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The Bank of Mum and Dad: The problem with family loans and gifts on divorce

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In times of ever-increasing property prices, parental contributions towards house purchases are becoming increasingly common. According to recent research by Legal & General, the "Bank of Mum & Dad" is now one of the UK's top ten largest lenders but what happens if the recipient later gets divorced and wants to repay the loan whilst the other spouse says it was a gift and should be shared as part of the family assets?

As lawyers dealing with divorce settlements on a daily basis we see the "... is it a gift, is it a loan ..." argument all too frequently. So how do you work out what is a gift and what is a loan and can you have a gift with a condition that it will be repaid in the event of a divorce?

The recent English case of P v Q (Financial Remedies) [2022] EWFC B9 (P v Q) provides some much-needed guidance.

The case itself involved two payments and the issue was whether they should be included on the asset/liability schedule as a resource/debt or excluded from the list as if monies should be returned from whence they came? The first payment was received by the wife from her father before the parties even met. This was for €30,000 to fund the wife's MBA course. The "loan" was recorded in a contemporaneous formal loan document but there was no history of repayment and no demand was ever made by the wife's father. Indeed, the wife had actually forgotten about the payment until shortly before the divorce trial, no mention was made of it in her financial disclosure and the wife gave evidence that she did not expect her father to ever-demand repayment.

The second payment was to the husband by his mother in the sum of £150,000 to assist him with "housing costs ...". There was no loan document, no demand was ever made for repayment nor were there any discussions about the circumstances in which repayment might be expected. The mother had made identical payments to her other two children and in effect this was an advance of inheritance.

The sting in the tail for the wife was that shortly after the marriage broke down the husband, without any demand from his mother and without consulting the wife, repaid his mother the £150,000 with an assertion that this was repayment of the loan. At trial, some two years later, the husband argued that the money was gone and should not appear on his list of assets as a resource to be shared equally.

Understandably, the wife was not too impressed with this and neither was the Judge who described the payment as a "... cynical manipulative device ..." which might give an early indication as to which way the Judge would eventually rule.

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In considering whether these were loans or gifts, the Judge said that as a general principle for an advance of money to be a gift there must be evidence of an intention to give. In each case, the Judge ruled that both payments were loans which could in theory be enforced. The Judge then went on to consider whether or not each loan should appear on the list of assets to be taken into account in the divorce proceedings. In dealing with this, the Court sought to distinguish between "hard" and "soft" debts as to whether or not repayment would be enforced. In what the Judge described as an "elusive topic" he set out the principles to define hard debts to include:

- whether it was an obligation to a finance company;
- whether the terms of the obligation had the feel of a normal commercial arrangement;
- whether there is a written agreement;
- if there is a written demand of repayment, a threat of or actual litigation or actual or threatened intervention in the divorce proceedings;
- whether there was any delay in enforcing the obligation; and
- whether the amount of money is such that it would be less likely for a creditor to waive the obligation either wholly or partly.

Similarly, in relation to soft debts the considerations included:

- whether it was an obligation to a friend or family member with whom the debtor remains on good terms and who is unlikely to want the debtor to suffer hardship;
- whether the obligation arose informally and if terms of the obligation do not have the feel of a normal commercial relationship;
- whether there has been any written demand for payment;
- if there has been a delay in enforcing the obligation; and
- whether the amount of money is such that it would be more likely for the creditor to be likely to waive the obligation either wholly or partly.

Applying these principles, perhaps not surprisingly, the wife's debt to her father was ruled to be a soft loan on the basis that it was never likely to be repaid nor would any repayment be required and thus the payment was not included on the list of assets. More tellingly, the husband's "cynical manipulative device" was not successful. His "debt" was ruled to be soft and was added back to the husband's schedule as if the payment had never been made in the first place.

So what can we learn from P v Q? Well first of all it seems that the rules are clear or certainly much clearer than has been the case previously and the judgment provides a non-exhaustive list of the factors to be taken into account. While there will always be some scope for judicial interpretation, it seems that the rules are pretty clear now so if you are considering making a gift or a loan to your children the obvious advice is to be clear from the outset and follow the rules of P v Q.

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