You are not a-loan: written agreements crucial in family financing

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Recent times have seen the rise in those seeking to get into the property market relying on the 'bank of mum and dad' for assistance to purchase a property. The increased reliance on the 'bank of mum and dad' has, unfortunately, also led to an increase in disputes involving family financing arrangements. These disputes often highlight the importance of clearly documenting agreements between parents and their children (or between family members or even friends) to prevent later uncertainty, family conflict and court intervention.

In this article, we highlight four case examples which demonstrate the difficulties that can arise when parents or other family members:

1. advance money;
2. guarantee loans; or
3. enter into informal arrangements with family members,

without a written agreement or without understanding the arrangements being entered into.

Property transfers

In *Donaghue v Donaghue* [2015] QSC 054, Mr Donaghue was struggling financially and could not meet repayments under a mortgage secured over his home, which was valued at $1.2 million. Mr Donaghue decided to transfer ownership of the home to his daughter and her de facto partner for $380,000. The sale proceeds were used to pay down the existing loan, and the daughter and her partner obtained a mortgage in their name.

Mr Donaghue believed that despite the transfer, he retained a beneficial interest in the property. He continued living in the home, was solely responsible for making repayments to the bank under the new mortgage and paying for rates and other expenses. Less than a year later, the daughter requested that Mr Donaghue pay an amount of $36,500 for costs associated with purchasing the property. Subsequently, statements were made by Mr Donaghue about the parties' respective entitlements to the house. His daughter and her partner rejected those statements and argued that the house was solely owned by them.

Proceedings were commenced by Mr Donaghue and Mr Donaghue was ultimately successful, with the Court finding that Mr Donaghue's daughter held the property on constructive trust for his benefit. While Mr Donaghue was successful, the absence of a written agreement between the parties significantly complicated the process and led to the need for court intervention.

Loan or gift?

The case of *Chaudhary v Chaudhary* [2017] NSWCA 222 involved the advance of $1.2 million by a father to his son and daughter-in-law (Adrian and Justine, respectively) to assist with the purchase of a family home in Sydney's inner western suburbs.

Prior to the purchase, Adrian and Justine had contemplated that Adrian would receive significant sums

of money or property from his parents during their relationship. With that in mind, a cohabitation agreement was entered into which stated that monies gifted or advanced to Adrian by his parents would be his sole property.

Adrian and Justine successfully bid for their intended family home at auction. The father originally agreed to "give" them $1.2 million to assist with the purchase and made clear statements to that effect to the bank. However, the father and Adrian ultimately decided the money would be advanced as a loan. A mortgage document was entered into naming the father as mortgagee, although it was never registered.

When the marriage broke down, the father commenced proceedings claiming that the money was advanced as a loan, while Justine argued that the money was advanced as a gift to the parties. The dispute was the subject of proceedings in three courts — the Family Court, and both the trial and appeal division of the Supreme Court. While the first instance judge found that the money was a gift, on appeal the court ultimately concluded that the money was advanced as a loan secured by the mortgage document and required a sum in excess of $1.6 million (including interest) to be paid from the property settlement pool of Adrian and Justine to Adrian's father.

Bank guarantees

In *Fast Fix Loans Pty Ltd v Samardzic* [2011] NSWCA 260, a short-term lender appealed orders made by a trial judge who found that a guarantee given by parents under a loan agreement was unjust and unenforceable.

Milan Samardzic was a builder and property developer for about 13 years. Milan, through his company, entered into an agreement to purchase a property, the purchase of which was subject to obtaining development approval for the construction of an apartment block. Milan needed $1.1 million to finance the purchase and the development, but was told that without additional security, he would not receive the amount needed for finance from his preferred lender. Motivated to help Milan, at Milan's urging, his parents agreed to offer their home in Bowral as security to a "last resort" lender. Milan ultimately defaulted on the loan repayments to the "last resort" lender.

The trial judge found that whilst the parents were aware that by signing the loan documents, they were putting the Bowral property at risk if Milan did not repay the loan, they thought the liability would cease after three months. It was clear that the parents did not fully understand the terms of the guarantee and the risk they were taking on, and the lender was unsuccessful. Although the Court of Appeal agreed with the trial judge, the parties were still put through the time and expense of court proceedings.

Tenancy agreements

Although the decision in *Dimov v Cagorski* [2017] VCAT 1039 involved a falling out between two "best friends", the circumstances giving rise to the dispute apply just as readily to a family situation where, for example, parents rent property to their child.

The parties were longstanding friends. Following the breakdown of her marriage, Cagorski and her children needed a place to live. Dimov offered her vacant home in Werribee for $275 per week, but no formal tenancy agreement was entered into. Ultimately, disputes about unpaid rent and requests for repairs led to Dimov giving Cagorski a notice to vacate the premises. The lack of documentation and asserted payments of rent in cash led to the tribunal having to determine what rent was owed and whether possession should be awarded. The Tribunal ultimately found that Cagorski owed Dimov $7,607.15 in unpaid rent and otherwise had to vacate the premises within 14 days.

Summary

These case examples demonstrate the difficulties that can arise when family members enter into financial arrangements, particularly with respect to property, without clearly stating and recording their intentions, rights and obligations in a written document. If the terms of an agreement or arrangement are not recorded in writing, it can later lead to:

- disputes between family members, and the corresponding impact upon family relationships;
- the involvement of a Court to determine the parties' positions; and
- the significant time, uncertainty and expense associated with litigation.

HopgoodGanim Lawyers has a team of professionals to assist you with these matters, including how your proposed arrangements may impact upon estate planning, property and family law issues. If you require assistance or more information please contact a member of HopgoodGanim Lawyers' HG Private team.

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Previous article Next article