Don’t risk missing
Your Ultimate Deadline®

Bank of Mum and Dad

SYDNEY ESTATE PLANNING LAWYERS

What is the bank of mum and dad?

Today it has been estimated that of loans made to help purchase a property in which the buyer will live, in over 50% of those loans, parents of the buyer will have contributed in some way to help make the purchase happen.

Those contributions are often called the “bank of mum and dad”.

It was not that long ago that the % was 15%.

The average contribution is said to be nearly $90,000.

How does the need for the bank of mum and dad arise?

The need for the bank of mum and dad arises normally because banks will not lend to first home buyers, even second and later home buyers, the level of finance that they require to buy the home that they want to buy, particularly in the Sydney market.

This happens because banks have loan to valuation ratios that they will not normally go beyond in making a loan.

So this means that relative to the market value of a property that is being purchased, banks will only lend up to a certain amount (called the loan to valuation ratio).

Can Sydney Business Lawyers help you with this “bank of mum and dad” need?

Sydney Business Lawyers unique position of advising families in business about the legal needs of their business and the key private client needs of property and death positions it perfectly to assist with the legal needs that are connected to “bank of mum and dad” situations.

What is the bank of mum and dad service offered by Sydney Business Lawyers?

Sydney Business Lawyers is able to assist you with all of the legal aspects that relate to the bank of mum and dad, which include:

- The property purchase transactions that are the subject of the bank lending and the conveyancing of those property purchases
- The bank lending documentation that is attached to the bank loans for the property purchase
- The loan or gift documentation to record the bank of mum and dad contribution that is made to help make the property purchase possible, whether or not there is also bank lending
- The estate planning provision that should be made by parents if they have given 1 or more of their children a helping hand through the bank of mum and dad and the parents want to square up the ledger between their children when they die if they have not already squared it up

The lawyers at Sydney Business Lawyers have over 50 collective years of legal experience helping families and their children purchase and sell property, meeting the bank’s requirements for lending related to it and dealing with the loan and/or gift and estate planning requirements that flow from it. So we are well placed to assist with all of the needs that relate to the bank of mum and dad.

As a result of the experience, we have also developed document packages to manage bank of mum and dad contributions and the legal requirements that arise from them.

The things that need to be managed in doing a loan from the Bank of Mum and Dad are set out below.

Unsecured loan agreement

A decision will need to be made about whether the loan is secured or unsecured (ie is there to be a mortgage or charge in place).

If it is unsecured, this means that if the borrower becomes insolvent, the lender has no security and has no protection for the purpose of recovering the loan. If that happens, the lender will line up with all of the other unsecured creditors including in the case of a bankruptcy, and normally, the lender will not get their money back. Certainly, they will not get back 100% of it.

It is also means that at no time can the lender force the sale of any assets of the borrower to be able to recover the loan amount and any unpaid interest.

Before agreeing to make an unsecured loan, the lender must satisfy themselves that they may never be able to recover the loan amount and any interest that is payable on the loan. If they are not, they should be seeking appropriate security or not making the loan.

Do you need a registered mortgage / charge?

You only need a registered mortgage / charge if:

- you are concerned about the borrower becoming insolvent; and/or
- you want a power of sale to sell the borrower's property to recover the loan.

If you only want to protect against the borrower's relationship breakdown, you don't need a registered mortgage.

In the case of relationship breakdown, it is enough that the loan agreement records:

- the fact of the loan; and
- that it is repayable in the case of the borrower's relationship breakdown.

However, please ensure you read the comments below about relationship breakdown.

No loan forgiveness

We do not normally make the loan forgivable on the death of the lender or the borrower.

The reason for this is that it is very important for the lender to ensure that the wills of the lender and the terms and conditions of their estate plan and any loans to their children will allow for the intended outcome.

If a loan is forgiven and there are not enough other assets to square up the ledger as required between all of the children of the lender, the forgiveness can inadvertently avoid the intention of the parents for what is to happen on their death.

Another reason not to forgive it is that the Family Court has the discretion not to take the loan into account in dividing the marital assets even though the loan is recognised as being enforceable as a loan. A loan forgiven on death may lend to the court exercising that discretion, as may an unsecured loan.

Lender's estate planning

If the borrower is 1 of multiple siblings and the lender is / lenders are the parents of the borrower, the lender should be satisfied that in making the loan to 1 sibling, if the loan cannot be recovered, that the parents have enough other assets with which to make the gifts that they want to make to achieve the outcome that they want to achieve on their death.

So it is most important that the lender's estate planning marries up to loans that they make to their children.

Assuming that the lenders have enough other assets to make it work, including in their will a legacy for equality clause can be a very effective way to square up the ledger for any loans made to 1 or more children and not to the others. However, if the loans are repayable, providing the borrowing child has the ability to repay the loan, it should not be an issue.

Repayment event - marriage / relationship breakdown

Most parents want to know that making an amount available to a child as a loan will be recoverable if the child's marriage or relationship comes to an end.

So long as the parents can prove the amount was a loan and not a gift, an unsecured loan agreement is all that is required.

That however is subject to the Family Court's discretion not to take the loan into account in dividing the marital assets even though the loan is recognised as being enforceable. A secured loan supports the argument that it was always intended for the loan to be repaid.

If the parents want to also protect the capital growth in the asset purchased using the loan, that is more difficult. On the assumption that an asset will double in value every 10 years, a 10% per annum simple interest rate will help to protect the capital growth of the property (relative to the value of the loan).

Parents often do not want to charge interest but having an interest provision that allows the lender to recover interest "if demanded" is a useful tool to protect the capital growth in the property that is being purchased with the loan.

Bank lending policy and loan vs gift

A potential problem with a Bank of Mum and Dad loan and the "if demanded" condition is that often the loan will be made so children can buy a home. Most banks require the amount being made available by Mum and Dan to be a gift, not a loan, so there is a conflict that often cannot be resolved. In that case, a decision will need to be made about whether the desire to get the bank loan is greater than the risk to be protected against.

However, subject to the bank's lending criteria and any statutory lending obligations, legally it is possible for the bank's loan and the Bank of Mum and Dad loan to co-exist and both be registered on the title of the property being purchased.

Loan lapsing - VERY IMPORTANT NOTE

It is most important to note the problem that exists if the loan becomes repayable but action is not taken to recover it.

If the loan becomes repayable but action is not taken to recover it within 6 years from the date it became repayable, the loan lapses unless the parties agree in writing before the end of that 6 years (and again at 6 yearly intervals) that it can be recovered. This is called refreshing the loan.

The loan can be refreshed by agreement in writing between the parties or the borrower making a principal or interest repayment within that time period.

We document the loan as a deed which means that the loan can instead be refreshed at 12 yearly intervals. The ability to extend the period is limited to a 30 year period in total.

Sydney Estate Planning Lawyers provides estate planning services.

The below flow chart sets out all of the required information to have an estate planning discussion.

So don't risk missing …

Your Ultimate Deadline®

Tax & risk

Risk Assessment (ICADI)

Spendthrift
select the trustee

Special needs (DAGS)
select the trustee

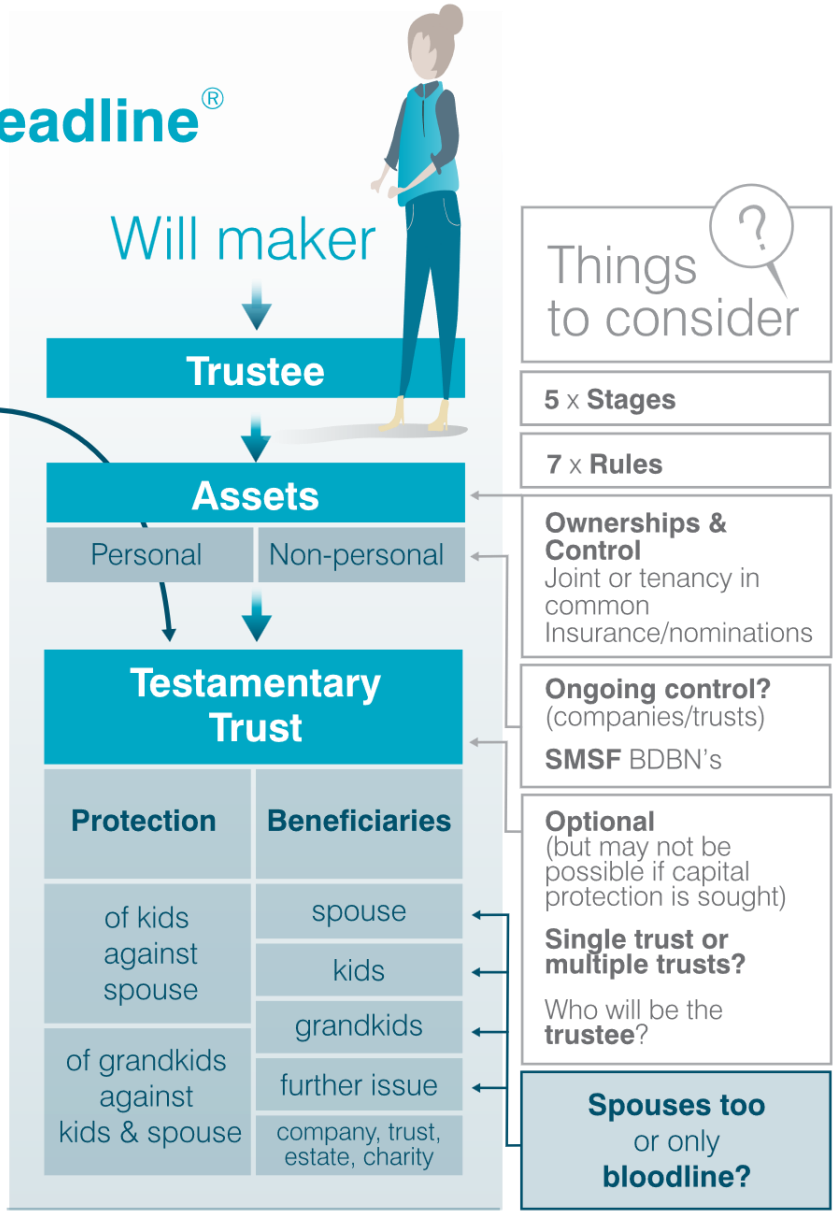
Special needs (Disability)
select the trustee & gift over

Betrayal
mutual wills
OR independent trustee
OR limited capital rights

Bankruptcy
trustee control

Divorce - Family law
BFA
OR independent trustee
OR limited capital rights
OR single trust

Death - A contested will
control
OR independent trustee
OR limited capital rights



Things to consider

5 x **Stages**

7 x **Rules**

Ownerships & Control
Joint or tenancy in common
Insurance/nominations

Ongoing control?
(companies/trusts)
SMSF BDBN's

Optional
(but may not be possible if capital protection is sought)
Single trust or multiple trusts?
Who will be the **trustee**?

Spouses too
or only
bloodline?

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