Top 10 questions we are asked about: Mortgage Renewal

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Renewing your mortgage is an important event with many considerations. Most mortgages issued in Canada have a term of five years and are amortized over 25 years. This means you will likely renew your mortgage at least four times before it is paid off. With the right advice from your trusted Edward Jones financial advisor, you can potentially shave years off the life of your mortgage and save thousands of dollars along the way. That's why we've put together a list of the top 10 questions we receive from those approaching mortgage renewal.

1. What does it mean to renew my mortgage?
2. How is my mortgage payment determined?
3. How can I decrease my mortgage payment?
4. Should I go with a fixed or variable rate mortgage?
5. How much interest will I pay?
6. Does it make sense to sell my investments to pay down my mortgage?
7. Does extending my amortization require me to pass the stress test again?
8. Does the mortgage stress test apply to all lenders?
9. The bank offered me life insurance linked to my mortgage - Should I get it?
10. Does the Bank of Canada (BoC) decision to raise or lower their policy rate impact my mortgage payment?

1 What does it mean to renew my mortgage?

Renewing your mortgage means paying off your existing mortgage, which has ended, with a new mortgage. It usually involves renegotiating the terms of your mortgage contract, or accepting the "new terms" that your existing lender provides. At renewal you can:

- Make lump sum payments on your existing balance without penalty
- Select the term that works best for you
- Choose between a fixed or variable rate
- Change the payment frequency
- Switch to a different lender
- Refinance (borrow against the equity in your home)

2 How is my mortgage payment determined?

Your mortgage payment is made up primarily of 4 factors:

- Amount owing
  The more you borrow, the higher your required payment will be.
- Interest rate
  A higher interest rate will lead to more interest being paid on the mortgage loan.
- Payment frequency
  Paying your mortgage more frequently will reduce the amount you owe in the long term.
- Amortization period
  Longer amortization results in lower payments but will increase the total amount of interest paid over the lifetime of your mortgage.

3 How can I decrease my mortgage payment?

If you feel like you can no longer afford your mortgage payment, speak to your Edward Jones financial advisor and have them complete a cash flow review. To decrease your mortgage payment, you can try any combination of:

- Make a lump sum payment to decrease the overall amount owing on your mortgage.
- Secure a lower interest rate at mortgage renewal. This could be done by selecting a variable rate when rates are expected to decrease over your mortgage term or locking into a fixed rate that is lower then your current mortgage interest rate.
- Increase your payment frequency. Paying your mortgage more frequently will reduce the amount you pay at each interval and decrease the amount of interest you pay over the life of the mortgage.
- Extend your amortization to reduce your mortgage payment; however this will mean you pay more interest in the long run.

Refinance: This works if you have equity in your home however there are drawbacks including additional costs in the form of fees and additional interest owed over the lifetime of the mortgage.

4 Should I go with a fixed or variable rate mortgage?

Like many personal financial decisions, it depends on you and your unique personal circumstances. While there is no one-size-fits-all answer, there are a few items to consider when making this decision.

Variable rates are usually lower than fixed rates, have lower prepayment penalties and restrictions, and have proven to be less expensive over time. However, variable rates are less stable, and your interest rate and corresponding mortgage payment could increase during the term. On the other hand, a fixed rate mortgage provides stability with a locked-in mortgage rate and payment, thereby easing any potential anxiety around budgeting and cash flow. Yet, fixed rates are typically higher than variable rates, and have higher prepayment penalties compared to variable rate mortgages.

5 How much interest will I pay?

The amount of interest paid on a mortgage depends on several factors including the amount borrowed, the interest rate, and the number of years it takes to pay off the mortgage (amortization). Consider, for example, a house purchased for $716,000 (currently the average house price in Canada) with a $36,000 down payment, and a 25 year mortgage with a 6.45% interest rate.

- Mortgage (amount borrowed): $680,000
- Time to repay (amortization): 25 years
- Interest rate: 6.45%

In this scenario, the mortgage payment would be $4,534.22 per month. Over the span of 25 years, the total amount of interest paid is $680,259 Notice that the amount of interest is more than the original amount borrowed. At the end of 25 years, although the total amount borrowed was only $680,000, the total amount repaid is $1,360,259.

6 Does it make sense to sell my investments to pay down my mortgage?

Maybe. Depending on your induvial goals and your comfort level with risk. To determine if this makes sense financially, speak with your advisor about the type of investments you own, the rate of return you are expected to earn, the tax treatment of those investment returns, and the rate of interest on your mortgage.

Aside from the math, there may be other personal factors to consider as well. For example, some people are comfortable carrying significant amounts of debt, while others are naturally more debt-averse and sleep easier at night when they aren't burdened with significant debts. Furthermore, this doesn't have to be an 'all or nothing' type decision – it may make sense to use some, but not all, of your investments to pay down your mortgage. Before making this decision, pay attention to pre-payment penalties as many mortgages have fees or penalties for early payments, so be careful to check the terms of your agreement first.

Many products with guarantees and principal protection, such as GICs, typically offer low rates of return and poor tax efficiency. If you're carrying a high rate of interest on your mortgage, it may make sense to use the proceeds from a GIC to pay down a portion of that debt. On the other hand, some investments can provide higher rates of return over time, as well as increased tax efficiency.
If you're enjoying a low rate of interest on your mortgage and earning a higher rate of return on your investments, it may be more beneficial to leave your investments intact and make your regular mortgage payments from other sources.

7 Does extending my amortization require me to pass the stress test again?

It depends. If you remain with the existing lender, this is likely not required. However, if you decide to switch lenders (say to secure a lower rate or more favourable terms), you may be required to pass the mortgage stress test again.

Keep in mind that the Canada Mortgage and Housing Corporation (CMHC) will only insure mortgages with an amortization period of 25 years or less, so to extend the amortization beyond 25 years, you will need to have at least 20% equity in your home.

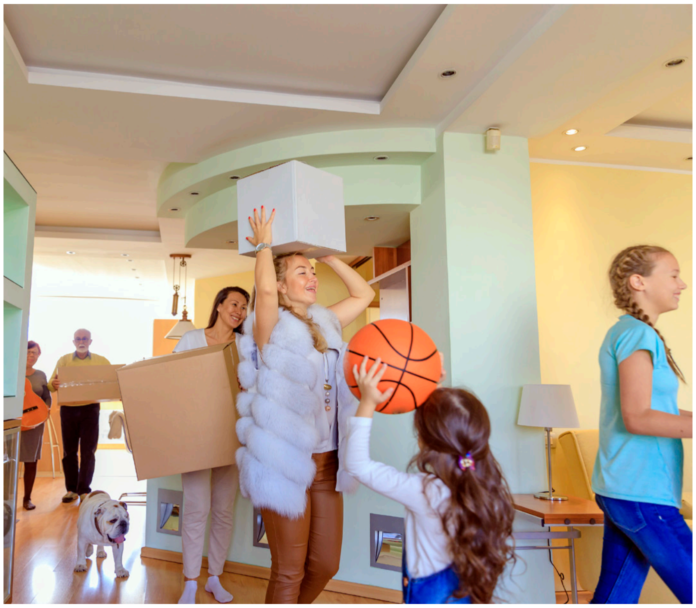
Additionally, there may be fees charged by the lender to facilitate an extension of the amortization period.

8 Does the mortgage stress test apply to all lenders?

No, the mortgage stress test only applies to federally regulated lenders such as Banks, Trust Companies and Life Insurance Companies. Credit Unions and other private lenders that are not federally regulated do not need to use this mortgage stress test for qualification. That said, they can still use it when determining a person ability to repay the loan.

9 The bank offered me life insurance linked to my mortgage - Should I get it?

There are a few important differences between life insurance purchased as an individual versus through a lender. An individual policy is usually far superior to a lender-owned policy. Here is a summary of some key differences:



Life Insurance – Individually Owned vs. Bank-Owned

	Individual Insurance Policy	Bank-Owned Insurance Policy
Policy Owner	You	Lender
Death Benefit Type	Remains constant during the lifetime of the policy*	Decreases with every mortgage payment
Amount of Coverage	Your choice – the amount of life insurance can be chosen to meet your needs	No choice – Coverage matches mortgage amount owing at death and decreases as the mortgage is paid, although your premiums do not decrease accordingly
Term	Your choice – typically 5-, 10- or 20-year terms are available, often with the option of converting to permanent insurance	No choice – your coverage is cancelled when the mortgage is paid or moved to another lending institution
Beneficiary	Your choice – You can name anyone you wish to receive the insurance proceeds	No choice – The lender is the beneficiary and will receive the insurance proceeds
How the insurance proceeds are used in the event of death	Your choice – Life insurance proceeds are paid as tax-free cash, and your beneficiary can spend, save, or invest the money any way they choose	No choice – Insurance proceeds are paid directly to the lender
Other uses for your policy	Your choice – You can use the same policy to cover your general life insurance needs as well, such as paying off outstanding debts or funding your childrens' education	No choice – Only the current mortgage amount is covered
Premium payments	Your choice – Most insurance companies offer monthly, quarterly, or annual payment schedules	No choice – Insurance premiums are added to your mortgage payment

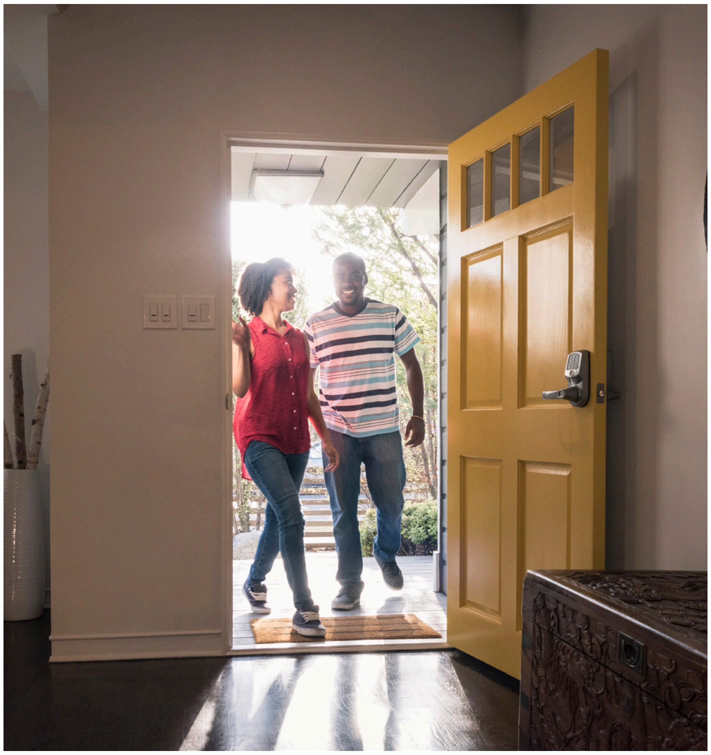
	Individual Insurance Policy	Bank-Owned Insurance Policy
Premium discounts	Premium is affected by gender, age, and smoking status	Premiums are usually the same for all clients of same age
Portability	Yes – Your insurance is not linked to the mortgage and stays with you regardless of where you live, work, or where you obtain or renew your mortgage	No – Your insurance can be cancelled if you renew your mortgage with a new lender, or even if you refinance at the same institution
Professional advice	Yes – Personalized service from a licensed life insurance advisor to address your financial security needs	No - Advice is typically limited to the mortgage insurance product only
Regulated sales	Yes – Only licensed life insurance agents can sell individual life insurance policies	No – Retail bank staff and mortgage representatives are not required to meet life insurance licensing or education requirements

*Increasing and decreasing death benefit amounts are available from some insurers
Insurance and annuities are offered by Edward Jones Insurance Agency (except in Québec). In Québec, insurance and annuities are offered by Edward Jones Insurance Agency (Québec) Inc.

10 Does the Bank of Canada (BoC) decision to raise or lower their policy rate impact my mortgage payment?

It might. If you have a variable rate mortgage and your payments are adjusted with rate changes, the Bank of Canada's policy rate decisions will have an impact on the amount you owe each time.

If you have a variable rate mortgage and fixed payments, you will likely not be immediately impacted by the BoC rate decision unless it causes you to exceed your trigger rate. In a period where the BoC is raising rates, with fixed payments on a variable mortgage, you will pay less towards the principal of the mortgage and more towards interest. This will cause your amortization period of your mortgage to increase, and you will end up paying more interest over the mortgage term. The opposite is true in periods where the BoC is decreasing the policy rate. If you have a variable rate mortgage and variable payments, your mortgage payment will decline as it will be adjusted downward to reflect less interest owing and to keep true to the agreed upon amortization period. In a period where the BoC is decreasing rates, with fixed payments on a variable mortgage, you will pay more towards the principal of the mortgage and less towards interest. This will cause your amortization period of your mortgage to decrease, and you will end up paying less interest over the mortgage term.



Common Mortgage Renewal Terms and Explanations

Variable Rate Mortgage
A variable rate mortgage is a loan with an interest rate tied to your lenders prime rate. In most cases, a variable rate mortgage is quoted as "prime minus x%".

Fixed Rate Mortgage
A fixed rate mortgage is a loan with an interest rate that is locked-in and agreed upon when you sign your documents. This rate will not change for the term of your mortgage and closely resembles the Government of Canada's bond yield curve.

Open Mortgage
An open mortgage is one that allows for unlimited prepayments towards the balance owing. Open mortgages tend to come with higher interest rates to compensate the lender for the unpredictability of prepayments. For the borrower, these are often used when the intention is to pay off the loan in a very short period (less than a year).

Closed Mortgage
A closed mortgage restricts the borrower's ability to make large prepayments. This doesn't mean that you cannot make prepayments however there are penalties if you go beyond what your contract allows. Closed mortgages are the most common mortgage type and typically have lower interest rates than open mortgages.

Amortization Period
The amortization period is the estimated life remaining on your mortgage loan, assuming no changes are made to your current payment amount, frequency, and interest rate. With a fixed rate and assuming you make no changes to the payment amount or frequency, your amortization period will reduce at the same rate as your mortgage term. If you have a variable rate, and assuming you make no changes to the payment amount or frequency, your amortization period will fluctuate with changes to the Bank of Canada's policy rate. An increase in the policy rate will reduce the amount you pay towards principal and increase your amortization period. A decrease in the policy rate will increase the amount you pay towards principal and decrease your amortization period faster than had rates stayed the same.

Mortgage Term
The mortgage term is the number of years you agree to for your interest rate. In Canada, a 5-year rate is most common, but it may not be suitable for everyone. For instance, if you only plan to stay in your home for 3 more years, choosing a 3-year term would likely be your best option to avoid having to pay additional fees for breaking your mortgage early. Always ensure your read and fully understand the terms and conditions of your mortgage contract.

Principal Payment
A principal payment is the amount of money paid that goes towards paying down the amount owed on your mortgage.

Interest Payment
An interest payment is the amount of money paid that goes towards paying the interest that has accrued on your mortgage.

Interest Rate
The interest rate is the rate used to calculate the amount of interest you will pay on your mortgage. This rate is displayed as an annual figure

Prime Rate
The Prime Rate is set by the individual financial institution, however in almost all cases, the banks set the same rate. The Prime Rate is higher than the Bank of Canada Policy Rate and will fluctuate when the Bank of Canada adjusts the policy rate. The prime rate is used for variable rate loans such as lines of credit and variable rate mortgages.

Trigger Rate
The trigger rate only applied to variable rate mortgages with fixed payments. It is the interest rate that equates to the interest portion of your payment equaling the total payment amount. This would mean that you no longer are paying down any of the principal on the mortgage and therefor your payments must be adjusted upwards.

Mortgage Renewal
A mortgage renewal happens when the term of the mortgage expires. In most cases, you'll renew your mortgage four or more times over the life of your mortgage.

Mortgage Refinancing
Mortgage refinancing is the act of borrowing against the value of your home by increasing the size of your mortgage and receiving the cash now to spend, invest, or reduce other higher interest rate debts.

Bank of Canada Policy Rate
The Bank of Canada Policy Rate is the rate set by the Bank of Canada for institutions to borrow and lend money to each other in the overnight market. The public doesn't have access to this market, but the rate is important because its impacts the rates offered on GICs and cash deposits, as well as the interest charged on lines of credit and variable rate mortgages.

Mortgage Stress Test
The mortgage stress test was introduced for federally regulated lenders to help ensure that borrowers could withstand a potential rise in interest rates. The mortgage stress test is required on all new mortgages, mortgage refinancing, and when a borrower switches to a new lender. The stress test examines your ability to afford the mortgage based on the higher of 5.25% or your negotiated rate plus 2%.