Helping Your Adult Children

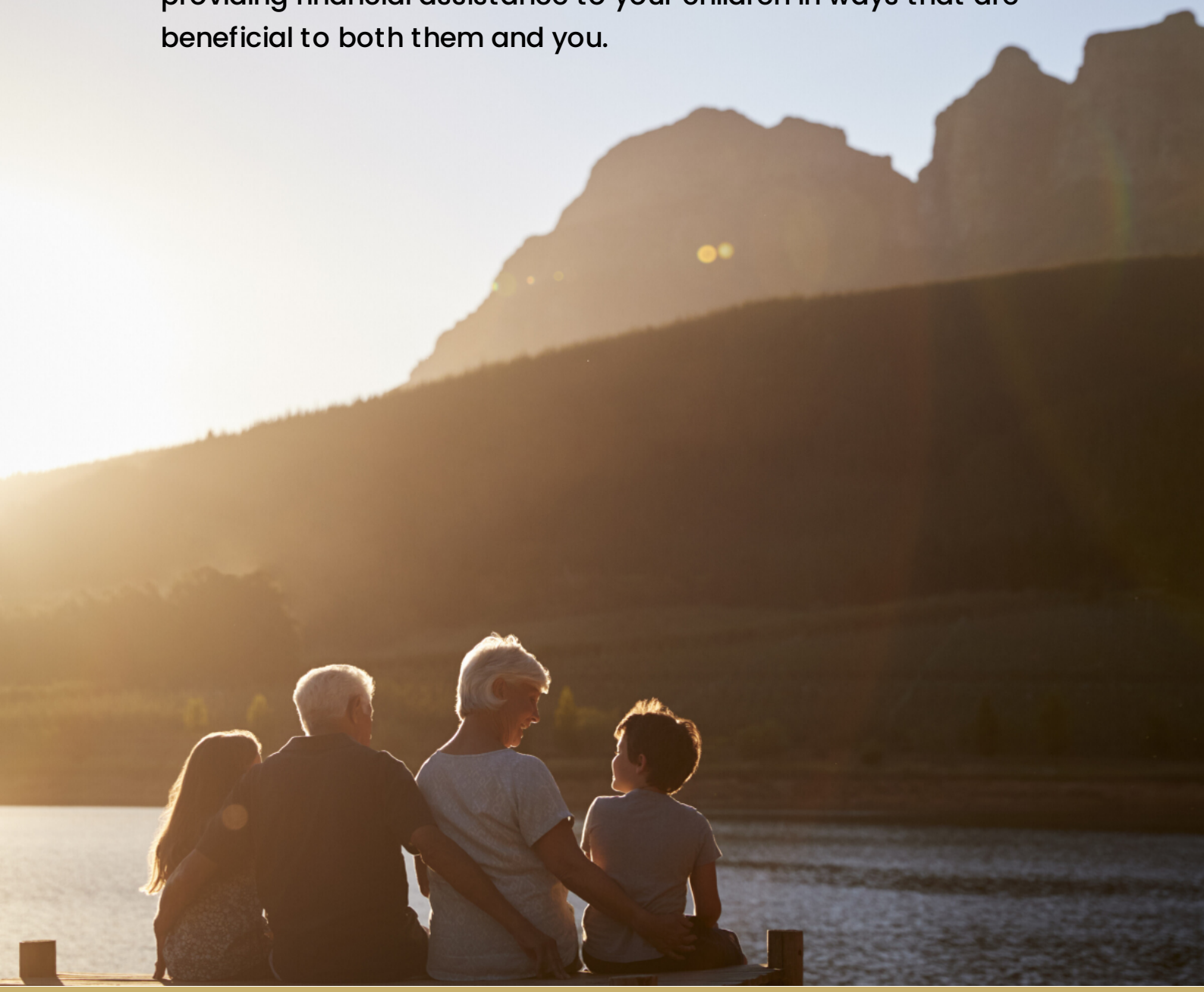
Financial education and considerations

ALTERIS FINANCIAL GROUP

Helping Your Children Financially: A Parent's Guide

As parents, one of the most impactful things we can do for our children is to help them build a secure financial future. Whether it's by gifting money, offering financial advice, or ensuring they understand key financial concepts, our support can set them up for success.

This guide explores various strategies and methods for providing financial assistance to your children in ways that are beneficial to both them and you.



Different Ways to Help Your Children Financially

There are numerous ways to assist your children financially, depending on their current situation and your means. Here are some common approaches:

Lump sum for significant expenses: A lump sum is a one-time financial gift often used for major expenses such as a home deposit, starting a business, or repaying a student loan. This can be an excellent way to give children a significant financial boost, allowing them to make life-changing purchases or investments without taking on excessive debt. Lump sums are often used to accelerate savings goals or reduce borrowing costs, particularly in high-value areas like real estate.

Income stream: Instead of a one-time gift, some parents choose to provide ongoing financial support through an income stream. This could take the form of regular payments to assist with ongoing costs such as mortgage repayments, rent, or utility bills. An income stream can provide ongoing relief for children facing long-term financial pressures, such as a young family or those with irregular income.

Helping children into property ownership: A lump sum for a deposit, an income stream for Mortgage repayments, and acting as a guarantor are some of the ways parents can assist their children into property ownership depending upon your financial capacity and their needs.

Covering education expenses: Education is one of the most valuable investments a parent can make in their child's future. By paying for private school, university tuition, or postgraduate studies, parents can help their children avoid student debt and focus on their education. This can also extend to covering the cost of specialised training or certifications that can improve job prospects.

Contributing towards insurance premiums: Parents can help alleviate financial stress by covering or contributing towards their child's insurance premiums. This could include life insurance, health insurance, or car insurance. While these payments may seem smaller compared to larger expenses, they can provide significant peace of mind and security for the child.

Boosting superannuation: Contributing to your child's superannuation fund is a long-term financial strategy aimed at securing their retirement. Early contributions can significantly boost future savings through compound interest. This is particularly valuable for children who may not yet be in a financial position to prioritise retirement savings.

The "Bank of Mum and Dad" – What Is It?

The "Bank of Mum and Dad" refers to parents who provide financial support to their adult children, especially when it comes to large expenses like purchasing a home or funding education. With rising living costs and property prices in Australia, this financial help has become more common as young people face greater financial hurdles than previous generations.

Statistics on Parental Financial Support

Research shows that more than 40% of first home buyers* in Australia receive financial assistance from their parents (For people who bought their first house before 1980, just over 15% received a loan or a gift from family members). These contributions help them overcome challenges like saving for a deposit or avoiding lenders' mortgage insurance (LMI). The Bank of Mum and Dad is now considered between the fifth and ninth largest mortgage lender in Australia**, highlighting its significance in helping young Australians enter the property market.

* https://percapita.org.au/wp-content/uploads/2023/03/Housing-Monitor-Report-1-VF-smaller.pdf

** https://www.pc.gov.au/research/completed/wealth-transfers/wealth-transfers.pdf

Lump Sum vs Income Stream

Choosing between giving a lump sum or providing an income stream involves weighing the immediate and long-term benefits for both you and your child. Each approach has its advantages, but they work best in different circumstances depending on your goals and your child's financial habits.

Lump Sum

A lump sum is a one-off payment that can be used for a significant financial goal, such as a home purchase, debt repayment, or starting a business. This method of financial support provides immediate and substantial assistance, enabling your child to achieve major milestones without prolonged financial strain. By offering a lump sum, parents can help their children bypass certain financial hurdles that might otherwise take years to overcome through savings alone.

Benefits:

- Provides immediate financial assistance, helping children achieve large goals quickly.
- Grants them flexibility in how to use the funds.
- By providing a substantial amount upfront, you can help alleviate the stress and pressure associated with large financial commitments.

Disadvantages:

- Children may mismanage the funds if they lack financial experience.
- Can strain the parent's finances if not considered alongside their own financial security and plans.
- Large gifts may have tax consequences

> Emily and her husband Greg had always planned to help their daughter Lily with a house deposit when she was ready to buy her first home. Lily had been diligent with her savings, but housing prices had continued to rise faster than she could save. When Lily found a property she loved, she was $100,000 short of the required deposit. Emily and Greg discussed their financial situation with their adviser and decided they were in a good position to offer the $100,000 as a lump sum. With this, Lily was able to secure the property without the need for additional loans or financial assistance. Over the next few months, Lily focused on managing her mortgage payments and felt secure knowing her parents' gift had reduced her financial burden. For Emily and Greg, the satisfaction of seeing Lily move into her dream home outweighed the sacrifice, and they remained financially comfortable after the contribution.

Income Stream

An income stream involves providing regular payments to assist with ongoing expenses, such as living costs, education, or mortgage repayments. Unlike a lump sum, an income stream offers sustained support, making it particularly beneficial for situations requiring long-term financial aid. This method can help your child manage regular commitments, giving them more financial stability and peace of mind over time.

Benefits:

- Parents retain access to capital
- Encourages long-term budgeting and financial responsibility.
- Offers parents more control over the timing and size of the financial assistance.
- Amount and frequency can be adjusted as needs change.

Disadvantages:

- Risk of creating dependency.
- Long-term financial commitment can be burdensome for parents.

Mark and Jane's daughter, Alex was attending university and had taken on part-time work, but she was struggling to cover her rent and living expenses in a city with a high cost of living. To help her focus more on her studies, Mark and Jane decided to provide a monthly income stream of $500. This amount covered most of her rent, allowing Alex to spend more time studying and less time worrying about making ends meet. The arrangement worked for everyone involved: Alex learned how to budget with a consistent income stream, and Mark and Jane were able to gradually provide support without draining their own savings. Over time, Alex's part-time income increased, and by her final year of university, she no longer needed the extra financial help, having learned how to manage her own money effectively.

Gifting vs Lending

When providing financial support to children, parents must decide whether to offer the funds as a gift or a loan. Both approaches have distinct implications, and understanding the differences can help ensure clarity and protect both parties.

Gifting:

- **No Repayment:** A gift is a one-time or ongoing financial contribution with no expectation of repayment. This can provide immediate relief or support without adding financial obligations to the recipient.
- **Age Pension Considerations:** Gifts can have an impact on those who are in receipt of the Age pension, as they may still count towards your income and asset tests.
- **Structure:** A gift is often informal, but parents may want to document it for clarity, particularly when it's a large sum, to avoid future misunderstandings among siblings or for tax purposes.

> **Tom's parents gave him $30,000 as a gift for a house deposit. There was no expectation for him to repay this amount, and they updated their will to reflect this early distribution, ensuring fairness among his siblings.**

Lending:

- **Repayment Required:** A loan implies that the funds will be repaid under agreed-upon terms, which could include a specific repayment schedule, interest rates, or deadlines. This formalises the financial assistance and places responsibility on the child to return the money over time.
- **Legal Protection:** A loan should be documented with a formal loan agreement to avoid potential disputes and to ensure both parties understand the terms. This document can outline repayment expectations, interest rates (if any), and consequences of default.
- **Family Dynamics:** While loans provide financial assistance, they may also introduce tension into family dynamics, especially if the borrower struggles to repay or if there are disagreements over terms.

> Jane's parents loaned her $50,000 to start her business, with the agreement that she would repay $500 a month until the loan was paid off. They documented the agreement with a formal contract to protect their interests and ensure clarity.

Key Differences:

- **Gift**: No expectation of repayment, tax considerations, often informal.
- **Loan**: Repayment required, documented agreement, legal protection.

Parents should carefully assess their financial capacity and the potential impact on family relationships when deciding between gifting or lending. Consulting with a lawyer and financial adviser can also help structure these arrangements appropriately.

> When Sarah needed financial help to cover unexpected medical expenses, her parents offered to lend her $20,000. They verbally agreed on a repayment plan but did not formalise the arrangement in writing. Over time, Sarah struggled to keep up with her other expenses and fell behind on the repayments. When her parents asked for payment, Sarah disputed the amount owed, claiming she didn't remember the exact terms of the agreement. Tensions escalated, leading to a family conflict and ultimately forcing her parents to seek legal recourse. In court, the lack of documentation made it difficult for her parents to prove the loan's existence and terms, resulting in a disappointing outcome for both parties.

Helping Children into Property Ownership

One of the most impactful ways to help your children is by supporting them in purchasing property. Given the rising property prices in Australia, this type of support can make a huge difference, whether it's through a deposit, acting as a guarantor, or assisting with repayments. Each approach has its pros and cons.

- **Lump Sum for a Deposit**: Providing a one-off payment to assist with the deposit, and potentially avoiding lenders mortgage insurance (LMI).
- **Income Stream for Mortgage Payments**: Regular payments that assist with ongoing mortgage costs.
- **Acting as a Guarantor**: By guaranteeing part of the loan, parents can assist their children secure better terms for the loan including avoiding lenders mortgage insurance or getting a better interest rate.

These strategies vary in terms of financial risk and commitment for parents, so it's important to consider the long-term implications of each approach.

> Jake had always dreamed of helping his son Noah buy his first home, but Noah was struggling to save for a deposit. Jake decided to step in when Noah found a small two-bedroom apartment he liked in Melbourne. After consulting his financial adviser, Jake provided $50,000 towards the deposit and agreed to act as a guarantor on the loan. This significantly lowered the amount Noah had to borrow, helping him secure a more favorable interest rate. Although acting as a guarantor carried some risk for Jake if Noah couldn't keep up with mortgage payments, the two had a clear plan: Jake's contribution and guarantee gave Noah the opportunity to own a home much sooner than he ever thought possible. Over time, Noah learned to manage his mortgage responsibly, and Jake took pride in knowing that his support had made a lasting difference.

Superannuation and Insurance Contributions

Helping your children with their superannuation and insurance can be a smart way to ensure long-term security. Super contributions give your child a head start on their retirement savings, while insurance payments can provide peace of mind in case of emergencies.

Superannuation: contributing to your child's superannuation fund can significantly enhance their financial future. By making additional contributions, parents can help build a stronger retirement nest egg, leveraging the power of compound interest over time. These contributions not only increase the funds available at retirement but also provide parents with tax advantages, particularly through non-concessional contributions, which can be made without immediate tax implications. This strategy not only supports their child's future but can also lead to potential tax deductions for the parents, making it a mutually beneficial arrangement.

> Consider two individuals, Anna and Tom, both in their early 30s with identical salaries:
>
> **Anna** makes additional non-concessional contributions of $5,000 a year to her superannuation. By the time she retires at 65, Anna's super has grown significantly thanks to compound interest, giving her a comfortable retirement nest egg. Additionally, she benefited from tax advantages during her working years.
>
> **Tom** doesn't make any extra contributions, relying solely on his employer's super guarantee. By the time he retires, his superannuation fund is considerably smaller than Anna's, leaving him with fewer resources to maintain his desired lifestyle in retirement. Without the additional contributions, Tom's fund didn't compound as quickly, and he has fewer tax benefits over his career.

Insurance Payments: Assisting your children with insurance payments can provide crucial financial security. By covering health insurance, life insurance, or income protection premiums, parents ensure their children are adequately protected in case of unforeseen circumstances, such as serious illness or job loss. This support can alleviate financial stress and prevent potential debt accumulation during difficult times. Furthermore, helping with insurance can encourage responsible financial behavior, as it instills the importance of protecting one's future and managing risks effectively. In the long run, this assistance fosters financial stability and security for the entire family.

Estate Planning and Preparing for the Future

When planning to give financial assistance to your children, it's essential to consider the impact on your estate plan. Providing financial support during your lifetime, such as a lump sum or regular payments, may affect the balance of your remaining assets. To ensure fairness and avoid future disputes, it's important to keep your will updated, reflecting any substantial gifts or changes to your financial situation. Consulting with a legal adviser can help structure these contributions in a way that aligns with both your current support and your long-term legacy.

Pre-Inheritance: Sharing the joy today

Many parents choose to provide financial help during their lifetime, rather than waiting for inheritance. This allows them to experience the joy of seeing their children and grandchildren benefit from their support, whether it's helping them purchase a home, pay for education, or start a business. By giving while alive, parents can be actively involved in these milestones, witnessing the positive impact firsthand and potentially reducing the complexity of estate planning.

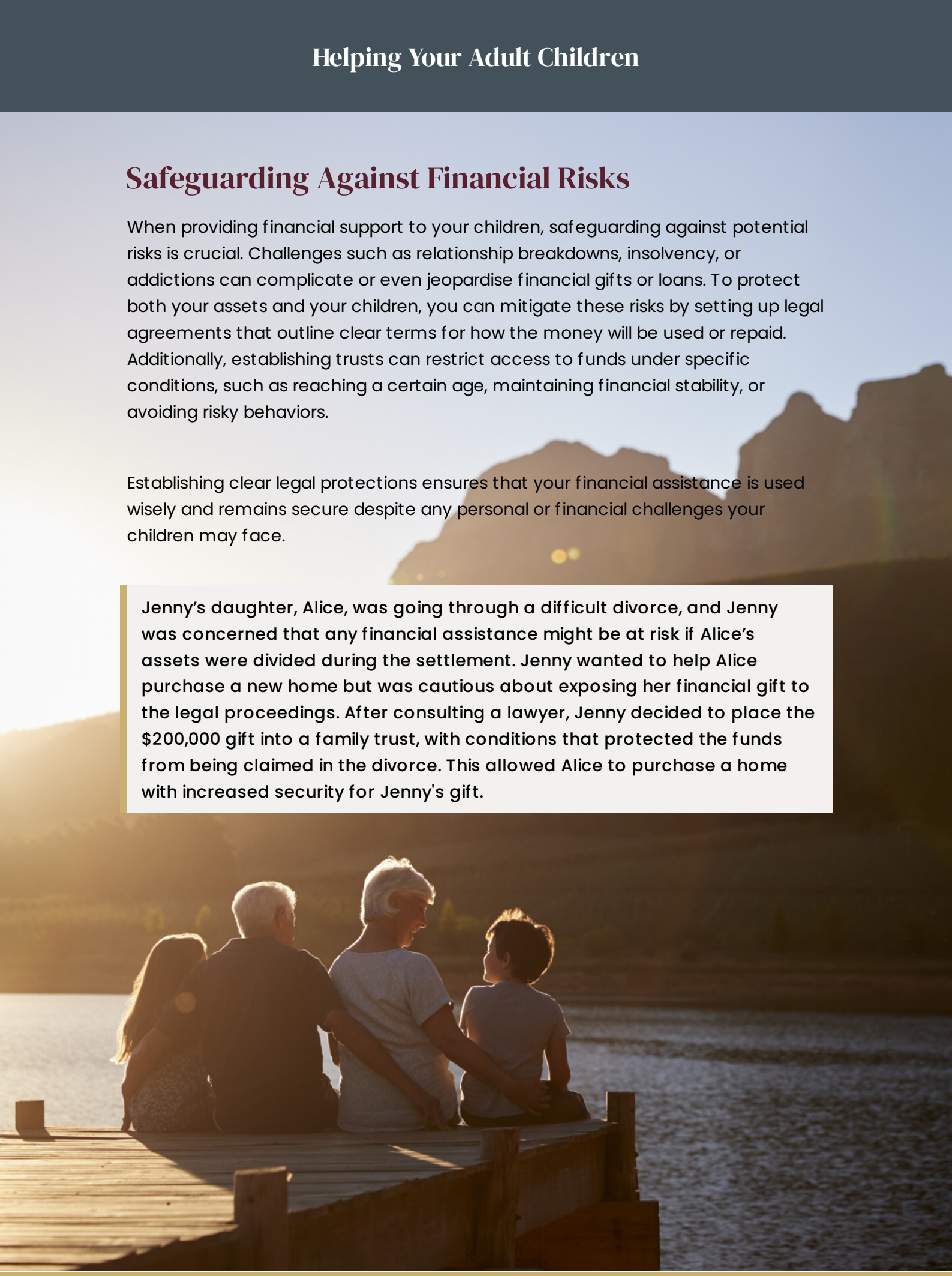
> **Maria and her husband had built significant wealth through years of careful investment. Rather than waiting until their passing to distribute their estate, they decided to gift $100,000 to their son Chris, who was struggling to save enough for a house deposit. Chris and his wife had been renting for years, and this gift allowed them to finally buy a home in a family-friendly suburb. Maria and her husband were thrilled to help and enjoyed visiting their son and grandchildren in the new home. The couple felt immense satisfaction in knowing they had made a tangible difference while they were still alive, and they updated their estate plan to reflect the gift, ensuring all their children were treated fairly in the future.**

Safeguarding Against Financial Risks

When providing financial support to your children, safeguarding against potential risks is crucial. Challenges such as relationship breakdowns, insolvency, or addictions can complicate or even jeopardise financial gifts or loans. To protect both your assets and your children, you can mitigate these risks by setting up legal agreements that outline clear terms for how the money will be used or repaid. Additionally, establishing trusts can restrict access to funds under specific conditions, such as reaching a certain age, maintaining financial stability, or avoiding risky behaviors.

Establishing clear legal protections ensures that your financial assistance is used wisely and remains secure despite any personal or financial challenges your children may face.

> **Jenny's daughter, Alice, was going through a difficult divorce, and Jenny was concerned that any financial assistance might be at risk if Alice's assets were divided during the settlement. Jenny wanted to help Alice purchase a new home but was cautious about exposing her financial gift to the legal proceedings. After consulting a lawyer, Jenny decided to place the $200,000 gift into a family trust, with conditions that protected the funds from being claimed in the divorce. This allowed Alice to purchase a home with increased security for Jenny's gift.**



Encouraging Financial Education

Encouraging financial education is one of the most valuable gifts you can offer your children. By teaching them about essential concepts like budgeting, investing, and money management, you empower them to make informed financial decisions throughout their lives. Financial literacy helps them understand the importance of living within their means, planning for long-term goals like homeownership or retirement, and navigating complex financial products. It also instills confidence, reducing their reliance on parental support in the future.

> Paul was concerned that his daughter Ava, fresh out of university, didn't fully understand how to manage her finances. She had a decent job but was unsure about budgeting and often ended up spending more than she intended. Paul sat down with Ava and helped her create a simple spreadsheet to track her income and expenses. They worked together to build a realistic budget, factoring in her rent, utilities, groceries, and discretionary spending. Paul also introduced her to the concept of emergency savings and the benefits of contributing to her superannuation early. Over time, Ava became more confident in managing her money, and within a year, she had saved enough to buy her first car without taking on any debt. This experience not only improved Ava's financial literacy but also brought her and Paul closer as they bonded over discussions about money.

Grandchildren and Beyond

Many parents extend their financial support beyond their children, helping their grandchildren with significant life milestones. This might include contributions to their education funds, assisting with the purchase of their first car, or even helping with a house deposit. These gestures offer financial stability for the next generation and can relieve pressure on parents who may not yet have the resources to provide such large-scale assistance. By offering early support, grandparents can create a lasting impact and foster long-term financial security across multiple generations.

> **Claire had always dreamed of seeing her grandchildren have access to opportunities that would set them up for life. When her first granddaughter was born, Claire set up a special savings account in her name. Each year, she deposited $5,000 into the account with the goal of eventually covering some of her granddaughter's private school tuition and university expenses. By the time her granddaughter turned 18, the account had grown substantially. Claire's thoughtful planning ensured that her granddaughter could graduate without the burden of student loans. Claire was overjoyed to see her granddaughter succeed, knowing that her early contributions had made a real difference in shaping her future.**

The Power of Collaboration

Collaboration between a financial planner and an estate planning lawyer offers numerous advantages when it comes to managing your assets, protecting your wealth, and planning for the future. By leveraging the expertise of both professionals, you can develop a comprehensive and effective strategy to ensure your wishes are carried out.

How to get in touch

With the guidance of our advisers, you can benefit from the peace of mind that comes with knowing your best interests are being taken care of. We're here to help answer any questions you may have and guide you through the complexities of your financial journey.

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