

Are you borrowing money from friends or family? If so put the terms and conditions in writing first.

"Never again," says Martha Woods of lending money to family or friends for business ventures.

Woods and her husband once invested about \$10,000 in an auto racing team with his brother, but her brother-in-law wanted out after one season. Her husband had to buy back the business, including a car and trailer he paid for and built.

"Friends and family" investments are increasingly popular given the limited capital and credit available. Banks have raised credit requirements, homes don't have the equity they once did and start-ups seldom have the assets professional lenders seek when they're doling out loans, says Cap Willey, a CPA with CBIZ Tofias in Rhode Island.

Given the paltry interest rates being offered on bank CDs, getting 3% to 4% interest on a loan to your second cousin may sound like a great idea. But while it may be safer than forking over cash to a stranger, friends and family investments are not without risks. "Those are the relationships that oftentimes get people in trouble," says Kentucky Attorney General Jack Conway. ...

So how to reap the benefits while avoiding the risks?

Consider whether you can afford to lose the money, says Willey, whose clients include small-business borrowers, lenders and investors. Willey and Conway both recommend getting everything in writing, but Conway says a promissory note has no value unless it follows state laws.

Promissory-note fraud is one of the leading violations pursued by state securities officials, according to the **North American Securities Administrators Association**.

Conway says a promissory note should specify whether it can be redeemed on demand and what collateral is being put up. "Put yourself in the shoes of a bank and consider: 'What's this person's ability to repay me?'" he says.

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