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HELPING CHILDREN AND OTHERS NOW

Consider the following scenario: A retired couple with four adult children feel they have sufficient wealth to see them through their golden years. Their adult children, on the other hand, are all struggling with mortgages and the parents would like to share their estate now so they can enjoy the pleasure of seeing their children get ahead. What are their options?

<u>Direct Gifts</u>

The parents could give some capital to their children as a direct gift. Not only would the children benefit immediately, but the parents would pay less income tax because they no longer would receive earnings from the assets they give away. The parents should be aware, of course, that capital given to the children may be exposed to risk. For example, if the children are less prudent with their finances than their parents obviously were, the gift to any one child may go to a creditor if that child becomes bankrupt. A married child who finds himself or herself in the throes of divorce may see a parents' gift split with the ex-spouse, especially if the gift went towards buying a home.

<u>Family Loans</u>

One possible solution is for the parents to loan money to their children rather than giving it. This approach also has possibilities for loss, of course, especially if a child becomes bankrupt. When the bankruptcy is over, not only will that child have the difficult task of starting afresh, he or she also may feel morally obliged to repay the parents' loan. (Unlike the legal position of a discharged bankrupt and unsatisfied creditors, the stigma of not repaying a family member will often transcend any bankruptcy legislation.) If the child is married, and gets divorced, the animosity that often accompanies dividing matrimonial property may be compounded by the question of who will repay the parental loan. Even if these domestic disasters do not occur, it is possible that the parents may need money as they get older, and the child or children may be unable or unwilling to repay all or part of their loans to help out. Few parents can imagine suing a child for repayment of a loan.

Good estate planning can provide one possible solution to remedy this situation: The parents can loan the money to each child and hold mortgages on the childrens' homes as security. From a tax perspective, because the loans will be used to retire indebtedness rather than to earn income, there will be no threat of income being attributed back to the parents under the *Income Tax Act.* In the event of the bankruptcy of a child, the child may actually find himself or herself in the fortunate position of having the parents' mortgage repaid at the expense of unsecured creditors. And if the child's marriage fails, the mortgage will have to be repaid by both divorcing spouses before the matrimonial home can be sold. The parents then have the option of giving the money back to their child once the divorce is settled.

If the parents are concerned about having sufficient capital to maintain their standard of living, the mortgages could be made payable on demand. Unlike simple loans, which often suffer from lack of enforceability, family members tend to treat mortgages seriously. Although this is not a guarantee of enforceability, a loan given by way of mortgage has a greater likelihood of repayment and of timely periodic payments. Finally, the parents' wills could be drafted to forgive any mortgage balances still owed by their children.

Interest-Free Loans to Charity

Interest-free loans to charity are another way to help others now while retaining the right to recover principal. For example, a charity might be building a new facility and need an infusion of capital to get the project started. A donor who does not wish to make a permanent gift could give the charity an interest-free loan, giving the charity temporary use of the money and any earnings on it. This would save the donor from paying taxes on those earnings. At a specified future time – or upon demand, if the loan is so structured – the principal would be repaid. Anyone contemplating this option should know, however, that loans can be made to a registered charity but not to a public or private foundation.