Information on Mortgage Prepayment

Learn more about your mortgage prepayment

If you're thinking about buying a new home, prepaying your mortgage faster or using the equity in your home for renovations, the information below will help explain prepayment charges and ways to avoid them.

What is a closed mortgage?

A closed mortgage is one that cannot be prepaid, renegotiated or refinanced before the end of the term without paying a prepayment charge.

However, most closed mortgages contain certain prepayment privileges, such as the right to make a prepayment of 10-20% of the original principal amount each year, without paying a prepayment charge.

A closed mortgage often has a lower interest rate than an open mortgage.

What is an open mortgage?

An open mortgage can be prepaid, in part or in full, during the term of the mortgage without paying a prepayment charge. The interest rate on an open mortgage is often higher than the interest rate on a closed mortgage. An open mortgage can provide flexibility until you are ready to lock into a closed term.

What is a fixed interest rate mortgage?

- With a fixed rate mortgage, in most cases your interest rate does not fluctuate during the mortgage term. Your regular mortgage payment amount does not change.
- You know exactly what your regular payments will be and how much of the principal balance will be paid off during the term.

What is a variable interest rate mortgage?

- With a variable rate mortgage, the interest rate changes with changes to the CIBC Prime Rate. In addition, your regular mortgage payment amount is fixed and does not change.
- When the CIBC Prime Rate decreases, the amount of interest you pay will also decrease. A smaller portion of your regular mortgage payment will be applied to pay interest, and a larger portion will be applied to pay down the principal amount of your mortgage.
- If CIBC Prime Rate increases, the amount of interest you pay will also increase. A larger portion of your regular mortgage payment will be applied to pay interest, and a smaller portion will be applied to pay down the principal amount of your mortgage.

Why choose a short term mortgage?

A short term mortgage generally offers a lower interest rate than a longer term mortgage. When current interest rates are high and you think rates may drop, choosing a short term mortgage allows you to lock in for a shorter period. A short term mortgage may also be a good option if you plan to see your home or pay off the mortgage early.

Why choose a long term mortgage?

A long term mortgage generally offers a higher interest rate than that of a shorter term mortgage. When current rates are reasonably low, choosing a long term mortgage secures the interest rate for a longer period of time and makes budgeting easier.

How can a mortgage be paid off faster without paying a prepayment charge?

A mortgage is a big commitment. Most mortgages are paid over 25 years but we have some tips to help you pay yours off faster. Reducing the number of years you make mortgage payments can add up to big savings.

There are several ways to "pay down" your mortgage and get out of debt faster without incurring prepayment charges.[1]

1. Some types of mortgages allow you to increase your regular principal and interest payment amount by up to 20% each mortgage year. A mortgage year is the 12-month period following the interest adjustment date and each anniversary of the interest adjustment date. This allows you to pay down your mortgage faster.

   For example, if you increased your mortgage payment amount by $170 from $830 to $1,000 you could save almost $48,000 in interest over the entire amortization period of your mortgage. You could also pay off your mortgage about 8 years earlier.

2. You can make your regular mortgage payments more frequently, which saves you money in interest charges over the long run as your principal is paid down faster.

   For example if you made accelerated bi-weekly payments of $415 instead of monthly payments of $830, you could save almost $27,000 in interest over the entire amortization period of your mortgage. This would allow you to pay off your mortgage about 4.5 years sooner

3. You have the option of making lump-sum payments to pay down your mortgage faster. To avoid any prepayment charges, your payment must not exceed your allowable prepayment privilege. A lump-sum payment is applied directly to your outstanding principal if there is no outstanding interest owing. This saves you money over the course of your mortgage.[2]

   For example, if you made a $1,000 lump-sum payment annually, you could save almost $28,350 in interest over the entire amortization period of your mortgage. This would allow you to pay off your mortgage about 4 years sooner.

4. You can pay as much as possible at renewal. All FirstLine mortgages become open at renewal. This means you can pay as much as you want on your mortgage before you renew.

   For example, if you chose 5-year, fixed-rate terms, and made a $10,000 lump-sum payment every time your mortgage came up for renewal, you would save about $37,481 in interest over the entire amortization period of your mortgage, allowing you to pay off your mortgage about 6 years sooner.

[1] For illustration purposes only. Payment option scenarios assume a 5-year closed, fixed-rate mortgage of $120,000 with a 25-year amortization and a constant annual interest rate of 6.85% over the entire life of your mortgage compounded semi-annually, monthly payments of $830 and assumes no additional payments. Actual rates will vary, which will affect your payment amount, your mortgage payout date and the amount you could save.

[2] Payment options are subject to the terms and conditions of your mortgage. In some cases, making a prepayment on your mortgage or paying off your mortgage early can lead to a prepayment charge, depending on the type of mortgage you have. Prepayment charges may also apply if you renew early or refinance your mortgage. Please contact us in advance to discuss all your options.

How can prepayment charges be avoided?

You have a number of options available to prepay your mortgage and avoid prepayment charges:

Portability

If you're selling and buying a new home, your mortgage may have a portability option that allows you to Port[1] your existing mortgage term, outstanding principal balance and maturity date to a new property. Porting a mortgage means taking your current mortgage, with its rates and terms and moving it to another property.

Assumption

If you're selling your home, the purchaser may have the option of applying to assume your mortgage with the existing terms and conditions on closing[1].

Open mortgage

Enjoy the flexibility to pay off as much of your mortgage at any time without paying a prepayment charge.

[1] Subject to approval and eligibility based on the terms of the mortgage. Please contact us at 1-800-970-0700.

When does a prepayment charge apply?

- Renewing your mortgage before the maturity date
- Prepaying more than the amount of your annual prepayment privilege
- Refinancing your mortgage and selecting a new term
- Transferring your mortgage to another lender
- Paying off your mortgage before the maturity date

In all of the above scenarios, the mortgage balance is being prepaid before the maturity date, which may result in a prepayment charge.

What is the prepayment charge calculation for a closed mortgage?

If you're thinking about early renewing into a new term, refinancing your mortgage or making a lump-sum payment that exceeds your annual prepayment privilege amount, a prepayment charge may apply.

If you have a fixed rate closed mortgage and would like to prepay your mortgage before the maturity date, your prepayment charge will be the greater of the following:

- three months' interest on the amount you are prepaying
- the Interest Rate Differential on the amount you are prepaying.

If you have a variable rate closed mortgage and would like to prepay your mortgage before the maturity date, you may pay a prepayment charge equal to three months' interest on the amount you are prepaying. The interest rate used to calculate the prepayment charge will be the CIBC Prime Rate.

What is Interest Rate Differential (IRD)?

If you prepay your mortgage, you may be charged a prepayment charge. There are different methods for calculating prepayment charges. In some cases, the amount charged is the Interest Rate Differential amount. At FirstLine, the Interest Rate Differential amount is the difference between the following two amounts:

- interest over the remaining term of your mortgage, calculated at your current mortgage interest rate, plus any interest rate discount you received.
- interest over the remaining term of your mortgage, calculated at FirstLine's current posted interest rate for the mortgage product that we've determined to be similar to your mortgage.

For a full prepayment, the prepayment charge is calculated on the full amount of the prepayment. For a partial prepayment, the prepayment charge is calculated on the amount of the prepayment that is more than your annual prepayment privilege amount.

Examples of prepayment charges are calculated

The following illustrates how prepayment charges are calculated. To estimate your prepayment charge, you can use FirstLine's Mortgage Prepayment Charge Calculator. (https://www.firstline.com/moreprepay.html#).

Example of estimating the prepayment charge for a variable rate mortgage

Sebastian has a variable rate mortgage. His original principal amount was $150,000.00. Earlier in the current mortgage year, he made a prepayment that was equal to the amount of prepayment that can be made without paying a prepayment charge.

He now wants to make an additional payment of $12,500.00 to reduce his mortgage.

The prepayment charge is equal to 3 months' interest at the current CIBC Prime Rate which is 5.00%.

Here is how Sebastian can calculate the prepayment charge.

Step 1:	The amount of prepayment	$12,500.00
Step 2:	The current CIBC Prime Rate (written as a decimal, which is the same as dividing it by 100). Thus, 5% = 0.05	0.05
Step 3:	He multiplies the prepayment amount by the interest rate. This is equal to one year's interest.	$625.00
Step 4:	He divides the annual interest cost by 12 to get one month's interest.	$52.08
Step 5:	He multiplies one month's interest by three to get three months' interest. This is the prepayment charge.	$156.24

When Sebastian makes his payment, he needs to pay an additional $156.24 to pay for the prepayment charge. This is only an estimate. Sebastian can call FirstLine Mortgages to find out the exact amount of the prepayment charge.

Example illustrating the cost of prepaying the full amount of a fixed rate closed mortgage

Maria has a 5-year fixed rate closed mortgage. When she arranged the mortgage, she received an interest rate discount of .500%. The existing annual interest rate on her mortgage is 6.500%.

The principal amount she still owes is $100,000. She has two years (or 24 months) left in the term of this mortgage. However, Maria has just inherited some money and wants to pay off the mortgage.

In Maria's case, the prepayment charge will be the higher of the following two amounts:

- three months' interest at her interest rate of 6.500% plus the discount she received of .500%, which is equal to 7.000%; or
- the interest rate differential amount.

The following shows an estimated prepayment charge for prepaying the full amount of Maria's mortgage:

Estimate of Three Months' Interest

Step 1:	The amount Maria wishes to pay off is $100,000.00.	$100,000.00
Step 2:	Maria's current interest rate plus the discount she received equals 7.000%. Written as a decimal, this becomes 0.070.	0.070
Step 3:	The amount Maria wishes to prepay multiplied by her interest rate plus the discount ($100,000.00 x 0.070) equals the estimated annual interest costs.	$7,000.00
Step 4:	The estimated annual interest costs divided by 12 equals an estimate of one month's interest.	$583.33
Step 5:	One month's interest costs multiplied by three equals an estimate of three months' interest.	$1,749.99

So, an estimate of three months' interest would be $1,749.99.

Estimate of the Interest Rate Differential Amount

Step 1:	The interests costs over the term of a mortgage with Maria's current principal balance of $100,000.00, her monthly payment amount of $693.47, a term of 2 years (which is the remaining term of Maria's mortgage) and her interest rate plus the discount that she received, which is 7.000%, would be $13,603.92.	$13,603.92
Step 2:	In Maria's case, we determine that the FirstLine brand 2 year closed fixed rate mortgage is similar to Maria's mortgage. On the date we prepare the mortgage payout statement, the posted rate for this product is 5.000%.	0.050
Step 3:	The interest costs over the term of a FirstLine brand 2 year closed fixed rate mortgage with the same principal amount as Maria's remaining balance of $100,000.00, the same monthly payment amount of $693.47 and our current posted rate of 5.000%, would be $9,567.59.	$9,567.59
Step 4:	The interest costs set out in Step 3 is subtracted from the interest costs set out in Step 1. This is the interest rate differential amount.	$4,036.33

So, an estimate of the interest rate differential amount would be $4,036.33.

The Estimated Prepayment Charge

Maria's prepayment charge is the higher of the estimated three months interest costs of $1,749.99 and the estimated interest rate differential amount of $4,036.33. So, if Maria's mortgage payout statement was prepared today, an estimate of her prepayment charge would be $4,036.33.

Maria should call FirstLine Mortgages to find out the exact amount of her prepayment charge. The amount above is only an estimate.

What additional charges may apply when prepaying a mortgage?

There are sometimes additional charges that may apply when prepaying a mortgage in full or renegotiating the existing mortgage term before the maturity date:

- If you received cash back on the mortgage, you may be required to repay some or all of the cash back amount received.
- A discharge fee for document preparation and registration when the mortgage is prepaid in full.

Where can I get additional information?

For additional third party information regarding mortgage options and prepaying your mortgage, visit the **Financial Consumer Agency of Canada**:

FCAC Home Page (http://www.fcac-acfc.gc.ca/)

FCAC Mortgage Details (http://www.fcac-acfc.gc.ca/eng/consumers/mortgages/index-eng.asp)

To discuss these and other options, please contact us at Local Telephone at (416) 865-1999 or Toll Free at 1-800-970-0700.