Mortgage Default Insurance

*For the purposes of the information below, **real property** and **property** mean a home and land.*

Legislation limits financial institutions to lend a maximum of 80% of the purchase price (or appraised value) of the property you are purchasing, whichever is less. These mortgages are referred to as “low ratio” or “conventional” mortgages.

Should the borrower have less than 20% for a down payment (therefore exceeding the 80% loan to property value maximum) mortgage default insurance must be obtained. The benefit of mortgage default insurance is that it allows borrowers to purchase a property with a down payment of less than 20% (as little as 5% down in some cases). The insurance provides protection for the lender against borrower default. Default insurance does not provide protection to the borrower if they are unable to make their mortgage payment.

Innovation Federal Credit Union (Innovation) uses two mortgage default insurance providers: Canada Mortgage and Housing Corporation (CMHC), a government crown corporation, and Sagen, a private insurer approved by the Office of the Superintendent of Financial Institutions.

The mortgage insurer charges a premium based on the amount borrowed. Increasing your down payment as a percentage of your home price will minimize your mortgage default insurance premium. The premium can be added to the amount of the mortgage loan and paid to the insurer, or the borrower can pay the premium to the insurer separately. If the premium is added to the mortgage loan, it increases the balance of the mortgage loan and interest would apply to the premium amount as well.

To qualify for mortgage default insurance, the borrower must meet both the financial institution’s and the default insurer’s borrowing requirements. Mortgage default insurance is only available for properties purchased for less than $1 million in Canadian funds.

Mortgage Insurance Premiums

Mortgage default insurance premiums are calculated as a percentage of the amount borrowed. The larger the percentage of the total purchase price that is made as a down payment, the lower the premium percentage. Other factors that affect the insurance premiums are:

• *Employment status:* Self-employed borrowers may pay higher premiums than regular borrowers as their income cannot be validated in the same manner.

• *Non-traditional down payments*: For example, gifted funds received from other than an immediate family member or borrowed funds increase insurance premiums.

Current mortgage insurance premiums range from 0.6% to 4.5% of the mortgage principal, but ultimately depend on criteria as set out in the insurer’s guidelines.

Here is an example of how the mortgage default insurance premium is calculated based on a 5% down payment and a 25-year amortization period with the premium added to the mortgage:

Purchase price of home	**$ 400,000**
Less: Borrower down payment (5%)	**$ 20,000**
Equals: Mortgage loan required	**$ 380,000**
Plus: Default insurance premium @ 4% of mortgage amount	**$ 15,200**
Total Mortgage	**$ 395,200**

How Default Insurance Works

Should the borrower default on their mortgage payments or contract and no re-payment solution can be found, the lender will attempt to recover what is owed by following the mortgage insurer's default guidelines. This means the lender, or mortgage insurer, will normally pursue legal action to take possession of and sell the property to recover the balance owing including principal, interest and legal costs. If there is a shortfall between the amount owing and the amount recovered, the insurer will cover the shortfall based on certain limits the insurer has put in place. As applicable by provincial or territorial law, the mortgage insurer will then take legal action to collect the shortfall from the borrower.