



Should I Loan Money to Friends?

I have read about “keeping it local” and the concept of being my own bank instead of giving money to a far-off mutual fund or greedy multinational bank. Do you think it is good idea to lend my savings to friends or others in my local economy?

I think it is a great idea. This country was built on friends and neighbors making loans to each other, and every dollar that stays in a local economy rather than a big-box store or a big bank is at least three times more beneficial to the local community. But after years of watching relationships go bad over “kinda loans” and “kinda gifts,” I have developed some simple rules.

If you want to help someone with a gift, give the money with no expectations. If the money is a loan, it is a business transaction. The person who is borrowing should write a proposal to you with the terms of the loan and a paragraph on each of the items I call the four C’s.

The terms include who is borrowing the money and who is responsible for paying it back. If both husband and wife won’t sign the loan, don’t do it! If you are lending to a business, get a copy of the business plan, have the owners tell you their business story, and have all the stakeholders sign the loan. Write down the loan amount, interest rate — I suggest a simple ½ percent or 1 percent a month (6 percent or 12 percent annually, respectively) until it is paid off — monthly payment, and penalty for being late. The penalty could be babysitting for you, canceling the borrower’s cable TV, or a financial penalty such as \$50.

THE FOUR C’S INCLUDE:

1. **COLLATERAL.** The borrower should describe the collateral and why it is

for your loan and not 10 other loans. If the borrower has no collateral, he should promise not to borrow more money until your loan is paid.

2. **CASH FLOW.** How does the borrower know she can pay you back? Will she get a bartending job, if necessary?
3. **CREDIT.** Who else does he owe money to? What is his credit score?
4. **CHARACTER.** Does your friend keep commitments? Does she show up on time? Did she screw the credit card company or bank? Get references; being listed as a reference causes that person to take at least a psychological interest in his friend’s loan.

If things go bad, you might have to say, “Here is a help-wanted ad for a toilet scrubber. I think you can make enough to pay me back.” For larger loans, get a lawyer involved, or ask a friendly banker to guide you.

My mom died and left me some cash. I spent it on what I thought was a “wise” investment — propping up a friend’s business. It failed. So now, my friend owes me money, my mom is turning in her grave, and I feel guilty for screwing up my inheritance. What do I do?

Someday I want to write a book called *Hard-Ass Zen*, and then I would say, “Get

over it and get on with it!” But I’m a softy, so I have three bits of advice: 1. Ask if your friend could pay you back over the next 10 years in equal monthly payments. 2. Realize your mom loves you. She gave you a great lesson, and she taught you to admit or share your so-called screw-ups. 3. Here is a favorite story that I told four times just last week:

In ancient China, a young man was given a fine horse for his kindness to a stranger who was passing through the town. The townspeople said, “Oh, such good fortune has fallen upon the young man.” The wise man said, “Perhaps.” A few days later the young man fell off the horse and broke his leg. The townspeople said, “Oh, such bad fortune has fallen upon the young man.” The wise man said, “Perhaps.” The next day an emissary from the king came into town to collect young men for war. They did not take the young man because of his broken leg. The townspeople said, “Oh, such good fortune has fallen upon the young man.” The wise man said, “Perhaps.”

In other words, get over it and get on with it.

I would love to hear of your successful loans, or stories of “friendly” loans gone bad. Please email me.

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