HEADSTART MORTGAGEARCHITECTS®

www.okanaganmortgages.com

MORTGAGE PRE-APPROVAL

KNOW WHAT YOU CAN AFFORD

Before you venture out to look at houses for sale, meet with your mortgage professional to complete an application and determine how much you are qualified to borrow. This will help you determine the price range you can be looking at, as well as give you an opportunity to learn more about how mortgages work. Your mortgage professional will outline how much you need to have on hand to cover your down payment and closing costs. As well, this will give you an opportunity to address any issues with your credit bureau.

Your mortgage professional will complete a credit application with you. Information you need to have on hand includes: personal data such as your legal name, birth date, and social insurance number; home address and employment information; a description of your assets that includes what you will use for your down payment; and a list of your outstanding debts (credit cards, loans, etc).

Once you have signed an authorization form, your mortgage professional will access your credit report. Your credit report provides a history of how you manage your credit and is a key factor that potential lenders review when considering your application. Your lender will also ask for confirmation of the information that you have provided in your application. You will be asked to provide documentation such as bank statements and current pay stubs. It is helpful to start gathering this information ahead of time to avoid last minute stress.

You will be required to show that you have at least 6.5% of the purchase price of your home set aside to cover your minimum down payment and closing costs. Your down payment ideally comes from your own savings. If you have invested in RRSPs (provided they are not considered locked in), you may be able to take advantage of the Home Buyers Plan and use them as your down payment. Your down payment may also come from funds gifted by a first degree relative.

The minimum down payment required to purchase a primary residence is 5% (for purchases up to $500,000). Over this amount, the minimum down payment required changes to 5% up to $500,000 and 10% of the balance over $500,000. That being said, the more you are able to put down towards your purchase, the less interest you will pay over the long term.

If you are putting down less than 20% of the purchase price, lenders require default insurance. The purpose of this insurance is to protect the lender in the event that you default on your mortgage payments. It is a one-time up front cost that can be added to your mortgage. It is calculated as a percentage of the amount you borrow and is based on a sliding scale - the more you put down, the lower the percentage that is charged. In some remote areas, lenders may require default insurance even if you put down more than 20%.

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CLOSING COSTS

Closing costs include items like an appraisal, a home inspection, title insurance, Property Transfer Taxes, and legal fees. Depending on your particular circumstances, an appraisal may not always be necessary. As a first time buyer you may not have to pay property transfer tax. In unusual situations, you may also require a property survey if the original has been lost or if the property has been significantly altered.

Your mortgage professional can give you an idea of what these costs are in your particular area. It is a good idea to use a checklist to keep track of your estimates for these expenses, to ensure that you have enough money set aside to cover them. Once you have completed an application and demonstrated that you have your down payment in place, your mortgage professional will submit an application on your behalf to determine if you are pre-approved. You will find out the maximum amount you are qualified for, and most lenders will issue a 120 day rate guarantee. This rate guarantee means that even if rates go up while you are shopping, your mortgage will be at the pre-approved rate provided it closes within the 120 day period.

If you have not purchased within the 120 days, it is often possible to extend the rate guarantee if rates have not increased. It is important to understand that even though you are considered pre-approved for a mortgage, final approval is still subject to the property you buy being considered suitable by the lender. As well, you must be able to satisfy the lender's requirements for appropriate documentation. It is important to consider your lifestyle and spending habits … just because you are pre approved to a certain amount does not mean it will be comfortable to carry that particular mortgage payment.

Practice making the higher mortgage payment and additional expenses of owning your own home for a few months. This will give you a good idea of whether you want to commit to the maximum amount, or perhaps scale back a little to allow for more discretionary spending. Knowing the amount you are pre-approved for will help guide your search as you move to the fun part of the process – shopping for your new home.

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HOW MUCH CAN I AFFORD?

How much can I afford? Your mortgage specialist will be able to calculate the amount that you are eligible to borrow. The standard rule of thumb (subject to certain exceptions) is that your housing costs should not be more than 32% of your gross income, and your total debt payments should not exceed 40% of your gross income. According to Canada Mortgage and Housing Corporation, lenders follow two rules to help calculate the maximum mortgage payment you qualify to carry.

These two rules are explained as follows:

Affordability Rule 1

The first rule is that your monthly housing costs shouldn't be more than 39% of your gross monthly income. Housing costs include your monthly mortgage payments (principal and interest), property taxes and heating expenses. This is known as PITH for short —Principal, Interest, Taxes, and Heating. Lenders add up your housing costs and figure out what percentage they are of your gross monthly income. This figure is called your Gross Debt Service (GDS) ratio. To be considered for a mortgage, your GDS must be 39% or less of your gross household monthly income.

Affordability Rule 2

The second rule is that your entire monthly debt load should not be more than 44% of your gross monthly income. Your entire monthly debt load includes your housing costs (PITH) plus all your other debt payments (car loans or leases, credit card payments, lines of credit payments, etc.). This figure is called your Total Debt Service (TDS) ratio.

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DOCUMENTATION

Information required to be pre-approved for a mortgage:

- Ask your employer to prepare a letter on company letterhead outlining your name, base salary or hourly rate, normal hours worked per week, position and length of service. A recent pay stub and a copy of your T4 from last year may also be required.
- If commission sales, previous two years personal tax returns together with the Notice of Assessments from Canada Customs & Revenue Agency
- If self-employed, previous two years personal tax returns together with the Notice of Assessments from Canada Customs & Revenue Agency, previous two years business financial statements, and two years business tax returns (if applicable)
- Social Insurance Numbers
- At least 3 years history of residence and employment
- Banking information (name of financial institutions, address, and type of accounts, account numbers)
- Know your assets (what you own) and their value. i.e. cash amounts, stocks, bonds, RRSPs, car
- Know your liabilities (what you owe). i.e. car loan, credit card balances, child or spousal support payments

It's also a great idea to write down a list of any questions you would like to have answered.

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