Down Payment And Home Equity Explained

By: Chad Moore

Download each of my pillars for Mortgage qualifying at www.chadmoore.co/mortgage-calculator.

You'll learn about:

- Income eligible for Mortgage qualifying.
- Understanding how much you can afford to purchase.
- Credit required for a successful Mortgage application.

For other information related to understanding your Mortgage qualifying, the local Real Estate market and for strategic economic updates, please visit my blog:

www.chadmoore.co/blog.

My goal is to become the number one Mortgage Broker in Alberta by 2025. My plan for doing so is to ensure you feel confident in your Mortgage plan and strategy that helps achieve your Real Estate goals.

I do this with expert advice, personal customer service and ongoing Mortgage management so you feel very confident referring your friends, family and co-workers.

Reach my team or I by calling 403-809-5447 or emailing chad@canadamortgagedirect.com

Thank you,
Chad Moore

Down Payment And Home Equity Explained

I've had last minute purchase files come across my desk with buyers in the middle of making an offer on a home. Trust me, with how strict Mortgage qualifying is in Canada, I do not recommend this.

Why?

Because planning eligible money to be used as a down payment is a very common occurrence in a successful Mortgage application.

Without proper down payment planning, or awareness, a Mortgage application could be declined resulting in loss of time, energy and money invested in the potential home purchase.

I've bore witness to buyers having their Mortgage application declined due to improper Mortgage planning – specifically regarding their down payment!!

Down payment options, rules, eligibility and criteria are constantly changing in the Canadian Mortgage landscape. Zero down payment, or flex down payment options use to be the norm. Those options are now nearing extinction.

At the very least, proper down payment planning will save you a flood of additional paperwork to verify the path of money. I swear, half of my time spent with clients is apologizing how much paperwork is required to secure a Mortgage – specifically related to down payment verification.

Let's learn about down payment in Canada so you're well prepared for your future home purchase!!

Here's what you'll discover below:

1. What is a down payment?
2. Down payment percentages.
3. Mortgage insurance.
4. Down Payment eligibility.
5. Tips & tricks.

<u>What Is A Down Payment:</u>

Mortgages exist because people are allowed to purchase homes without having enough money to purchase the home at full price.

I find it pretty rare that a buyer has cash to purchase a home (especially first time buyers) so there is a BIG market for people to borrow money. However, eventually becoming Mortgage free OR purchasing a home with cash does become more common for homeowners later in life.

People have some money saved up to put towards the purchase price of their home. This is referred to as their down payment.

Down Payment Percentages:

The minimum down payment in Canada is 5% of the purchase price of the home up to $500,000. The minimum down payment for homes over $500,000 is 5% of the first $500,000 and 10% of the remaining home purchase price over $500,000.

Quick example of minimum down payments:

The minimum down payment for a buyer purchasing a condo valued at $350,000 is $17,500 (350,000 * 0.05).

The minimum down payment for a buyer purchasing a detached home valued at $590,000 is $34,000. Remember, the first $500K is a minimum of 5% and the remaining balance requires a minimum down payment of 10%. The calculation is this: $500,000 * 0.05 = $25,000. $90,000 * 0.10 = $9,000. $25,000 + $9,0000 = $34,000.

A down payment percentage of 20% or more does not require Mortgage Insurance.

A down payment can be as little as 5% or any number up to the total purchase value of the home. Various down payment percentages, lower than 20%, will trigger different percentages of Mortgage Default Insurance.

Mortgage Default Insurance:

In Canada Mortgage Default Insurance is required for any down payment less than 20% of the purchase price. The Mortgage borrower pays the Mortgage insurance premium and the Mortgage lender get the protection. The insurance premium is capitalized (added into) the total Mortgage loan balance. The Mortgage insurance protects the Mortgage lender from any financial loss should the homeowner default on their Mortgage.

Mortgage default is when the borrower cannot pay their Mortgage payments. The homeowner falls into payment arrears which leads to the Mortgage lender initiating foreclosure proceedings. In the worst and most extreme cases of foreclosure, the home is sold for less than the Mortgage amount creating a loss for the Mortgage lender. The lender would file a default insurance claim to the Mortgage insurance company to cover the financial shortfall.

The Mortgage Default Insurance premium is paid one time. Should the Mortgage be ported to another property, it is possible to port the Mortgage Default Insurance certificate too.

Mortgage Default Insurance is distinct from Mortgage Life & Disability insurance. Remember, Mortgage Default Insurance protects the Mortgage lender from any financial loss. Mortgage Life & Disability insurance protects the client from any financial loss. These are separate and distinct insurance tools.

There are three Mortgage Default Insurance companies in Canada. The largest, and I think most recognizable, is Canada Mortgage and Housing Corporation (CMHC). This is a crown owned corporation. The other two Mortgage Default Insurance companies are private. Their names are Genworth Financial and Canada Guarantee.

Each of these Mortgage Default Insurance companies have virtually the same Mortgage underwriting guidelines and regulations. However, I have had Mortgage Default Insurance companies decline a file, and have another Insurer approve it. This is another benefit of working with an independent Mortgage Broker. I have access to Mortgage lenders that prefer certain Mortgage Insurance companies over others where I can make custom Insurer requests.

Down Payment Eligibility:

Down payment eligibility is something many people do not have a clear understanding of. Ill preparation of presenting down payment documentation to a Mortgage lender may result in a file being declined, delaying the home purchase, extending financing conditions OR creating a seemingly endless request of document verification.

Note: when providing down payment paperwork please ensure your name, date and account numbers are legible/available for viewing. Please do not blackout any information from these documents.

Below is more information on eligible down payment:

Eligible sources of down payment money: 90 Day Rule

Please be aware of the “90 Day Rule”. For money to be eligible for purchasing a home in Canada, the Mortgage lenders need to know of its’ whereabouts for the past 90 days.

There needs to be paperwork verifying the money earmarked for down payment has been in the applicants possession for 90 days. Examples of this are 3 months bank statements or a most recent quarterly statement.

I suggest freezing any large irregular money transfers between accounts. Although seemingly harmless, this will create additional questioning and paperwork to verify original sources of money. Ask your money to "say cheese", hold still and capture documents of everything when ready.

The 90-day rule also applies to money arriving from overseas. Often, money will come from overseas as a gift or own resources of the applicant from overseas with the intention of it being used for purchasing a Canadian home. For the majority of the time, the 90 day rule will apply for money arriving from all countries except the U.S or the U.K. Again, exceptions are made BUT I think it is prudent to plan for money being in a Canadian bank account for 90 days to be eligible for a home purchase down payment.

Please call me directly for customized down payment planning advice (in addition to this document).

Exceptions To The 90-Day Rule:

There are a few reasonable exceptions to the 90-day down payment verification rule. For the most part, the Mortgage industry is reasonably reasonable when looking at Mortgage application documents. There are extreme cases, but for the most part documentation requests are understandable.

Down Payment Exception: Gift Down Payment

If money is gifted to the applicant for down payment, there does not need to be a 90-day history of this money. It is possible the Mortgage lenders wish to see the source of the gift money. Proving the source simply means seeing its origin. This request is usually made with large amounts of gift money ($100,000+).

Gifted down payment also requires a gift letter to be signed and dated by the giftee and giftor. Customized gift letters are provided to you for each Mortgage lender. To verify the gifted funds are in the Mortgage applicants possession, one simple statement is required proving the gifted money is in the applicants account. That statement needs to show the date, account number/name of applicant and amount of gift money matching the same details of the gift letter.

Borrowed Down Payment:

Money from a Home Equity Line Of Credit (HELOC) is eligible to be used for down payment with most Mortgage lenders.

When qualifying for a Mortgage some lenders will apply different philosophies to their application underwriting practices. Some lenders will use the outstanding balance of the HELOC as a payment for Mortgage qualifying. Other lenders will use a payment of the entire limit of the HELOC. When planning to use your HELOC for your down payment, or a part of your down payment, be sure to understand the lenders underwriting policy.

Borrowed money from a personal line of credit is also eligible as a source of down payment with some lenders. However, when qualifying for a Mortgage in this circumstance, a very sharp eye will review the application. Additionally, the applicant has to be able to debt-service the borrowed money from the line of credit. This debt-servicing payment is higher than money borrowed from a HELOC.

Registered Retirement Savings Plan (RRSP) As Down Payment:

A first time homebuyer can use up to $25,000 of RRSP money toward the down payment of their primary residence, penalty free. The money borrowed from the RRSP has to be repaid over a minimum time period of 15 years (it can be repaid faster without penalty). Money needs to be in the RRSP for a minimum of 90-days to be eligible for down payment.

A first time homebuyer is someone who is legitimately purchasing a home for the first time. Previous homebuyers can become classified as first time buyers again IF they have been renting a home for four years after purchasing.

A bit of a grey area exists in the classification of first time homebuyers when there is small amount of co-habitation length with a partner who is a homeowner. My philosophy on the matter is this …do NOT mess around with Canada Revenue Agency. Don't do it. A homebuyer could face significant tax ramifications should the with drawl of their RRSP not be classified correctly.

PRO TIP: in some circumstances, borrowing money for an RRSP loan can help solve the problem of not having money saved for a down payment. A homebuyer can meet with a Banker for a specialized RRSP loan. This money would then be deposited into the applicants RRSP where it needs to seed for 90-days. Once the 90-days are complete, that money is eligible for down payment. This is a work around for a zero down payment Mortgage. Please consult with me to determine if your Mortgage qualifying ratios are still below the maximum for your home purchase. This is a very intricate and delicate Mortgage maneuver.

Thank you again for reading!

My name is Chad Moore and I would LOVE to help with your next Mortgage! You know, I'd just like to take a second and acknowledge you for reading this material. Most people with Real Estate ambitions don't make the time you have to educate yourself. And that's why I think you're the perfect person I can work with. I choose clients based on a common values match. Realistically, I could work with every person interested in Mortgage financing, but I don't. Why? Because I want to be the best for a smaller group of people. I think that's you. Contact me today!