exclusion. If you and your spouse make a joint gift, together you may give up to $20,000 per person per year with no federal gift tax. If you make gifts larger than the annual exclusion, you must file a gift tax return. You do not pay the tax; rather, you reduce your federal estate and gift tax credit.

Can you afford to make a loan?

Before lending money, look at your total financial situation. What large expenses will you have in the future? What changes might you experience in income?

Can you really afford this loan? Saying no may be difficult, but not saying no may be even more difficult.

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If you do make a loan, what are your expectations for when and how the loan will be repaid? Be clear about the expectations of both the lender and the borrower. Put expectations in writing. Be sure the loan document includes the amount of money you are lending; the interest rate, if any; the date by which the loan must be repaid; and a description of any collateral.

You may want to purchase a form called a "promissory note" at a stationery or business supply store. If there is collateral and/or if the loan is large, you may want an attorney to prepare or review the lending agreement to protect you in the event of nonrepayment and/or bankruptcy, divorce, or death of the borrower.

What if you cosign a loan?

Sometimes a friend or relative asks you to cosign a loan from a financial institution. A cosigner is required when the lender considers a loan "risky."

Being a cosigner affects your future ability to borrow. The loan is your "contingent liability" and the monthly payment is considered a monthly payment owed by you. This monthly payment, the contingent liability, is a factor when a lender evaluates your loan application and your ability to repay a loan.

If the borrower for whom you cosigned does not repay the loan, you—the cosigner—are legally responsible for the debt, late charges, fees, and even court costs and attorney fees. Before you agree to cosign, be sure you can afford to repay the loan.

If you are consideringcosigning a large loan, have your attorney review the lending agreement. There are protections for you that may be included. If you do cosign a loan, get and keep copies of all the papers signed by the borrower and you.

As cosigner, you have the right to information on payments and you will be notified if payments are not made.

It's your choice

When a friend or relative asks you for financial assistance, it's your choice. Think through the situation—both the financial and the emotional aspects. What will the loan do for your own and the borrower's financial situations? How will giving or not giving financial help make you feel about yourself and about your relationship with the person seeking help? How might making or not making the loan affect your relationship with other family members or close friends? Remember, it's your money and your choice.