



# How to make a borrowing agreement with family and friends



Borrowing from friends and family to fund your business is a cheap and flexible form of financing, but it can lead to misunderstandings unless you agree on the terms upfront.

What should you discuss with your loved ones before drawing up a financing agreement? Use this worksheet — along with the information in the article [Managing family and friends financing](#) — to get clarity and avoid potential conflicts.

## Loan, gift, or investment?

First, clarify what kind of funding you’re discussing with your loved one. Are you borrowing money in the form of a loan or are they investing in your business? Is the money a gift with no expectation of repayment?

- Loan    Investment    Gift

After you’ve agreed on the nature of financing, proceed to the appropriate step.

## Loan

If you’re taking a loan, talk through each of these questions with your family member or friend and make a note of the answers here.

*Note: The IRS requires family loans **great than \$10,000** to have a minimum interest rate known as the [Applicable Federal Rate](#), which changes every month.*

### Loan specifics:

- What is the amount of the loan? \$ \_\_\_\_\_
- When will you start making payments on the loan? *A starting point could be six months or one year from the borrowing date.*

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- The [Applicable Federal Rate](#) at the time of making this agreement is \_\_\_\_\_ %.
- At what frequency will you make payments? *Options can include biweekly, monthly, etc.* \_\_\_\_\_

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- What will happen if you need to pause payments temporarily? For how long can you pause payments? \_\_\_\_\_

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• What will happen if you cannot pay back the loan? \_\_\_\_\_  
\_\_\_\_\_  
\_\_\_\_\_

## Investment

If your family member or friend is investing in your business, talk through these questions to decide what they get in return.

1. What kind of investment is it?

- Angel investment.** This means your loved one may offer mentoring in addition to money but not necessarily expect anything in return.
- Equity investment.** This could be in the form of common shares, which allows your loved one voting rights in your business, or preferred shares, which gives them an agreed-upon dividend. Equity investments such as these require a legal document that outlines the specific terms of the investment.

2. As an investor, will your loved one be part of business decisions? Or just a silent investor? Here are a few options to consider defining their role.

- Silent investor.
- Advisor role: When consulted, will offer guidance/suggestions.
- Would like to be consulted for major decisions.
- Would like to play an active part in growing the business.
- Other: \_\_\_\_\_

## Gift

If you've agreed to accept the money as a gift, make note of the amount here. The IRS requires people to pay "gift tax" for amounts over a specific limit each year. For 2023, you can [check the limit and learn more about the gift tax](#) on the IRS' website.

Gift amount: \$ \_\_\_\_\_

It's also worth discussing whether the gift carries an expectation that you will involve your loved one in business decisions.

This worksheet is a starting point to understand how to accept funding from friends and family for your business. Remember that while there are advantages to taking money from loved ones, you won't be able to build business credit for future financing needs.

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