Family loans – what can happen when things don't go to plan

Lisa Morrissey & Taylor Horne | July 2018 | Banking & Commercial Disputes and Transactions

Summary

The Banking Royal Commission has highlighted the dangers involved in parents 'going guarantor' for their children.

Two recent NSW Supreme Court decisions (*Gladys Hargreaves v Susan Eveston*[1] and *Dunphy v Russell*[2]) illustrate precisely what can happen when financial dealings between family members do not go to plan. In a time where it is becoming more common for parents to assist their children with the purchase of real property, these cases are reminders that not all family financial arrangements will end well.

By adopting a careful approach to drafting and documenting of such arrangements, parties can reduce the chance of a dispute if things don't go to plan…

Decisions

In *Hargreaves*, Mrs Hargreaves (mother) loaned Mrs Eveston (daughter) nearly $1.7M in 2013 and 2014. The loan was due for repayment in September 2015.

In early 2015, the parties verbally agreed to vary the original term of the loan by a further 12 months to allow for real property owned by Mrs Eveston to be sold. Mrs Everston's property was sold, however completion of that sale was deferred for a period of 12 months (on terms agreed with the purchaser).

A dispute emerged regarding repayment of the loan to Mrs Hargreaves. Mrs Eveston alleged her mother had verbally agreed to a further deferral of repayment until completion of the sale. Mrs Hargreaves denied the conversation and maintained that the loan was due and payable. Mrs Hargreaves commenced proceedings to recover the loan.

The original loan agreement and correspondence between the parties was examined. The Court found that other than the alleged conversation, there was no other evidence to support a further deferral of repayment.

The Court found that the terms of the alleged conversation were ambiguous and uncertain as to be enforceable. The Judge concluded:

> *'some of the contingencies upon which the variation was based may never manifest and others were in such general terms that it would be difficult to know whether had eventuated.'*[3]

As a result, Mrs Eveston was ordered to immediately repay her mother for the owed amount, borrowed plus interest, and the costs of the proceedings.

In *Dunphy*, Mr Dunphy (father) contributed $200,000 towards the purchase of a property by Mrs Russell (daughter) and her partner.

Mrs Russell alleged the advance was a gift. Mr Dunphy said that it was an investment made by him in the property, and that it was loaned on the following terms:

(a) The property would be in Mrs Russell's name solely;

(b) No rent would be payable by Mrs Russell and her partner to Mr Dunphy; and

(c) In return, Mrs Russell's partner would carry out the renovations to the property.

The property was purchased and Mr Dunphy and Mrs Russell established a joint bank account. It was agreed Mr Dunphy would pay $150,000 into the joint account and the balance of the advance would be used to meet the cost of renovating the property.

At the time, Mr Dunphy drafted a partnership agreement between him and Mrs Russell. He also sought legal advice regarding that agreement. Prior to settlement of the property, the draft agreement was emailed to Mrs Russell, who subsequently emailed it to her mother for her advice. The agreement was never formally executed by the parties.

The terms of the draft agreement included how the shared account would be operated, the likely renovation costs and detailed arrangements for Mrs Russell and her partner to live at the property. It also provided that on the sale of the property, the net proceeds of sale would be distributed in accordance with the original proportions contributed.

The Court found Mr Dunphy had acquired a one third beneficial interest in the property, and that even though the draft partnership agreement was not formally executed, the conduct of both parties gave rise to an informal agreement, or implied contract supported by acts of part performance such as:

(a) payment of $200,000 by Mr Dunphy and $400,000 by Mrs Russell towards the purchase price

(b) preparation of the draft partnership agreement

(c) the opening of the joint account with Westpac

(d) the renovation of the property by Mrs Russell and her partner; and

(e) creation of the spreadsheets to account for rent and other expenses.

Implications

Both cases highlight the pitfalls of loans between family members, particularly large sums of money from parents to children for purchase of real property.

Family arrangements should never be treated as informal. Arrangements should always be documented, carefully drafted and always executed by the parties involved. Independent legal advice should be obtained by both parties before entering into arrangements, and any variations to the original terms should be documented.

Taking these precautions will help reduce any confusion among parties and limit the risk of unfortunate litigation, which may result in great expense (both monetary and personal).

[1] *Gladys Hargreaves v Susan Eveston* [2018] NSWSC 505
[2] *Dunphy v Russell* [2018] NSWSC 721
[3] [2018] NSWSC 505 at paragraph 41.

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