



THE FIRST-TIME BUYER

by Peter Dolezal [The Naked Homeowner](#)

Dreaming about buying your first home in Greater Victoria? Mission-impossible? Or is it?

With historically-high prices in our idyllic corner of Canada, I hear many residents, not yet fortunate enough to own a condo or house, despairing that they may never be able to escape the rental rut.

In many instances their concern is misplaced. What is needed in some cases is simply a clearer understanding of the various tools, available to first-time buyers, which may allow them to qualify for early ownership of that coveted first home.

How can the prospective first-timer qualify for a purchase? Let's use the example of a very nice two-bedroom condominium which, even in today's market, can be bought for around \$300,000.

Down Payment:

Until about two years ago, every buyer was required to make a minimum 5% down-payment to qualify for a CMHC or Genworth Financial-insured loan. This was mandatory before any front-line Lender, such as a bank, would advance a mortgage. Then the rules were eased, and zero down-payment became an option.

Unfortunately for the first-time buyer, the Federal government recently reversed itself. As of October 15, 2008, a 5% minimum down-payment is again required. A \$300,000 condominium purchase will require the purchaser to have at least \$15,000 down, plus several thousand dollars for closing costs.

Amortization Period:

About the same time two years ago, financial institutions began offering mortgage amortization periods for up to 40 years, thus stretching the previous maximum of 25 years. As of October 15, 2008, this maximum is reduced to 35 years.

On a \$285,000 mortgage, the 35-year option still offers the buyer a significant opportunity to reduce monthly payments from \$1658/month (25-year) to \$1430/month (35-year). This opens the door for many aspiring homeowners whose income would not qualify them for the higher of these monthly payments.

Borrowing from RRSP's:

For many years now, first-time buyers have qualified to borrow up to \$20,000 each from their RRSP account, without tax consequences if:

- The funds are used toward the down-payment on a personal residence;
- Repayment is made to their RRSP, of the amount borrowed, at a minimum 1/15 annually, beginning with the second year after the funds are first borrowed. Failing to do so will attract tax on the amount not repaid on schedule.

Property Transfer Tax:

A major cost of buying a home in British Columbia is the Property Transfer Tax which must be paid on closing of the purchase. On a \$300,000 purchase price, this amounts to \$5,000 – a hefty sum for the first-timer! Fortunately, the BC Government has exempted first-time buyers from this tax, as long as the value of the property purchased does not exceed \$425,000.

Why then do so many would-be purchasers not qualify, even if they have managed to save the 5% down-payment? Let's look at the qualification rules:

Credit Rating:

You need a solid credit-rating before a financial institution will lend you \$285,000, and CMHC or Genworth will insure the loan. If you are not able to meet this test, work on paying all your bills on time, so that a Lender will see you as a responsible borrower.

Gross Debt-Service Ratio:

Lenders will generally require that your proposed mortgage principal and interest payments, plus estimated property taxes, utility costs, and 50% of any strata fees, *not* exceed 32% of your *household* gross income.

If we assume a 5% fixed-rate mortgage with a 5-year term and 35-year amortization on a \$285,000 mortgage, this will result in the monthly principal and interest payment of \$1430. If we add \$300 per month for property taxes, utilities and half of the strata fee, the total monthly obligation would become \$1730.

These numbers mean that to meet this lending test, you (and your partner) would have to show a *monthly* gross household income of \$5406 – not an impossible number for two adults, with good jobs, in our area.

Total Debt-Service Ratio:

Unfortunately, even if you meet the above criteria, there is one final hurdle. Lenders want to see that your total debt-service obligations, such as monthly car loan and credit card payments, when added to the above-listed costs of living in your new home, do not exceed 40% of your *household* gross income. If your household gross income is \$5406, this means that your total allowable monthly payments can not exceed \$2162. If the home-cost portion comes to \$1730/month, as in our example, this means that you may spend no more than \$432/month for all other debt repayment obligations. If your monthly payments are greater, you will *not* qualify for the \$285,000 mortgage.

If you fail to meet this second test you will, in order to qualify for this loan, first need to either:

- 1) reduce these other debts;
- 2) increase your income;
- 3) or a combination of both.

Closing Costs:

Remember, even after you qualify for your desired mortgage, *some* extra cash will be required to buy your first home. The legal costs of closing, the necessary inspection, and lender-appraisal costs, could well total \$1500 to \$2000 before you move into that wonderful first home.

If any of these issues disqualify you from the desired loan, don't despair.

If you can't start out with that \$300,000 condo, lower your sights. More modest one-bedroom condos are available for \$225,000 to \$250,000. To qualify will be much easier, and you will at least be in the market. Don't give up your dream until you check out *all* the possibilities!

Run your own numbers. See if you can qualify, and for how much. Check around for the best type of mortgage and interest rate.

Remember, because yours is a 100% insured loan, your Lender is assuming zero risk of any default, and should be willing to grant you the best deal possible on your mortgage. An extra 1% reduction in your rate will not only save you thousands of dollars over the term of your mortgage, but also, may make the difference between your qualifying, or not qualifying, for the amount of loan you require.