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Glossary of
Mortgage Terms

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0/40 Mortgages
An abbreviation for $0-down and/or 40-year amortization mortgages.

ABCP (Asset Backed Commercial Paper)
ABCP is a package of debt -- anything from mortgages, to car loans to credit card debt. Typically, ABCP is backed by a major bank and sold to others. Banks generally agree to buy back the ABCP in the event no one else will.

According to the Financial Post:
A bank packages a collection of mortgages, credit card balances, or lines of credit into an ABCP that matures in 30 days. - The bank sells ABCP for a fee to an intermediary that assumes all the risk associated with the underlying assets. - The intermediary sells pieces of the ABCP to investors, including pension funds or corporations or individuals. - Investors are paid interest and assume there will be a buyer for their piece of the ABCP after 30 days. - For a fee, the bank supplies funds to buy the ABCP if there are no other buyers.
Note that, in Canada, this last feature did not work in August 2007 during the ABCP crisis. Investors were therefore left without any buyers and the ABCP market crashed. Before 2007, ABCP was quite popular. A wide range of institutional investors bought it because it offered higher returns than other reasonably "safe" investments.

All-in-One Mortgage
All-in-one mortgages let you co-mingle savings and a mortgage in a single account. Your savings reduces your mortgage balance so that you're charged less interest. Interest on all-in-one mortgages is usually calculated daily. That ensures deposits into the account (like your paycheque) immediately reduce your debt to save more interest.

Alt-A Mortgages
Alt-A mortgages are mortgages that are more risky than prime but less risky than subprime.

Amortization
Amortization, referred to as "am" by mortgage professionals, refers to the process of paying off a mortgage in regular payments composed of both interest and principal. The "amortization period" is the time over which the mortgage is to be completely repaid, assuming equal payments.

A mortgage with a 25-year amortization period, for example, means that it would take 25 years to reduce the balance to zero. That assumes all regular payments were made on time and the terms (payment and interest rate) remained the same.

An "amortization schedule" is a table showing the amounts of principal and interest in each mortgage payment, as well as the remaining principal balance after each payment is made.

Amortization Schedule

A table, or schedule, providing the amount of principal, interest and the balance of the debt in regular installments over a period of time.

Assignment

The transfer to another of a right, interest, or title to property.

Assumability (Mortgage Assumption)

An assumable mortgage can be taken over (assumed) by the buyer of a property when that property is sold. The buyer must typically apply and qualify for the mortgage in order to assume it. If approved by the lender, the buyer then takes over the mortgage payments and receives the seller's existing mortgage rate and terms.

Mortgage assumptions have benefits:

- If the seller's mortgage has a below-market interest rate, the buyer can save some money
- If the seller has paid for mortgage default insurance, the buyer may pay insurance premiums again. This is relevant when the new buyer is putting less then 20% down.

If you're considering assuming a mortgage, make sure that:

- The mortgage terms, features, and restrictions are to your liking
- The rate is sufficiently low compared to current alternatives
- There is enough time remaining on the mortgage to make it worthwhile

These days, most (but not all) lenders offer assumption privileges.

B Lending (Subprime Lending)

Mortgages are typically classified based on the payment risk that the lender faces. Prime mortgages (also known as "A" deals) entail lower chances of the borrower defaulting than non-prime mortgages (aka., subprime or "B" deals).

"B" mortgages are riskier so lenders rely heavily on the equity in the subject property and/or on charging rate premiums to mitigate that risk.

Bankable

An applicant or project that is acceptable to a bank for financing purposes.
For residential borrowers, this generally means someone with a 600+ credit score, satisfactory credit and who falls within normal underwriting guidelines.
For commercial deals, this means a project or proposal that has sufficient collateral, future cash flow, competent management and a good probability of success.

Bankers' Acceptance (BA)

A bankers' acceptance (BA) is a short-term credit investment created by a non-financial firm and guaranteed by a bank. BA's are frequently used to finance the lending activity of Canadian banks.

30-day bankers' acceptance rates are also correlated with variable-rate mortgage discounts since lenders factor in BA yields when setting variable pricing.

Basis Points (bps)

A basis point is 1/100 of a percent. 50 basis points therefore equal ½%. The basis point is commonly used for calculating changes in mortgage rates and bond yields.

BDM

BDM stands for "Business Development Manager."
In the mortgage industry, BDMs most commonly work for lenders. Their role is primarily to generate new business and support existing business partners (e.g., brokers).

BFS (Business for Self)

Business-for-self is mortgage lender lingo for "self-employed."
Canadian mortgage default insurers and lenders each have their own specialized BFS programs. These programs often allow self-employed borrowers to qualify for a mortgage without the typical documentation requirements of a salaried individual. This is done to allow flexibility for BFS applicants who may have business deductions or other circumstances that make their income hard to qualify.

Big Six Banks (Big 6)

The term "Big 6 Banks" refers to Canada's six largest banks. They are (alphabetically):

- Bank of Montreal (BMO)
- Canadian Imperial Bank of Commerce (CIBC)
- National Bank of Canada (NBC)
- Royal Bank of Canada (RBC)

- Scotiabank
- TD Bank

Blended Rate

This is the rate that results from the blending of an existing mortgage and a new mortgage with differing interest rates into one consolidated mortgage.
The calculation to determine the final blended rate takes into account both the interest rates and the amount of principal for each of the component loans.
Often, a lender will offer a blended rate if the borrower chooses to break his/her mortgage early and refinance. Beware that such blended rates often include a penalty built in. A mortgage planner can calculate if it makes more sense to pay the whole penalty and refinance elsewhere at a lower rate. It often does.

Bond Yields

A bond yield is the percentage return that an investor will receive on holding a bond to maturity

Breaking a Mortgage

Breaking a mortgage is the act of terminating a mortgage early, before maturity.
Breaking a mortgage typically results in a mortgage penalty when the mortgage being broken is a "closed" mortgage.

Bulk Insurance (a.k.a. Portfolio Insurance)

Bulk insurance, also known as portfolio insurance, is a type of mortgage default insurance.
Lenders buy bulk insurance on their low-ratio mortgages for three reasons:

- Capital relief (lenders need to maintain less capital for mortgages that are insured)
- Risk reduction (bulk insurance covers the lender in the unlikely scenario that a borrower with 20%-plus equity defaults and the lender can't recover its principal)
- Securitization (insured mortgages are easier package up and sell to investors)

CMHC summarizes portfolio insurance as follows:
"Portfolio insurance helps lenders manage their capital more efficiently and small lenders to compete on an equal footing with large lenders. It allows more lenders to compete in the mortgage loan insurance market by lowering entry barriers, thus expanding consumer choice."

Buyers' Agent

A real estate agent that represents the buyer in a real estate transaction.

"Canadas" (GoC's)

"Canadas" or "GoCs" (Government of Canadas) are short form for "Canadian government bonds."

Charge

The name given to a mortgage document when title is registered under the Land Titles System. Also known as Certificate of Charge.

Closed Mortgage

A mortgage agreement that cannot be repaid, refinanced or renegotiated until maturity, unless otherwise stated in its terms.
In practice, most closed mortgages can be broken before maturity if you pay a penalty, but not all.

Co-Borrower (Co-Signor)

A co-borrower is an additional mortgage applicant that can help you qualify for a mortgage. A co-borrower is on title and responsible for the mortgage payments, along with all other applicants. A co-borrower is different than a guarantor.

Collateral Charge

A collateral charge is basically a different method of securing a mortgage or loan against your property.

It differs from a standard (traditional) mortgage in some very important ways:

1. Unlike a standard mortgage, a collateral charge is readvanceable — That means the lender can lend you more money after closing without you needing to refinance and pay a lawyer.
2. A collateral charge is non-transferable — It cannot be assigned (switched) to a new lender like a regular mortgage.

In addition, regular mortgages put all of their key terms in a document that's registered with your provincial land title/registry office. A collateral mortgage, however, puts key terms in a loan agreement which is not registered in the same way.
That collateral loan agreement may therefore contain terms that other lenders are not aware of, or might find objectionable. For that and other reasons, lenders don't accept transfers from borrowers with collateral charges. Instead, the borrower must refinance in order to switch lenders, and that entails legal costs.

Collateral charges also allow lenders to do things like change your interest rate, increase your loan amount, and use your mortgage payment to pay down other debts you have with that lender (if you default on those debts).

If you're considering a collateral charge, have a mortgage planner explain the pros and cons before you jump in.

Construction Draw Mortgage (Builder Loan)

A loan designed for borrowers who need financing for construction projects. These differ from normal loans as the funds are received in stages (also known as draws) during the building process to protect the lender from construction abandonment.

Contract Rate

The contract rate is the actual mortgage rate you agree to in your mortgage contract. This is the rate your payments are initially based on.

Conventional Mortgage

A conventional mortgage does not exceed 80% of the market value of the property. This means that the borrower must have 20% or more available for the down payment. Unlike most high-ratio mortgages, conventional mortgages are not required by law to carry mortgage default insurance.

Conversion Rates

A "conversion rate" is the interest rate your lender offers you when you convert from one mortgage term to another.
Conversion rates apply when you convert from a:

- Variable rate to a fixed rate
- Convertible term to a fixed or variable term
- Line of credit to a fixed or variable term

Conversion rates are rarely as good as the rates lenders offer on "new business." Five-year fixed conversion rates, for example, are often 20 basis points more than the five-year rate a new customer can get from that same lender.
Usually, conversion rates are one of the following:

- A set amount below posted rates
- A negotiated rate at the time of conversion
- A pre-defined discounted rate
- The lender's "broker rate."

Broker rates are typically the lowest of the above options but it depends on the lender.
Tip: If you're converting from a variable to a fixed rate, the term of the new fixed mortgage must often be at least 3-5 years (depending on lender).

Convertible Mortgages

Mortgages with a convertible rate feature allow borrowers to move into a fixed rate at any time with no penalty.
There are also a few 1-year fixed mortgages that can be converted to either a fixed *or* a variable rate.
When converting, you generally need to choose a new term that is at least as long as the term you have remaining.
Variable-rate and short-term fixed-rate mortgages are commonly offered with a convertible feature. In the case of variables, you can only convert into a fixed rate.

Debt Ratios (GDS / TDS Ratios)

Lenders have long relied on two standard measures of one's "ability to pay" their mortgage:
Gross Debt Service (GDS): The percentage of the borrower's income that is needed to pay all required monthly housing costs (mortgage payments, property taxes, heat and 50% of condo fees).
Total Debt Service (TDS): The percentage of the borrower's income that is needed to cover housing costs (GDS) plus any other monthly obligations that an individual has, such as credit card payments and car payments.
The acceptable ratios for both have generally been 32% and 40% respectively.
For people with very high credit scores, GDS requirements are often waived and the TDS maximum is slightly higher (44% as of January 2011).

Discretionary Rate

A preferable mortgage rate that is not disclosed to a borrower up front.
Banks and credit unions often use discretionary pricing models to maximize profit. In practice, such lenders advertise higher rates and then lower them based on a customer's:

- Application characteristics
- Negotiating skill, and
- Business with that institution.

Dual Agent

Dual agency refers to the situation where the agent represents both the buyer and the seller at the same time.

Two different real estate sales representatives from the same Real Estate brokerage would also be considered dual agency.

Effective Rate

The term "effective rate" is used in two ways. It can refer to:

1. The actual rate that the borrower must pay on a loan after the effects of compounding are considered (This makes it different from the *nominal interest rate*.), and/or
2. The rate that reflects the borrower's actual borrowing cost, after accounting for any cash back that is received.

Equity Lender

A lender who lends primarily based on the value of the property (i.e the security). Equity lenders often put less emphasis on a person's credit and income.

Loan-to-values are usually lower at an equity lender to offset the higher risk.

Equity Mortgage

A mortgage where approval is based predominately on the amount of equity in a property, and its marketability. Traditional income confirmation is usually not required.
Prime lenders also rely on the applicant's credit history and score. Non-prime lenders don't care as much about the applicant's credit history.

Equity lending is more risky. Therefore, loan-to-values rarely exceed 75-80%.

Equity Mortgage (Equity Lending)

A mortgage where approval is based predominately on the amount of equity in a property, and its marketability. Traditional income confirmation is usually not required.
Prime lenders also rely on the applicant's credit history and score. Non-prime lenders don't care as much about the applicant's credit history.

Equity lending is more risky. Therefore, loan-to-values rarely exceed 75-80%.

Equity Take-out

The act of refinancing a mortgage to take money out of a property with sufficient equity.

Front-loaded Mortgages

Front-loaded mortgages feature a deeply discounted rate for an initial "teaser" period—often 6-12 months. After that, the mortgage reverts to a higher rate.
Lenders in the past have offered 5-year front-loaded variable mortgages where the first year is at prime – 1.00%, for example, followed by prime – 0.60% in years 2-5.
Front-loaded variables are popular with borrowers who want the lowest rate possible for 6-12 months, knowing that they plan to lock into a fixed rate thereafter.

Guarantor

A person who will make repayments on a mortgage if the borrower(s) default. Guarantors must be able to cover the entire mortgage payment by themselves. Guarantors are sometimes necessary when the original applicant(s) have enough income, but have insufficient or imperfect credit. Unlike co-borrowers, guarantors are not on title to the property.

High Ratio Mortgage

A mortgage with a loan-to-value over 80%. In other words, a mortgage where the borrower has put down less than 20%. In Canada, most high ratio mortgages have to be insured against default. This requires the borrower to pay mortgage default insurance premiums to an insurer like CMHC, Genworth, or Canada Guaranty.

Hold The Payment

"Hold-the-payment" is a feature that lenders sometimes offer with their variable rate mortgages.

Generally, if you have a variable-rate mortgage, and prime rate increases, your monthly payments will also increase.

If you've got a hold-the-payment feature, your payments would instead remain the same.* (However, the portion paid to interest would increase.)

Hold-the-payment options help people budget better for their mortgage payments and have become very popular.

** If prime rate rose to a point where your monthly mortgage payments were insufficient to pay the interest due, your lender would increase your monthly payments regardless of any hold-the-payment feature.*

Home Equity Line of Credit (HELOC)

Home equity lines of credit (HELOCs) are essentially revolving lines of credit secured against one's home.

Or, to put it another way, a HELOC is a mortgage loan that lets the borrower take multiple advances of the loan proceeds at his or her own discretion, up to the lender's stipulated maximum loan-to-value. Borrowers only pay interest on the money they use.
The maximum loan-to-value of a HELOC in Canada is typically 75-80% of a property's value.

One big difference between a HELOC and a variable-rate mortgage is that HELOC's do not have guaranteed interest rates or terms. Their rate can technically change at the lender's discretion.
A variable-rate mortgage, on the other hand, almost always has a rate that is tied to the lender's prime rate. So if prime does not change then one's variable mortgage rate will generally not change.

There are other key differences as well, both positive and negative. Speak with a licensed mortgage planner for a complete comparison.

Hybrid Mortgage

A hybrid mortgage is a mortgage with multiple terms. These terms may be part fixed and part variable, and/or part long-term and part short-term.

For example, a hybrid mortgage might be contain the following:

- 50% in a 5-year fixed rate
- 50% in a 5-year variable rate

As another example, a hybrid might contain:

- 20% in a 3-year fixed rate
- 30% in a 5-year variable rate
- 50% in a 1-year fixed rate

Interest Adjustment Date

Mortgage payments are made in arrears. In other words, when each payment period is over, lenders look back and calculate their interest based on the money you owed during that period.

The interest adjustment date is the date from which your lender first starts calculating the normal ongoing interest that you'll pay.
Interest adjustment dates tend to commonly fall on the 1st day of the month *after* mortgage funds are advanced to the borrower.

For example, suppose you close your mortgage on April 25 and have signed up for monthly payments. Here is how the dates might stack up:

April 25: Mortgage starts (a.k.a. the closing date)
May 1: Interest adjustment date
June 1: First payment date

Your first payment on June 1 will therefore be based on the interest that accrued since your interest adjustment date (i.e. from May 1 to May 31). If you plan to make bi-weekly payments, then instead of one month after, your first payment would be two weeks after

the interest adjustment date. Before the interest adjustment date, however, you will have held the lender's money for a period of time. In the example above, this period would have been April 25 to April 30. Lenders like to get paid for this time. As a result, lenders charge a one-time amount of pro-rated interest to cover it. This interest-only payment is called an "interest adjustment." It compensates the lender for the time you held their money *before* your first official payment period began.
Lawyers and notaries routinely collect interest adjustments at closing. Confirm this when you discuss your closing costs with them.

Keep in mind, it is possible to avoid interest adjustments altogether. To do so, you need to schedule your first mortgage payment exactly one payment period (e.g. one month) after your closing date.

Interest Offset Mortgage

An interest offset mortgage combines deposits and a mortgage in one line of credit account. When the homeowner deposits funds (like a paycheque) into the account, that decreases (offsets) the principal owed--and hence the interest owed. Unlike most mortgages, offset mortgages calculate interest daily as opposed to monthly. That ensures deposits immediately offset debt, with the aim being greater interest savings.

(Note: The process also works in reverse. Whenever you borrow more from the account, interest starts being calculated the same day.)

National Bank's All-in-One and Manulife's One are two popular examples of offset mortgages.

Interest Rate Differential (IRD)

The IRD is a compensation charge that may apply if you pay off your mortgage prior to the maturity date, or pay the mortgage principal down beyond the amount of your prepayment privileges.

The IRD is based on:

- The amount you are pre-paying; and,
- An interest rate that equals the difference between your original mortgage interest rate and the interest rate that the lender can charge today when re-lending the funds for the remaining term of the mortgage.

Most closed fixed-rate mortgages have a prepayment penalty that is the higher of 3-months interest or the IRD. Most variable-rate mortgages do not have IRD penalties.

The "Comparison Rate" is the lender's rate for the term most closely matching your remaining term. For example, if you have 22 months remaining, it is common for lenders to use the posted rate of their 2-year term as the comparison rate.

Things to note…

- Each lender has its own formula for calculating penalties.
- Some lenders do not use the discount you received in their calculation, which decreases the IRD and can lower your penalty considerably.
- When determining the comparison rate, some lenders round up your remaining months to the next longest term. Some round down.
- The Interest Act prohibits IRD penalties on terms over 5 years, *after* five years has elapsed. In such cases, a maximum 3-month interest penalty may apply. For example, someone who has been in a 6-year mortgage for 60 months or more would pay a 3-month interest penalty (maximum) to break it before maturity.
- A small number of lenders prohibit breaking a mortgage early—regardless of the penalty—unless in the case of an approved bona fide sale.
- The moral: Always contact your lender directly for an exact penalty quote.

Land Titles System

Where title to the land is registered. Land title records are held by the Land Registry Offices Registration of real property is done under either the *Land Titles Act* or the *Registry Act.* All registered and deposited records are held by the Land Registry Offices and are available for search of title or obtain information about the ownership of real property.

Lending Spreads

Lending spreads are the difference between a lender's cost of funds and what that lender sells a mortgage for.

For example, a lender may be able to raise capital in the mortgage backed securities market at 4.00% and sell a mortgage to the borrower at 5.50%. That 1.50% difference is the "spread."

When investors perceive added risk (or less return) in the mortgage market, spreads tighten. As a result, profit for lenders decreases and mortgage rates often go up to compensate.

Lending Value

Lending value is the property value for mortgage purposes. It's usually, the lesser of appraised value or sale price.

That said, insurers and/or lenders may assign a lending value that is less than the appraised value or sale price if they deem it necessary to mitigate risk.

Listing Agent

The real estate agent representing the Seller (or Seller's Agent). The listing agent "lists" the house for sale, typically on MLS.

Loan-to-Value Ratio (LTV)

Loan-to-value ratio (LTV) is the amount of the mortgage loan compared to the value of the property.

This ratio is calculated by the lender prior to providing a mortgage. The results of this calculation help to determine whether or not the applicant will qualify for a loan and whether the application, if approved, will be for a conventional loan or a high ratio loan.

Here is an example. Assume:

Property Value = $100,000
Down Payment = $10,000
In this case the LTV = **90%**

The calculation used is simple: 1 - (down payment / property value)
Or in our example: 1 - ($10,000 / $100,000)

Low-Ratio Mortgage

A mortgage loan that is no more than 80% of the value of a home.
Low-ratio mortgages are sometimes referred to as "conventional mortgages."
Unlike most high-ratio mortgages, low-ratio mortgages are not required by law to carry mortgage default insurance. However, lenders often insure them anyway to lower their risk.

Maturity

The end of a mortgage's term.

Modern Era of Monetary Policy

The modern era of monetary policy in Canada can be thought to have started in February 1991. That's when the Bank of Canada began its formal policy of inflation targeting. That mandate gave the Bank one overriding objective: keep inflation near 2%. This 2% target has governed the Bank of Canada's rate setting policy ever since.

Monoline Lender

A "monoline" is a mortgage lender that focuses just on mortgages. A monoline lender does not have other products it can cross-sell, which differentiates it from a bank or credit union.

Most monoline lenders securitize their mortgages, instead of keeping them on their balance sheet.

Mortgage Arrears

A mortgage is in "arrears" when the borrower is behind on one or more payments.
In Canada, arrears statistics typically measure the number of Canadians who are 90 days or more past due on their payments.

Mortgage Assignment (Switch)

Also known as an "assignment of charge," a mortgage assignment is a transfer of mortgage ownership from one lender to another.
Assignments are typically used when a homeowner's mortgage wants to "switch" ("transfer") his/her mortgage to a new lender. The new lender often accepts the transfer with no legal fees required.

With an assignment, it's important to remember that the key terms of the mortgage (e.g. the mortgage amount, amortization and loan-to-value) may not be increased.
If a borrower wishes to change lenders and also change the key terms of his/her mortgage, then an assignment typically cannot be used. In that case, a refinance is usually required (with the aid of a lawyer).

If you're doing a "straight switch" of a regular mortgage you'll often pay nothing but your existing lender's discharge fee to change lenders.
If any of the following are true, then it's possible that you'll have to refinance to change lenders (which involves legal/registration costs):

- Your mortgage is a collateral charge or a readvanceable mortgage, instead of a standard charge
- You're transferring into an open, 1- or 2-year fixed (some lenders don't pay switch costs for shorter terms)
- Your old lender is not on your new lender's "free switch" list
- You want to use your own lawyer to close instead of the lender-appointed closing company (lenders commonly use title companies to close, like FNF or FCT)
- Your loan amount, amortization, or loan-to-value is increasing

Mortgage Debt Ratios

Lenders have long relied on two standard measures of one's "ability to pay" their mortgage:
Gross Debt Service (GDS): The percentage of the borrower's income that is needed to pay all required monthly housing costs (mortgage payments, property taxes, heat and 50% of condo fees).
Total Debt Service (TDS): The percentage of the borrower's income that is needed to cover housing costs (GDS) plus any other monthly obligations that an individual has, such as credit card payments and car payments.
The acceptable ratios for both have generally been 32% and 40% respectively.
For people with very high credit scores, GDS requirements are often waived and the TDS maximum is slightly higher (44% as of January 2011).

Mortgage Insurance

Also called mortgage default insurance, this is insurance that protects the lender in case the borrower defaults on his or her mortgage payments. If an insured mortgage is in default, and the lender can't collect from the borrower, the insurer pays the lender back.

Mortgage default insurance is required by most lenders whenever a homeowner puts down less than 20%. The biggest mortgage insurers in Canada are CMHC, Genworth, and Canada Guaranty--in that order.

Mortgage insurers charge premiums to borrowers to cover the insurance expense. These fees can range from less than 1% to over 5% of the principal value, depending on the borrower's mortgage type, loan-to-value, property type, and amortization.

The insurance premiums are typically added to the mortgage at the time of closing. While possible, they are rarely paid in advance.

Mortgage Maturity

Maturity means the end of a mortgage term.

A maturity date is therefore the date when the principle balance of a mortgage comes due.
Once your mortgage matures, you can either pay it all off or renew it.
Most lenders send out renewal letters 30-60 days before maturity.
Tip: Never sign a renewal letter without having a mortgage planner present all your options. Very often you'll find better deals by switching to another lender.

Mortgage Originator

An institution or individual that works with a borrower to complete a mortgage transaction.

Mortgage Portability

A "portable" mortgage comes with an option that allows the borrower to transfer the mortgage to a new property (typically subject to credit approval and a property appraisal). The benefit is that the borrower avoids paying a penalty to break the mortgage early. The homeowner also gets to keep his/her present interest rate after moving.
If a borrower moves and buys a more expensive house, many lenders will permit a "port and increase." In other words, the lender will port the mortgage and increase the amount. The borrower gets the lender's current rate on the "new money," and that rate is then typically blended with the rate on the *existing* mortgage.

Mortgage Prepayment

A mortgage payment that is optional and made earlier than necessary.

Mortgage prepayments are applied directly to principal, thus saving you interest for the remainder of your amortization period.

Mortgage Term

In a mortgage, term is the length of time a lender agrees to lend its money. It is also the length of time for which the loan's interest rate is "guaranteed." Put another way, term is the length of one's mortgage agreement.

The term is usually shorter than the amortization period. At the end of the term the outstanding debt must either be refinanced at current market rates or paid off in full.

Mortgage Terms

The specific details regarding your mortgage including any fee/costs associated with the product and lender you have chosen

Mortgagee

A person who holds mortgaged property as security for repayment of a loan

Mortgagor

In a mortgage, "mortgagor" is another name for the borrower.

Negative Amortization

A situation where your mortgage payment is not enough to cover the interest due. The interest then builds up and your principal *increases* instead of shrinking.

Negative amortization can occur when you have a fixed-payment variable-rate mortgage and prime rate rises significantly.

Negative Equity

A situation where your mortgage balance is greater than the value of your home. This can occur when you make a small down payment (e.g. 5%) and home prices drop considerably.

Negative equity is problematic for people who can't meet their mortgage payments. That's because it eliminates the option of selling ones home to repay the mortgage in full.

Notice of Assessment (NOA)

An NOA is an annual statement sent by Canada Revenue Agency (CRA) to taxpayers detailing their tax account.

An NOA includes a taxpayer's:

- Income tax owed
- Income tax already paid
- Tax refund amount
- Tax credit amount
- Allowable contribution to a Registered Retirement Savings Plan (RRSP)

O.A.C.

OAC stands for "on approved credit."

Open Mortgage

A mortgage term whereby you can make prepayments at any time during the term, or even pay the mortgage off completely before the end of the term, without having to pay any penalty.

Origination

Origination refers to the day a mortgage closes. It can also refer to the process of arranging a mortgage transaction.
See also: Mortgage Originator

Overnight Index Swap (OIS)

An overnight index swap (OIS) is an over-the-counter* derivative in which two parties agree to exchange, or swap, for an agreed period, a fixed interest rate determined at the time of the trade for a floating rate** that will vary over time.

Market participants predominantly use the OIS market for hedging activities, which are often related to risk management. Specifically, participants can use the OIS to hedge either their funding costs or their exposure to short-term interest rate movements.

The OIS market can also be used to alter the term structure of a portfolio or for taking a speculative position on the future path of the Bank of Canada's target overnight rate. (Overnight index swaps provide a gauge of what the overnight rate is expected to average over a given period.)

Related to the speculative and hedging functions of the OIS, the fixed-rate portion is also used by some market participants to derive market expectations of the Bank's future policy rate changes. If the duration of the swap extends over a Bank of Canada interest rate meeting, for example, the difference between the fixed rate and the current overnight rate can be used to calculate the market expectations of a future change in policy rates.
The OIS has several advantages over other money market instruments in calculating expectations. Unlike other financial instruments, it is directly linked to the Canadian overnight rate. Furthermore, given that they are derivatives instruments, the supply of OIS contracts is not fixed. Supply factors can occasionally influence the pricing of other instruments, such as bankers' acceptances (BAs).

The use of the OIS market to gauge expectations also presents some challenges. At times there is a lack of price information or market depth in the OIS market, particularly in farther-dated contracts. Moreover, if the CORRA rate were expected to deviate from the overnight target, gauging expectations of future interest rates would become more difficult.

** Over-the-counter trades occur directly between participants and not through a centralized exchange.*
*** The floating rate of an OIS is the Canadian Overnight Repo Rate Average (CORRA) over the period.*

Payout Date (Discharge Date)

The date a mortgage is paid in full and discharged, thus releasing the borrower from all obligations and covenants contained in the mortgage.

Payout Statement (Discharge Statement)

A statement given by a lender (mortgage holder) to the mortgagor (borrower) setting out how much must be paid to discharge the mortgage.

Percentage Points (pp)

"PP" is an abbreviation for percentage points.

Pre-Qualify / Pre-Approve

Pre-qualifying is a process whereby a mortgage professional informally determines the maximum amount an individual is eligible to borrow.
The mortgage advisor typically:

- Reviews the borrower's application and credit
- Calculates the debt ratios
- Confirms the borrower meets the chosen lender's guidelines
- Provides an informal list of financing conditions
- Provides a rate hold for 90-180 days (this is optional)

A pre-qualification is different from a pre-approval.

A pre-qualification is quicker and the lender itself does not review the borrower's application.

With a pre-approval, the lender provides a rate guarantee on the assumption that the borrower meets its guidelines. The lender will often (but not always) review the application—in part or in full.

In addition, pre-approvals sometimes involve a more thorough check of the borrower's credit and documentation (by the mortgage advisor, not the lender).

Primary Dealer

A government securities distributor whose participation in the primary and secondary markets for Government of Canada securities is above a certain threshold level.
As of this writing, the primary bond dealers in Canada include:

- BMO Nesbitt Burns Inc.
- Casgrain & Company Limited
- CIBC World Markets Inc.
- Desjardins Securities Inc.
- Deutsche Bank Securities Limited
- HSBC Securities (Canada) Inc.
- Merrill Lynch Canada Inc.
- Laurentian Bank Securities Inc.
- National Bank Financial Inc.
- RBC Dominion Securities Inc.
- Scotia Capital Inc.

Prime Mortgages (aka. "A" Mortgages)

"Prime" is a classification of lending based on the payment risk that the lender faces. Prime mortgages (also known as "A" deals) entail lower chances of the borrower defaulting than non-prime (aka., sub-prime or "B") mortgages.

Prime Rate

A reference interest rate used as a basis for quoting other lending rates, like those of variable-rate mortgages and lines of credit. Prime rate used to be the rate at which financial institutions lent to their best customers. This is no longer necessarily the case.

Prime-BA Spread

The "prime-BA spread" is simply prime rate minus the 30-day bankers' acceptance yield. In raw terms, it represents gross lender margins on variable-rate mortgages.
From this spread, lenders have to pay liquidity/risk premiums (when raising lending capital in the credit markets), customer acquisition costs, overhead, salaries, etc. The remainder is profit.

Property Title Search

A property title search is a search conducted to look for outstanding encumbrances and title deficiencies as well as to confirm the owners name and state of land tenure, so that when a purchaser buys a property, the encumbrances and deficiencies are removed from title and the purchaser would have clear title.

Qualifying Rate

Mortgages with variable rates or fixed terms under five years typically require that you qualify at a higher rate (called the "qualifying rate.").
For example, if you apply for a 2.25%, 5-year variable mortgage, the lender might make you qualify at their posted 5-year rate (5.39% for example).
Qualifying rates are used to ensure borrowers can handle their payments if rates go up.
In practice, lenders use the qualifying rate to calculate your debt service ratios. Lenders then check to ensure your debt ratios are low enough to meet their guidelines.
Here are a few things to keep in mind:

- Your payments are typically based on the contract rate (i.e., the regular rate you are quoted), not the qualifying rate.
- As of April 19, 2010, all insured variable and 1- to 4-year fixed mortgages over 80% loan-to-value must be qualified using the posted 5-year fixed rate, as published every Wednesday by the Bank of Canada.
- Some lenders also apply the Bank of Canada qualifying rate to uninsured mortgages, and mortgages with a loan-to-value of 80% or less.

- Other lenders allow lower qualifying rates if the loan-to-value is 80% or less (e.g. they use a 3-year discounted fixed rate instead of the posted 5-year fixed rate).

Quick Close

A term used to describe a transaction that closes within a short period of time, typically 30-45 days. Discounted rates are offered for quick closings due, in part, to the lower cost of hedging rates for a shorter period.
By way of example, a lender's best 5-year fixed rates might be as follows:

- 5.49% with a 120-day rate hold
- 5.39% with a 60-day rate hold
- 5.19% with a 30-day rate hold

Rack Rate

A "rack rate" is colloquial expression for a mortgage rate that is not sufficiently discounted. People who simply sign their lender's renewal form, for example, are often given the lender's rack rates (i.e. rates that are higher than the lender's best rates). The term is derived from hotel parlance, where "rack rate" describes a hotel's full published rate without discounting. Almost no one pays rack rates today unless they fail to shop around, or cannot qualify with discount lenders.

Readvanceable Mortgage

(*see also reverse mortgage*) A readvanceable mortgage is a mortgage designed to provide income to seniors with home equity. A reverse mortgage does not require a set payment schedule. You can make monthly interest payments if you choose, but most people opt to pay back the mortgage when they sell their home.

Once you get a reverse mortgage, even if you never make a single payment, the lender cannot take your home. Moreover, you'll never owe more than your home is worth, even if it depreciates.

Since a reverse mortgage is a loan, the money you receive is tax-free and doesn't affect other retirement benefits.

Rent To Own

A contract whereby the tenant will be the future buyer of the home. Details regarding the amount of money set aside to be contributed towards the down payment of the home, the purchase price of the home after an agreed amount of time, and other details regarding missed payments, repairs to the home, etc. are set out in the contract.

Rental Add-Back

"Rental add-back" is the percentage of rental income a borrower receives that the lender is willing to use to qualify him/her for a mortgage. Rental add-back can range from 50%-100% on conventional mortgages. This percentage of rental income is *added* to the borrower's income to determine his/her debt ratio.

Here's an example of how rental add-back is used to calculate a borrower's total debt service (TDS) ratio:

___ _________ PITH + Other Debts___ ________Borrower's Income + (Rental Addback x Rental Income)

PITH = Principal, interest, property taxes, heat, and 1/2 of condo fees. PITH generally takes into account housing costs from all the borrower's properties.

Keep in mind, lenders have many different forumulas for calculating debt ratios with rental income, so check your lender's guidelines.

Rental Offset

"Rental offset" is the percentage of rental income a borrower receives that the lender is willing to use to qualify him/her for a mortgage. Rental offset is typically 50-80%, with a limited number of lenders allowing up to 100% on conventional mortgages. This percentage of rental income is *deducted* from the borrower's debts to determine his/her debt ratio.

Here's an example of how rental offset is used to calculate a borrower's total debt service (TDS) ratio:

PITH + Other Debts - (Rental Offset x Rental Income)
Borrower's Income

PITH = Principal, interest, property taxes, heat, and 1/2 of condo fees. PITH generally takes into account housing costs from all the borrower's properties.

Keep in mind, lenders have many different forumulas for calculating debt ratios with rental income, so check your lender's guidelines.

Restrictive Term

A highly inflexible type of closed mortgage term. Generally, a restrictive term mortgage cannot be broken before maturity unless you sell your home. Some restrictive term mortgages let you renegotiate early, but only if you do so with the lender that has the mortgage.

Reverse Mortgage

A **reverse mortgage** is a mortgage designed to provide income to seniors with home equity.

Unlike a traditional mortgage, a reverse mortgage does not require a set payment schedule. You can make monthly interest payments if you choose, but most people opt to pay back the mortgage when they sell their home.

Once you get a reverse mortgage, even if you never make a single payment, the lender cannot take your home. Moreover, you'll never owe more than your home is worth, even if it depreciates.

Since a reverse mortgage is a loan, the money you receive is tax-free and doesn't affect other retirement benefits.

Here are some basic reverse mortgage guidelines:

- You must be 55 or older and own an eligible home or condo
- Depending on your age and the property, you may qualify for up to 50% of the value of your home.

Sample uses of reverse mortgages:

- Supplementing retirement income
- Helping grandchildren with educational expenses
- Home renovations
- Eliminating existing debts to improve monthly cash flow
- Personal use (travel, recreation, etc.)
- Purchase of investment or recreational properties

Costs for setting up a reverse mortgage include appraisal, legal, and lender fees. Budget on $2,300, give or take.

Increasingly, people are using reverse mortgages to purchase income-producing investments. This is typically done to supplement their retirement income and generate a tax deduction.

It should also be noted that a line of credit (LOC) is often a cheaper alternative than a reverse mortgage. The problem is, some people don't qualify for a LOC due to insufficient income, non-employment, credit issues, debt ratios, etc. Moreover, a LOC requires monthly payments whereas a reverse mortgage does not.

Some lenders let you qualify for a LOC based primarily on the equity in your home. This option is not without risk, however:

- Seniors have been known to tap out their LOCs and get into a position where they have no more capacity to borrow. The worst case would be borrowing over 40-50% of your equity, not being able to make payments, not being able to refinance, and losing your house.
- Banks can shut off the tap at any time due to missed payments (even if accidental), a deceased spouse, or years of steadily growing debt with no principal reduction.
- Banks can also reduce your available borrowing limit or raise your interest rate

Other alternatives to a reverse mortgage include:

- Selling your home and downsizing, renting or moving in with family
- Selling other investments or real estate
- Cashing in on an uneeded life insurance policy

- Government assistance for low-income seniors
- Borrowing from another, with your property used as collateral
- Getting a roomate or renter to offset some of your home costs
- Property tax deferral (available in some locations)

People get reverse mortgages because they want to remain in their homes, can't make payments, are under/unemployed with minimal cash flow, and have no better solutions. Yes, reverse mortgages can eat up your equity, but this accelerated equity loss is a secondary concern for people with these challenges.
Some people even get reverse mortgages because they think home prices will fall (even if they don't plan to borrow the money right away). This, in effect, locks in the amount of equity at your disposal. Keep in mind, you don't have to take all the proceeds at once. You can withdraw (borrow) smaller amounts when you need it to minimize interest.

For more information, contact any professional mortgage planner or feel free to contact me.

Secondary Financing (2nd Mortgages)

Secondary financing is when you finance (borrow against) real estate using a loan that is subordinate to (i.e., "behind") a first mortgage.
A second mortgage is used when the borrower doesn't want to refinance his/her existing first mortgage. Determination of first, second, third mortgage, etc. is determined by priority of registration (time and date).

Securitization & CMB's

Lenders "securitize" mortgages when they package them up for the purpose of selling them to investors.
Securitization lets lenders raise new capital that they can lend to other borrowers.

Here is a basic overview of the most widely used form of securitization in Canada:

1. Lenders originate mortgages
2. Lenders arrange these mortgages into groups (pools)
3. Lenders sell these pools as mortgage-backed securities (MBS) to the Canadian Housing Trust (CHT), a CMHC-run entity
4. The CHT sells Canada Mortgage Bonds (CMBs) to generate funds to buy lenders' mortgages
5. The CHT uses the MBS cash flows to make interest payments on these CMBs to investors.

...and the process repeats itself over and over.
The mechanism above lets investors make secure investments in Canadian residential mortgages by buying CMBs.

Because CMBs are fully guaranteed by the government, investors demand less interest on CMBs. That lowers the cost of funds for lenders, which in turn lowers interest rates for homeowners.

Smith Manoeuvre

The Smith Manoeuvre is a technique that converts regular debt into tax-deductible debt. In the process, it affords the opportunity to pay off one's mortgage significantly faster.
The Smith Manoeuvre works basically as follows:

1. First find a readvanceable mortgage
2. Then sell your non-registered assets (like stocks held outside of an RRSP)
3. Use the proceeds as a down payment on your mortgage
4. Make your mortgage payments like normal
5. As you pay off principal, re-borrow that principal into a line of credit (LOC)
6. Invest this re-borrowed money at a higher rate of return than the interest you pay on the line of credit
7. Deduct your investment loan (LOC) interest and use the tax savings (refund) to pre-pay your mortgage
8. Repeat steps 3-7 until your mortgage is fully paid off.

Fraser Smith, for whom the Smith Manoeuvre is named, stated that the strategy can cut your mortgage payoff time in 1/2, while helping you invest more, sooner.
The Smith Manoeuvre is indeed a powerful strategy, but it's not for everyone. There are both investment risks and serious tax risks. Your returns could be insufficient, CRA could invalidate your application of the strategy, or you could wind up in a negative amortization scenario if your house value falls.
Therefore, always consult a licensed financial and tax advisor before considering it. Find an advisor that will work closely with your mortgage planner, offers free consultations, and charges no out-of-pocket ongoing fees.
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Implementing the Smith Manoeuvre takes more than just refinancing your mortgage and picking some mutual funds. Moreover, there is no off-the-shelf financial or income tax software that efficiently manages the process. The best advice is to get proper advice...from the start.

Spreads

Put simply, a "spread" is the difference between two rates.
Mortgage lenders maintain a spread between the rates they offer consumers and the lenders' cost of funds.
The following can be used as a starting point (base) when determining a lender's cost of funds:

- For fixed mortgages: The corresponding government bond yield
- For variable-rate mortgages: The 30-day bankers' acceptance yield

In reality, however, most lenders' base funding costs reflect a blend of funding sources, such as deposits, GICs, Canada mortgage bonds, covered bonds, etc. In addition, lenders sometimes fund longer-term mortgages with shorter-term assets.
Keep in mind, bond yields and bankers' acceptance yields represent the "base" cost of funding a mortgage. On top of that lenders incur a slew of other costs related to liquidity/risk premiums, underwriting, overhead, marketing, compensation, administration, securitization, hedging, etc.

In the financial markets, there is also a thing called a "credit spread." A credit spread is the difference between a government Treasury security and another non-Treasury credit instrument.

For example, a commonly quoted credit spread in the mortgage market is the "CMB spread." This reflects the difference between Canada Mortgage Bond yields and the corresponding government bond yield.

Standard Rate Simulation Assumptions

Amortization simulations are sometimes used to compare the hypothetical future performance of two different mortgage terms.
When performing simulations we make the following standard assumptions:

- Amortization is 25-years
- Compounding is semi-annual (unless otherwise stated)
- The borrower has no need for early termination before maturity
- The borrower makes equal payments in each case. (e.g., When comparing a variable and 5-year fixed, it's assumed that the variable-rate borrower will increase his/her payments to match the 5-year fixed payment [if it is higher].)

Furthermore, where we state that Bank of Canada rate changes are to occur "during" a particular year, we sample three different scenarios of when those changes might happen:

1. early in the year
2. in the middle of the year
3. late in the year.

We then take a simple average of borrowing costs, based on these three scenarios, and use that in our conclusion. This is necessary because it's impossible to know exactly when the BoC will change rates.
Always remember: Projections are based on hypothetical borrowing cost computations only. They do not consider individual borrower circumstances, which may dictate a different course of action than that suggested by a simulation. All data are hypothetical and rate-dependent and results we post may differ from actual performance. Speak to a licensed professional mortgage advisor before using any information you read online.

Stated Income Mortgage

A stated income mortgage is where the lender does not verify the borrower's income by looking at their pay stubs, income tax returns, or other income documentation.
Instead, borrowers are essentially asked to state their income, and taken at their word.
These loans are intended for self-employed borrowers, or other borrowers who might have difficulty documenting their income using conventional means.
To offset their additional risk, stated income mortgages often come with higher fees and/or higher insurance premiums. The rates are sometimes higher rates as well.

Target Rate

The Bank of Canada's target rate is the interest rate that the Bank of Canada wants major financial institutions to use when lending one-day (overnight) funds to each other.
The target rate therefore sets the "overnight lending rate" and is often referred to as the Bank's *key interest rate* or *key policy rate*.
Changes in the target rate influence other interest rates as well, such as those for consumer loans and mortgages.
In November 2000, the Bank introduced a system of eight "fixed" dates each year on which it announces whether or not it will change the target rate.

TDS Ratio (Total Debt Service Ratio)

Lenders have long relied on two standard measures of one's "ability to pay" their mortgage:
Gross Debt Service (GDS): The percentage of the borrower's income that is needed to pay all required monthly housing costs (mortgage payments, property taxes, heat and 50% of condo fees).
Total Debt Service (TDS): The percentage of the borrower's income that is needed to cover housing costs (GDS) plus any other monthly obligations that an individual has, such as credit card payments and car payments.
The acceptable ratios for both have generally been 32% and 40% respectively.
For people with very high credit scores, GDS requirements are often waived and the TDS maximum is slightly higher (44% as of January 2011).

TED Spread

The TED spread represents the difference (spread) between what banks and the U.S. government pay to borrow for three months.
The U.S. government is considered to be "risk-free" while banks are not. As such, the TED spread is a common indicator of credit market risk.
As risk goes up, it affects lenders' funding costs. That can manifest itself in higher mortgage rates.
A "normal" TED spread is considered to be 10 to 50 basis points (bps), with the long-term average being roughly 30 bps.

In October 2008, the TED spread reached an astonishing 460 basis points. That coincided with variable mortgage rates rising to a virtually unprecedented prime + 1.50% at some major banks.

Tightening & Loosening (of Monetary Policy)

"Tightening" is a course of action undertaken by the Bank of Canada (BoC) to constrict spending in an economy that is seen to be growing too quickly, or to curb inflation when it is rising too fast.

The BoC "makes money tight" by raising its key short-term interest rate (also known as the overnight target rate), which increases the cost of borrowing and effectively reduces its attractiveness.

Policy loosening is the exact opposite of tightening. In that case, the BoC lowers it's overnight rate to encourage borrowing and spending and stimulate a flagging economy.

Trailer Fees & Renewal Fees

A *trailer fee* is compensation that a lender pays to a broker or lender rep as an incentive to keep his or her clients with that lender. Trailer fees are usually paid annually, on or around the anniversary of a client's closing.

A *renewal fee* is compensation that a lender pays to a broker or lender rep once per mortgage term, when his or her clients renew with that lender.

Trailer and renewal fees compensate a mortgage originator for providing the borrower with ongoing mortgage advice and services. These two fees are paid on top of any upfront commissions and have long been common in industries like insurance and financial services.

Trailer and renewal fees are incentives that should be fully disclosed to the borrower, as they can sometime sway a broker's or lender rep's mortgage recommendation.

Trigger Rate

Some variable-rate mortgages offer the option of a fixed payment. So, even if interest rates rise (or fall), your payment stays the same.

There is an exception to this. It occurs when prime rate goes up so much that your fixed payment no longer covers the interest you owe each month. That point is called the "trigger rate."

When you hit the trigger rate, your lender will increase the fixed payment on your variable-rate mortgage to ensure you're covering the interest due.

As a very rough rule of thumb, prime rate generally has to rise about 2% or more for you to hit your mortgage's trigger rate.

Underwriter

A person who examines all the data about a borrower's credit profile, resources, employment, and property to determine whether the borrower should be approved for a mortgage.

Vendor Take-Back Mortgage (VTB)

A mortgage in which the vendor uses his or her own equity to provide some or all of the mortgage financing in order to sell the property.

Variable Rate Mortgage (VRM)

A variable interest rate mortgage is a mortgage loan with an interest rate that can change during the term. The interest rate varies with changes in market interest rates.

Y/Y (YOY)

An abbreviation for "Year-over-year."
In other words, it means "compared to last year at this time."

Acknowledgements

Thank you to CanadianMortgageTrends.com for permission to reprint the terms and definitions contained in this glossary.