Supplement to

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EXPANDED INFORMATION ON MORTGAGES

The book provides an overview about mortgages and buying a house. This discussion is intended to provide more detail for someone who is about to shop for a house.

A mortgage is inevitable for most homeowners because very few have enough cash to pay for a house outright. Not that it is impossible, though. A few years ago I had a student in his early thirties who had started saving from his part-time jobs when he was a teenager, and continued the habit as he worked throughout his twenties. Two months before coming to university as a full-time student, he had bought a condominium for which he paid cash. He was renting rooms to two roommates and using that money to cover his housing and living expenses, which were modest because he had no mortgage payments. He was able to be a student without needing either a loan or a job.

He didn't need to know about the ins and out of mortgages, but most of us do. Understanding how mortgages are structured gives you an edge. It clarifies what you can do to pay as little interest as possible.

Before we get there, though, let's look at housing costs and the income it takes to support a mortgage. To understand the analysis that follows, here is some fundamental information:

- In any market, condominiums are less expensive than detached houses of comparable size and quality. There are two reasons for this. Land costs less per unit in a condo because it's divided among many more owners, and construction costs of condos are less because there are fewer outside walls. Because of their lower relative cost, condos are more affordable for many people as their first home.

- When you apply for a mortgage, you are expected to put down at least some of your own money. The minimum down payment is typically 5% of the purchase price. At times in Canada, the required minimum has been 10% and occasionally mortgages have been available with nothing down; it depends on economic conditions at the time.

- A ***mortgage*** is a large loan for a long period of time—typically 25 years, although on occasion there have been 40-year mortgages. In March, 2011 the

Canadian government changed the rules, making a 30-year loan period the longest available for government-backed insured mortgages. In the summer of 2012, it was further reduced to 25 years. This policy was implemented because of concern that Canadians are carrying too much housing debt. The decision was prompted by economic conditions such as the state of recovery from the 2008 world economic collapse, rate of unemployment, value of the Canadian dollar, and the current rate of inflation.

- When you take out a mortgage with a low down payment (less than 20% of the purchase price) it is called a ***high-ratio mortgage***. The lender is taking a risk because you have little equity in the property, so you will be required to pay for ***mortgage loan insurance***. This is a different kind of insurance from the life insurance you buy to pay off the balance of your mortgage when you die. Mortgage *loan* insurance is insurance to protect the lender if you default on your payments and the property cannot be sold for enough to cover the outstanding balance of the mortgage. The charge for this insurance is typically between 1 and 3%. It is a one-time premium that can be paid in a lump sum or added to the amount you borrow.

- When you look at a real estate listing of a property for sale, the monthly cost is usually quoted as ***PIT***. This means principal + interest + taxes. Taxes, in this case, are ***property taxes*** paid to the municipality where the real estate is located. ***Principal*** is the amount borrowed, often referred to as the amount of the mortgage, and ***interest*** is what you pay for borrowing the money. When mortgage interest is low, many people jump into the housing market because it is more affordable. A word of caution when you are deciding if you will buy and what you can afford. It is inevitable that mortgage interest rates will rise again at some point, so leave room in your budget to accommodate this. To give you some perspective, average mortgage rates in 1951 were about 5.5%; through most of the 1970s they were 9–11%; in 1980 they went up to 15%; and in 1981 there was a rapid increase to as high as 21%. Average mortgage rates in 2010 were about 4.8%.[i]

- When you are a homeowner, you will have maintenance costs such as utilities and repairs in addition to the mortgage payment. If you buy a condominium, some of those costs are covered in the monthly condo fee. Others will be your individual responsibility. Be sure to find out what the condo fees do *not* cover, so you can realistically assess what your monthly expenses will be.

Supporting a mortgage…

With that background, let's look at some figures to see what income it would take to afford a mortgage. This example assumes purchasing a condominium with a 25-year mortgage at 5.2%.

A	Purchase price	$265,000
B	Down payment (A x 5%)	$13,250
C	Mortgage (A – B)	$251,750
D	Mortgage insurance (C x 2.75%)	$6,920
E	**Total loan** (C + D)	**$258,670**
F	Monthly loan repayment *	$1,534
G	Monthly property taxes **	$150
H	Monthly condo fees **	$350
I	Monthly property insurance **	$30
J	Monthly utilities (phone, electric) **	$80
	Total monthly housing cost (F+G+H+I+J)	**$2144**
	Gross income to support this cost	**$6700**

*Once you know the size of the mortgage, the monthly payment can easily be determined using an online mortgage calculator.[ii]

**These figures will vary depending on a variety of conditions. Representative values have been used for illustrative purposes. It is important to include these figures when doing calculations because they are part of the total cost of living in the home you are buying.

This analysis shows that this size of mortgage would require a gross (before taxes or deductions) income of $6700 per month. I calculated that figure based on the typical guideline that housing costs should be no more than 32% of gross household income. This can be calculated using a simple ratio formula:

If $2144 = 32%
Then y = 100%

By cross multiplying, we know that 32y = $2144 x 100

Therefore, y = $2144 x 100/32 = $6700

If you wonder why it is so important to keep your housing expenses at a reasonable proportion of your income, I recommend reading Gail Vaz-Oxlade's article about being ***house poor***. She identifies the issues:

> Ultimately it all ends in a mortgage meltdown. Folks find themselves struggling to make ends meet and keep their dream roofs over their heads. Their best intentions end up with the worst consequences. And all because they failed to add up the real costs of buying their home. While a mortgage is "good" debt—you're building assets, after all—too much mortgage is a fast route to bad debt. Why? Well, when it takes too much of your money to keep that "good" debt in good standing, you're more likely to turn to your credit cards and lines of credit just to make ends meet—never mind have some fun. The result: oodles of debt racked up, or a life given over to sitting in a home and staring at the bare walls. [iii]

The idea that we are all aspiring to a "dream home" is an aspect of the cultural story that usually goes unquestioned, but you might want to think about what it means to you—and what you are willing to give up to get a dream home. Holidays? Post-secondary education for your children? Financial freedom? Peace of mind? Examining the concept of a dream home can be a good focal point for thinking about what is really important to you, and why. This conversation is particularly valuable for couples, who frequently come together with different backgrounds and expectations. It's important to discuss the benefits of your "dream home" in relation to the costs of having it.

Money math is intimidating to many people. However, crunching mortgage numbers is not as daunting as it first appears. Online mortgage calculators can help you quickly and easily see what your interest and payments will be in varying scenarios. This comment came from one of my daughters-in-law:

> For me, using an online calculator was step one in learning about mortgages as related to buying my first place—taking theoretical numbers, crunching them, and then beginning to understand how down-payment dollars and amortization affected my payments. That is how I learned about mortgages initially. I find I still go to the mortgage calculators to figure out what we can afford for our "forever house" in the coming years. I would encourage people to "play with the numbers" to see what a difference time/payment schedule/down payment can make in their life and bottom line.

Industry attempts at making mortgages affordable…

When you do the calculations, you can see that it takes a substantial income to support a mortgage at current prices. This reality puts home ownership beyond the reach of many. To reduce monthly costs, lenders have come up with ways of making a mortgage seem less onerous. These options, offered at various times depending on market conditions, may not always be available.

Sometimes a lender may be willing to increase the amortization period, which is how long it takes to pay back the mortgage in full. Whereas the typical mortgage is for 25 years, at times this has been increased to 40. In the current fragile economic climate, the amortization limit of insured mortgages is no more than 25 years.

When the amortization is stretched out over a longer period of time, monthly payments are less and it seems more immediately affordable. In the example we've just seen, payments are reduced from $1534 to $1412 per month when the mortgage is increased to 30 years. The downside, though, is that you pay more in total interest because of the longer time period. On our 25-year loan, the total interest was $201,536. When the mortgage is extended to 30 years, you will be paying $249,483 in interest. That is $47,947 more in interest because the mortgage was extended for 5 years.

This is true for loans of all types. When people base their decisions on what costs them less at the moment, they end up paying a good deal extra in the long run. It's more constructive to consider the big picture—that is, what it will cost in total.

In another attempt to make mortgages affordable, lenders may allow the mortgagor (the person who is borrowing the money) to make interest-only payments. For example, this may be offered when the borrower has encountered hard times and is unable to make the full monthly payments. By paying only the interest portion, they are able to keep the mortgage in place until the situation returns to normal. A big disadvantage, though, is that the principal remains the same, so the loan itself is not being paid down. Once again, the borrower is paying more interest in the long run.

A third attempt to make houses accessible is by requiring no down payment. This results in a mortgage for 100% of the purchase price. This option has greater-than-normal risk for both the lender and borrower, so is not often an available choice. While it's appealing to folks who have not saved a down payment, there are a couple factors to seriously consider. First, such mortgages may carry a higher interest rate because the lender is taking a bigger risk on this loan. For you, this means paying more in total interest over the life of the mortgage.

Mortgaging a property for its full purchase price is also risky if housing prices fall and you need to sell. In a soft real estate market, when demand is low, the selling price may be less than the amount of the mortgage. If your purchase price was $265,000 and you could sell it for only $175,000, you would be accountable for the difference of $90,000. You are still responsible for paying back the entire mortgage amount, and the lender can go after your other assets when the amount from the sale is insufficient. This is a major risk to take and would require careful thought on your part.

Is buying a house even realistic?

What is a person to do, then, to be able to afford to buy a house? We need to start with our expectations. Until now, young people have generally expected that the standard of their first home will match that of the home in which they grew up. It was a reasonable expectation until recently. However, economic realities of this time no longer support that expectation. We have arrived at the first generation to find its housing standard below that of its parents. This may not seem fair, but it is the reality.

Changed expectations may involve size of the house, whether it's a single detached home, and how many people live in it. A large detached house in an expensive suburb with one or two occupants is now a luxury. A small condominium in a modest neighbourhood is more affordable. To further reduce costs you could consider taking a roommate or two; this can go a long way toward paying the mortgage. Or, for your first house, you might buy one with a basement suite where you live on one level and have a renter on the other. (Notes: You can charge more for a main-floor suite than one in a basement, so you may decide to live in the lower suite to give you the most rental income possible to apply toward the mortgage. Be sure to check zoning regulations because not all neighbourhoods permit rental suites.)

Another sound strategy is to get together the largest down payment you can. The more you can put down, the less you have to borrow and thus the lower your payments will be. Often older family members, appreciating the challenges of starting out today, are willing to lend money, perhaps even at a reduced interest rate. A strong note of caution, though: Be absolutely scrupulous with both the arrangements and repayments when it comes to dealing with family and friends. It's tempting to delay or skip payments on the assumption that they'll cut you some slack. Don't. These are people who will be in your life for a long time and it's not worth jeopardizing your relationship with them.

Your RRSP, under the Home Buyers' Plan, is another source of a lump sum you can put toward your down payment. It allows withdrawal of $25,000 from an RRSP, to be repaid at a rate of 1/15 per year for fifteen years. The withdrawal is not added to taxable income. However, if the prescribed repayment schedule is not met, then the money will be taxed. Therefore, the yearly repayment amount has to be factored into your budget for this to work. If you can't replace the pre-determined amount each year, you will be required to pay a large lump sum in taxes on the amount you took out of your RRSP.

Understanding mortgage interest so you can pay less…

A mortgage is the largest loan most of us will undertake. The size and length of a mortgage means it costs you a surprising amount in total interest. But it's not all bad. Carefully-chosen real estate is generally considered a good investment because it can reasonably be expected to appreciate in value. A mortgage is a means of leveraging your investment when you don't have the cash to pay for it outright. (Leveraging is defined as borrowing to invest.)

Just how much interest might your mortgage cost you? If you take 25 years to pay off your mortgage and the interest rate is 6.5%, you will pay as much again in interest as the amount you borrowed. So, if the mortgage was $200,000, then you will have paid the lender $400,000 when the last payment is made. When interest rates are higher, you pay a higher total amount of interest. For example, when rates were 11.6% in the 1970s, home buyers paid twice the amount of the loan in interest. In that case, on a mortgage of $200,000, the total paid to the lender was $600,000 over those 25 years. Clearly, anything that will reduce the interest you pay is a good strategy. To understand the rationale for such strategies, you need to first understand some basic mortgage terminology and how mortgages are structured.

A ***mortgage*** is a loan for the purchase of real estate, in which the property itself is the security. ***Foreclosure*** is the process of repossessing that security in the event of default (nonpayment) on the monthly mortgage payments. The ***homeowner's equity*** refers to the amount of the property that the borrower actually owns; it is the market value of the property minus the outstanding mortgage.

The ***amortization period*** is the length of time it takes until the loan is paid off in full. A unique characteristic of mortgages is that they are amortized for a significantly longer period of time than other loans.

A mortgage also has a ***term,*** which is shorter than the amortization period. Term is the length of time within the total amortization period for which there is an agreement at a specific interest rate. The term will normally be somewhere between one and five years, although some are as short as six months and you may see mortgage terms of seven or even ten years. At the end of the term, the lender offers you a chance to renew at whatever interest rate is then appropriate to market conditions. Also at the end of the term, you have the option to pay down the principal without any penalty.

Mortgages may be classed as either ***open or closed***. This determines whether you can pay down the principal at times other than the end of the term without penalty. As you might guess just from the name, an open mortgage gives you greater privileges for prepaying the principal. We will discuss later why this is significant in the big picture.

When applying for a mortgage, you might also be asked if you'd like a ***fixed or variable rate.*** A fixed rate is typical; the interest rate is established at the beginning of the term and it applies until the end of the term. Then a new rate is agreed to for the next term, depending on market conditions.

The variable rate mortgage is a newer product, developed in response to the volatile interest rates of the early 1980s as a means of helping people cope with the rapid rise in mortgage interest rates. With the original variable rate mortgages, the borrower pays a fixed monthly amount, even though the interest rate changes as the prime interest rate fluctuates. Calculations each month determine how much of the monthly payment goes to interest and how much is left to apply against the principal, given that month's interest rate.

The interest is taken first from the mortgage payment, and then the remainder is applied to the principal. If rates have gone up and there isn't enough money in the payment to cover both interest and principal, the shortfall is considered a loan and added to the balance of the principal. Conversely, if interest rates have gone down, the borrower is actually overpaying, and the extra is subtracted from the principal, bringing it down more quickly.

With a mortgage structured this way, the worst-case scenario is that rates will continually be up and the monthly payments will be insufficient for an extended period of time. In this case, a sum of money will be *added* to the principal every month. This is not what one expects when making mortgage payments—we want the loan to be going down.

I vividly recall a letter to the editor published in the newspaper a year after variable rate mortgages were introduced. The writer was incensed, having just received his mortgage statement at the end of the first year of his variable rate mortgage. His principal had started out at $65,000. (Remember this was 1981 and house prices were much lower.) When he received his statement, it said he now owed $72,000. He felt he had been ripped off, having paid thousands of dollars to the lender in monthly payments during the preceding year. How could this happen? he asked. As it turned out, he had renewed with a variable rate because it kept his monthly payments low enough to be manageable at that rough economic time. What he hadn't understood was the implications of having that variable rate.

Variable rate mortgages have evolved over the years. Now many are structured so the payments change with the interest rate. Some change quarterly, others change the month after the rate changes. If interest rates are moving downward, you will save money with a variable rate. However, the fluctuating monthly payments are uncomfortable for some people. Knowing yourself and your tolerance for uncertainty will help you decide if this type of mortgage suits you.

Mortgage structure…

Mortgages are structured with ***equal blended payments***. "Equal" means that the monthly amount you pay is the same throughout the life of the mortgage. "Blended" means that each month your payment covers a combination of both principal and interest. The proportion of these vary; in early years most of each payment goes to interest, and in later years most is applied to the principal.

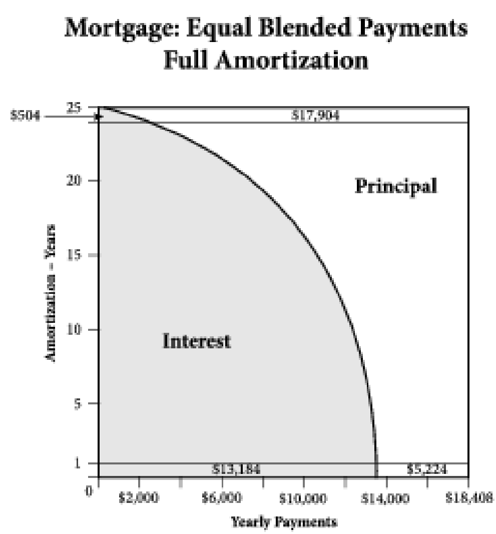
Let's examine this by going back to the example we used earlier:

Amortization period: 25 years
Term: 5 years
Amount borrowed: $258,670
Interest rate: 5.2%
Monthly payments: $1534

These monthly amounts of $1534 are used to pay the monthly interest and then pay back some of the principal which had been borrowed. Remember that the proportion going to interest and principal changes, although your payment is the same each month. Usually we aren't particularly aware of that breakdown, although it is possible to find out what it is. By putting the above mortgage details into an online payment schedule calculator[iv], I got the following:

month	Monthly payment	*Portion to interest*	*Portion to principal*
1	$1534	*$1109*	*$425*
2	$1534	*$1107*	*$427*
3	$1534	*$1105*	*$429*
4	$1534	*$1102*	*$432*
And after many more months and years…			
297	$1534	*$26*	*$1508*
298	$1534	*$20*	*$1514*
299	$1534	*$13*	*$1521*
300	$1534	*$7*	*$1527*

The same thing can be represented visually, as in the graph which follows.



As the graph shows, $18,408 is paid each year to the mortgage lender ($1534/month x 12 months). Of this amount, $13,184 went to interest and $5,224 was paid down on the principal in the first year. This shows on the graph in Year 1 if you look at the horizontal axis. This continues year after year, with a bit less being taken by interest and a bit more going to pay down the principal each year. In the last year, only $504 goes to interest and the remaining $17,904 pays off the entire remaining balance of the loan. The mortgage has been paid off, which is sometimes referred to as the mortgage being "retired."

At the end of each year, the lender sends a statement showing where things stand with your loan. In this example, the first statement would say:

Principal borrowed	$258,670
Amount repaid	5,222
Loan outstanding	$253,448

As you might imagine, if the structure of the debt was not understood, receiving such a statement can be upsetting to a new homeowner who has just paid out more than $18,000 to the lender.

The next year, the statement would show:

Loan outstanding	$253,448
Amount repaid	5,498
Loan outstanding	$247,950

It edges down slowly—and the operational word is "slowly," at least in the early years. In the last year, almost everything you pay goes toward the principal.

Not everyone takes 25 years to pay off their mortgage…

If you want to be inspired by someone who took the fast track to paying off a mortgage, read "How We Paid off Our House in Three Years." Author Perry Goertzen describes the circumstances that brought him to his early thirties with $37,000 in debt, a rusty old car, few possessions and no house. By then, he had a master's degree and a plan that changed everything. He and his wife decided to continue to live like poor students, work as much as they could, and buy a house.

> In June of 2002, we purchased our first home in a new subdivision in Milton [Ontario] for $302,000, and took on a five-year, 5.2 per cent fixed-rate mortgage for $220,000. At first, we intended to pay it off in 10 or 15 years. But then I looked at what would happen if I

doubled up the payments and paid an extra 10 per cent a year. It was incredibly motivating to see how much interest you could save. So we doubled up every bi-weekly payment, from $670 to $1,340. We also made the annual 10 per cent prepayment, which was about $22,000 a year.

At the end of the first year, we realized that we were saving much more than we needed, even with the doubled payments and annual prepayment, so I approached the bank and asked them if we could make an annual prepayment of 20 per cent instead. It took a little bit of coaxing and a few Tim Hortons coffees, but banks can be more flexible than you might think: don't assume the terms of your mortgage can't be changed.

At that rate of payment, we managed to pay off the whole thing in exactly 952 days. By paying off the mortgage in less than three years instead of 25, we saved a total of $153,000 in interest charges, which amounts to more than half the original cost of the house. Meanwhile, the house had already increased in value to about $420,000. [v]

Key strategies for reducing mortgage interest paid…

1. **Shorten the amortization period.**
   When you reduce the period of time for which you borrow a sum of money, you also reduce the total amount of interest you pay. However, this strategy will increase your monthly payments by a small amount. Play with the options, using an online calculator, to see what might work for you.

2. **Prepay the principal.**
   Prepayment means paying extra money, beyond your regular monthly payments, which goes directly to pay down the principal. Most of what you pay in the early years goes toward interest, so it takes a long time to pay off much of the principal if you just follow the regular schedule. By prepaying on your mortgage, you can retire it sooner than scheduled and save tens of thousands of dollars in interest. In our example, prepaying $2000 a year means the mortgage will be paid off in 20 years instead of 25, and you will pay $42,000 less in interest. When you get a mortgage, be sure to verify that it has prepayment privileges.

3. **Pay weekly or biweekly**
   Your lender may refer to this as making *accelerated payments*. If you pay every two weeks rather than once a month, you actually end up

making extra payments. This extra money pays down the principal in the same way that a prepayment does. The reason you pay extra is that there are 26 two-week periods in a year, but the amount of your payment is calculated as if there were 24. Essentially, you pay 2 extra two-week periods. In the example we've been using, making biweekly payments will get the mortgage paid off in 21 years and will save you $33,500 in interest. Think what would happen if you paid your mortgage biweekly *and* made a prepayment each year—perhaps using your income tax refund. The mortgage would be retired even sooner.

4. **Increase your monthly payment.**
   The extra paid beyond your scheduled amount goes directly to pay down the principal. You would need to confirm that your mortgage allows you to increase your monthly payments. If it doesn't, you could achieve the same goal by saving the extra portion of your salary each month and making a once-a-year prepayment if your mortgage permits.

5. **Shop for the best interest rate.**
   Because a mortgage is a lot of money borrowed for a long time, the effect of different rates is dramatic. Even half a per cent in interest means a difference of about $22,000 in what you pay over the life of the mortgage we've been using as an example. That's enough to make it worth the time and effort of shopping around.

6. **Make the largest down payment possible.**
   The availability of an extra amount of $25,000 or $100,000 might sound far-fetched, but could certainly be the result of an inheritance, for example. Using it to increase your down payment would be a means of investing the money for your long-term benefit since it will significantly reduce the over-all interest you pay on the mortgage.

Keep some money to cover your closing costs…

As compelling as the argument is for a large down payment, it's important not to put every penny into it since you will need some cash in reserve to cover ***closing costs***. Closing costs are expenses above and beyond the purchase price that must be paid in order for the deal to be completed. It is prudent to plan on keeping an amount equivalent to about 2% of the purchase price of the property. In our condo example, that would be a minimum of $5300 ($265,000 x 2%). If you aren't prepared you might end up, as one of my students reported, using a credit card at 19% interest to fill in the gap. That is a very expensive way to get the $5300 that caught you by surprise, and it will be hard to pay off once you have the additional expenses of being a homeowner.

In general, closing costs include a variety of fees, taxes, insurances, and adjustments which are required to complete the transaction and usually cost several hundred dollars each. Any or all of the following may apply in your situation. You can confirm with your realtor and lawyer which of these you should plan for and what they are likely to cost. Don't be embarrassed about asking—it only makes sense that you would know the costs before embarking on a transaction. Asking is a sign of strength, not weakness.

A ***property appraisal*** may be done to determine the value of the property. The appraiser provides a written report that becomes the basis for the mortgage lender's decision.

A ***home inspection*** is optional but highly recommended. This is a detailed assessment of the condition of the house and alerts you to fundamental construction flaws that make the property a risky purchase. It also alerts you to repairs that will be needed in the foreseeable future (replacing the roof, furnace, hot water tank, etc.), and provides you with information that will help you determine a reasonable price to offer.

A ***land survey*** establishes the exact boundaries of the property. Sometimes the existing survey is accepted and instead you pay for ***title insurance*** which would cover problems resulting from an incorrect existing survey. The *l**and transfer tax*** is the cost of changing ownership from the seller to the buyer.

Fire insurance on the building will need to be in place by the time you take possession. When you have a mortgage, the lender wants to be assured of recovering the outstanding loan if the property were damaged or lost due to fire.

Legal costs include the lawyer's fee for both service and disbursements. Disbursements are expenses that have been paid out on your behalf and must be repaid to the lawyer. These include registrations, searches, supplies, couriers, and such. The disbursements will be variable and your lawyer can give you an idea of what to expect.

Adjustments are reimbursement to the seller for prepaid bills. These are the closing costs that are most likely to catch first-time home buyers by surprise, yet the adjustment process makes sense when you think about it. The most common area of adjustment is property tax. If the seller has prepaid to the end of the tax year, and you are taking possession part way through, then you will need to reimburse the seller for taxes covering the period you are going to be living there. The lawyer will make the appropriate calculations and add the adjustment to the final statement of the transaction. That's why it can catch you by surprise—it suddenly appears on your final statement when you need to produce the money to settle the bill.

Who does what in a house sale?

Since buying a house requires interaction with a variety of professionals, it is useful to understand where each fits in the picture. You and the seller will individually hire a ***lawyer*** to act on your behalf. Your lawyer performs services such as reviewing your offer to purchase, searching the title, drawing up mortgage documents, doing the final accounting, and seeing that payment is made to the seller. You could do these things yourself, but it's a specialized area and costly mistakes could easily be made, so it usually makes sense to pay for legal services. Lawyers charge either a flat fee or by the hour. When interviewing them, it is quite within your rights to ask what the fee will be before committing to hire a particular lawyer.

The ***realtor*** is there to help you shop for your house and make an offer when you find one you'd like to buy. You are not required to have a realtor assisting you, but most people, especially first-time home buyers, find their services worthwhile. The realtor's fee is a percentage of the selling price and is borne by the seller. What this means in practice is that the selling price of a house is set high enough to cover the realtor's fee and the seller's desired profit. Another way of stating this is that the buyer pays, but indirectly, through the purchase price. If you buy a house that is "for sale by owner," the price does not include a realtor's fee.

A realtor is involved from the time you start looking at houses until you make an offer that is accepted by the seller. You should expect your realtor to be knowledgeable about the bylaws and services of the community, the real estate market in the area, and what is a reasonable price to pay for a given property. When you find something suitable, the realtor can help you decide what you will offer for it. (Houses are normally listed at a price above what the seller is willing to accept, on the understanding that there is a bargaining process involved.)

The realtor then helps you complete the offer to purchase. The offer specifies the purchase price and conditions of your offer, and is legally binding once you have signed it. You will be required to attach a deposit cheque made out to the seller's lawyer. The amount is generally somewhere between $2,000 and $10,000 depending on the market and the price of the property. Make sure you have enough money accessible in an account for which you have cheques so that this technicality does not hold up presenting your offer. The purpose of the deposit is to provide compensation to the seller if you back out of the deal along the way. In other words, if you fail to complete the deal, the seller keeps the deposit. That's only fair because the seller stops negotiating with other prospective buyers and gives up the possibility of other sales while your transaction is in progress.

Your realtor presents your offer to the seller, and reports back to you whether the offer is accepted or if there are further points for negotiation. In Canada, realtors do this on behalf of the buyer, who is not present while this meeting takes place. Practices vary in different countries, so check this out where you live. A good realtor will negotiate the best possible deal for you. This involves the purchase price and other important factors such as possession date, financing, and inclusions such as appliances. Remember, though: The realtor is also trying to get the best price for the property, as the realtor's commission is a percentage of that price. Consequently, you need to be clear about stating what *your* needs are in making the deal—that is, be prepared to look after your own interests rather than leaving it completely to the realtor.

Realtors and lawyers are both members of their respective professional associations and are governed by codes of ethics established by their associations. If you believe either has acted unethically, you can lodge a grievance with the association. Both are also bound by certain legal responsibilities. If these are not met, you would contact the level of government that administers the relevant legislation.

When buying a new home rather than a used one, you will be dealing with a representative of the ***builder or developer*** instead of with a realtor. The builder's representative is a salesperson for the builder and it will be up to you to look after your interests. With new homes, pricing tends to be less negotiable but you should certainly ask. In Canada, Goods and Services Tax (GST) is charged on new homes. Sometimes builders include GST in the purchase price and in other cases it is an additional amount included in your closing costs. It's important to know how your builder is handling GST so that you know exactly how much the property will cost you.

Historically, new home construction was fraught with difficulties for the buyer because developers sold homes and moved on, not always taking responsibility for poor quality workmanship and the resulting issues with the building. To address this, there are now a variety of new home warranty programs in Canada, covering certain structural defects in the building in the first few years. Such programs are voluntary and not all builders offer a new home warranty, so ask. If the answer is yes, you will also want to enquire about the cost—is the builder including it in the purchase price or will it be an additional cost. If the builder does not offer a warranty, you might wonder why.

Before signing any contract, the most important thing you can do is investigate the reputation of the builder. Start with an inquiry to your local Better Business Bureau, which is something that can be done online. See if there is a local homebuilders association and whether the builder is a member; if not, you should wonder why. Ask the builder to provide references from among its customers. Call those people and ask if they are willing to discuss their experience. Ask them about both the quality of workmanship and the level of service they received in cases where problems did arise. A very good question to ask: If you were doing this again, what would you do differently?

[i] "Average Residential Mortgage Lending Rate - 5 Year," (Canada Mortgage and Housing Corporation, quoted on Bank of Canada website), accessed October 3, 2012, http://www.bankofcanada.ca/wp-content/uploads/2010/09/selected_historical_page57_58.pdf

[ii] "Canadian Mortgage Payment Calculator," (CanEquity website), accessed October 4, 2012, http://www.canequity.com/mortgage-calculator

[iii] Gail Vaz-Oxlade, "House Poor," accessed October 4, 2012, http://www.gailvazoxlade.com/articles/home_sweet_home/house_poor.html

[iv] Mortgage calculator as above.

[v] Perry Goertzen, "How We Paid Off our House in Three Years," accessed October 4, 2012, http://www.moneyville.ca/article/991896