

Should You Become “The Bank of Mom and Dad?”

Considering the current economic climate, there's a pretty good chance one of your adult kids may soon ask you for a loan—to pay off credit cards, put a down payment on a house or just to get by after a job layoff. It can be risky business to mix family and money. However, if you're considering it, keep these tips in mind.

Think about your future.

Can you afford to provide a loan at this point in your life? If your child doesn't pay it back, could it affect your ability to pay for potential nursing home care or medical costs down the line? “Remember, your adult child can go other places for a loan. But if you run short, you can't get a loan for retirement,” says financial planner Mike Flower of Financial Principles, LLC, in Fairfield, NJ. Don't loan more than you can afford to lose.

Get outside help.

If you're loaning a large amount of money—for a mortgage, for instance—or are including a lot of details in your agreement, Flower recommends seeking the help of an attorney. If you want help with tasks like tracking the loan, setting up automatic payments and sending payment reminders, companies like virginmoney.com provide those services for a small fee.

Consider gifting it.

An outright gift has fewer strings attached than a loan. You can give up to \$12,000 per person per year without reporting the gift to the Internal Revenue Service. If you give more than that, you'll need to report the amount, since it counts toward your gift tax and estate tax exemptions when you pass away.

Consider putting it in writing.

A simple loan agreement—one that details the loan amount, monthly due date, interest rate and any reasons for forgiving the loan—can save you a lot of grief later. “This document makes the agreement feel more businesslike,” says Flower. Getting your signatures notarized is smart, but not essential.

Update your will.

If you've got more than one child, Flower suggests adding a provision to your will regarding the loan. If the borrowing child hasn't paid off his loan at the time of your death, the outstanding loan amount should be forgiven and considered that child's first share of any family inheritance. “Even if the loan is only a few thousand dollars, it's only fair to your other children that the money be taken into consideration,” he says. Be sure to leave a copy of any loan agreements with your attorney and with your will.