MONEY MANAGEMENT

TREAT LOANS AS BUSINESS TRANSACTIONS

Don't let your emotions cloud your thinking when making loans to family members. Family relationships are less likely to be jeopardized if you work out the details of any loan agreements before you hand over the money to a relative.

HOW MUCH CAN YOU AFFORD TO LEND?

The Nevada Society of CPAs recommends that before you lend money to anyone, you should assess your current financial situation. Consider the impact a loan will have on your cash flow, outstanding debts and future financial goals. This will guide you in determining how much you can afford to lend and for how long. Don't jeopardize your own financial situation by borrowing money against credit cards or from other sources in order to make a loan to a relative.

SETTING INTEREST RATES

Once you have determined how much money you can afford to lend, the next step is deciding how much interest, if any, you will charge. If you have cash in savings vehicles offering low returns, such as 3 percent, you can offer your relative an interest rate of 6 percent and earn more money. What's more, a 6 percent rate is advantageous to your relative since it is lower than typical rates on personal, consumer and home-equity loans.

In establishing an interest rate on an intrafamily loan, be sure to consider the federal tax implications. Minimum interest rates are fixed by the federal government according to the type and term of the loan. For a demand loan (a loan payable in full at any time on demand of the lender) if you don't charge the applicable short-term federal rate (recently 3.92 percent), you are considered to have "imputed" or unstated interest and will be taxed on the difference between the federal rate and what you actually charged. There are several important exceptions to these rules.

The imputed interest rule does not apply to loans of up to $10,000 if the loan is used for certain non-business purposes. For example, if your brother needs to borrow $5,000 to finish his college education and you opt to lend him the money interest-free, you will not incur any imputed interest.

On loans of up to $100,000, interest will be imputed to the lender only to the extent of the borrower's annual net investment income (i.e. interest, dividends, and capital gains). If such income is less than $1,000, no imputed interest is deemed transfered to the lender. So, if upon your daughter's completion of law schol, you lend her $50,000 to start a law practice and she has no investments that are producing income, you can provide the loan at an interest rate that is below federal minimum rate without any tax repercussions.

Keeping mind, too, that making loans of over $10,000 at a below-market interest rate may result in the loan being demed a gift in the IRS's eyes. As a result, you or the recipient may be required to pay a gift tax.

FINANCING A RELATIVES HOME PURCHASE

If a family member asks you to help finance a down payment on a new home, you can offer to make a number of different arrangements. For example, you can deposit the money needed to satisfy the down payment in a collateral account with the mortgage lender. With this type of arrangement, your deposit, plus interest, will be returned once the mortgage lender determines that the mortgage holder has built up sufficient equity in the home.

Depending on your financial situation, you can also consider holding the mortgage on the home yourself. Structured properly, you may be able to generate more income this way than by putting your money in other investments. Assuming you charge your relatives an interest rate that is lower than the current rate of mortgage lenders, your relatives will be able to build equity in their own homes. In addition, they save on points and other bank service fees.

If you prefer to provide your relative with a personal loan to help finance a down payment, your relative may be able to claim the interest paid to you as deductible mortgage interest if the loan is secured by the residence.

PUT AGREEMENTS IN WRITING

CPAs recommend that you put all loan agreements in writing, clearly specifying the amount of the loan, interest rate, repayment schedule, and if necessary, collateral. This will help ensure that you are repaid according to your wishes.

Money management is a public service announcement on personal finance prepared and distributed by certified public accountants. Nevada Society of Certified Public Accountants, 5250 Neil Road, Suite 205, Reno, Nevada 89502.

When To Revamp Your Fund Portfolio

BOSTON - Once you have chosen a portfolio of mutual funds to meet your future goals, it would be nice to flip a cruise-control switch and let the fund managers take over. But even the most passive investors should make periodic adjustments to their fund holdings.

As a rule, such changes should not be dictated by fluctuations in the financial markets, however. Instead, they should be linked to the rhythms of your life. As time passes, your financial goals will change and so will your ability to tolerate certain types of investment risk.

There will also be times when you take on new financial burdens, and your portfolio should reflect them.

For example, you might become responsible for an elderly parent in financial trouble at a time when you are saving for other long-term goals. Or you might decide that you want to change your career and accept a salary cut that will disrupt some of your investment plans.

In short, things change. Your fund strategy should be flexible enough to adapt to such changes as they happen, and to meet sometimes conflicting financial goals over time.

When you are starting your career, for example, you may be hard-pressed simply to meet the expenses of running a household. At the same time, you'll want to save for some short-term goals such as a downpayment on your first home, or the expenses of starting a family.

That money can go into money market funds that hold stable, cash investments, such as Fidelity Cash Reserves (no load; 800-544-8888; $2,500 minimum investment). Or you could choose funds that buy short-term bonds, such as Vanguard F/I Short-Term Corporate (no load; 800-662-7447; $3,000 minimum investment).

Still, financial planners and other experts insist that if you can get a headstart on saving for *(See Fund Portfolio, Page 24)*