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New Mortgage Rules for 2010

By Bob Carrick, Personal Finance

Home buyers are protected from their worst debt-guzzling tendencies in a package of new mortgage rules announced yesterday, while the housing market gets a mild tap on the brakes.

Unless you're a real estate investor, as distinct from your home owner, the most important of these measures amounts to this: Whatever type and term of mortgage you pick, you'll have to be able to carry the payments associated with a five-year fixed-rate mortgage, if you need government-backed mortgage insurance.

This is a sensible way of building some slack into the system as we look ahead to a cycle of rising interest rates. You can get a rate in the area of 2 per cent on a variable-rate mortgage today, but what happens when borrowing costs start their inevitable move higher? Under the new regulations, your lender would make sure you can afford payments pegged to the five-year rate.

Already, many lenders are testing borrowers to ensure they can make payments on a three-year mortgage. Starting April 19, buyers will face a little more resistance if they're inclined to follow the stupid old cliché about buying as much house as they can afford.

"Are we going to see the odd borrower have to come up with more money or not buy the house they want? Absolutely," said mortgage broker Peter Majthenyi. "But will it have a dramatic effect? No."

Toronto-Dominion Bank's economics department said that based on the national average home prices of $337,000, a buyer putting down 5 per cent would need about $9,200 more in annual income to obtain a mortgage under the new rules. On a $200,000 home, an extra $5,500 in income would be needed.

"It is clear that the regulatory change will temper demand from buyers," the bank said. "However, the impact will be constrained by the fact that many buyers may elect to still purchase, but at lower price levels."

Another reason why the changes won't be jarring is that a huge number of home buyers are actually choosing five-year mortgages these days. A study issued by the Canadian Association of Accredited Mortgage Professionals last month showed that fixed-rate mortgages accounted for 86 per cent of mortgages set up in 2009 and, of those, 70 per cent were for a five-year term.

Olympics aside, the favorite Canadian diversion of the moment is to debate whether there is a bubble in the housing market. Those most worried about the housing market plunging have urged Mr. Flaherty to raise the minimum down payment for a home and reduce the maximum payback period.

But the 35-year amortization, favourite of first time buyers across the land, remains. So does the 5 per cent down payment, which is heavily relied upon in high-cost cities like Vancouver, Calgary and Toronto.

Hardest hit by the new measures are buyers of what the government describes as “non owner-occupied properties purchased for speculation.” Flippers of real estate are included here, as are people who buy properties for rental income. They’ll have to put down a minimum of 20 per cent to qualify for mortgage insurance, up from 5 per cent.

Real estate speculators typically like to put down as little as possible, so this measure may curb some activity. But Mr. Majthenyi said he has found that stiff mortgage insurance premiums already discourage people from putting 5 per cent down on an investment property.

The third new mortgage measure restricts the ability of existing homeowners to refinance their mortgages to take on more debt. The new ceiling is 90 per cent of the value of your home, compared with the current 95 per cent.

Mortgage broker Jas Grewal said one group that will be affected is recent buyers who made a small downpayment and are struggling with high credit-card balances and other debts. By folding these debts into their mortgage, they can reduce their interest rate from as high as 19 per cent down to something closer to 3 or 4 per cent.

“Let’s say you put 10 per cent down - if we go from 95 to 90 per cent, you’re not going to be able to refinance,” Mr. Grewal said. “You’re going to have to wait until your house value goes up and gives you some equity.”