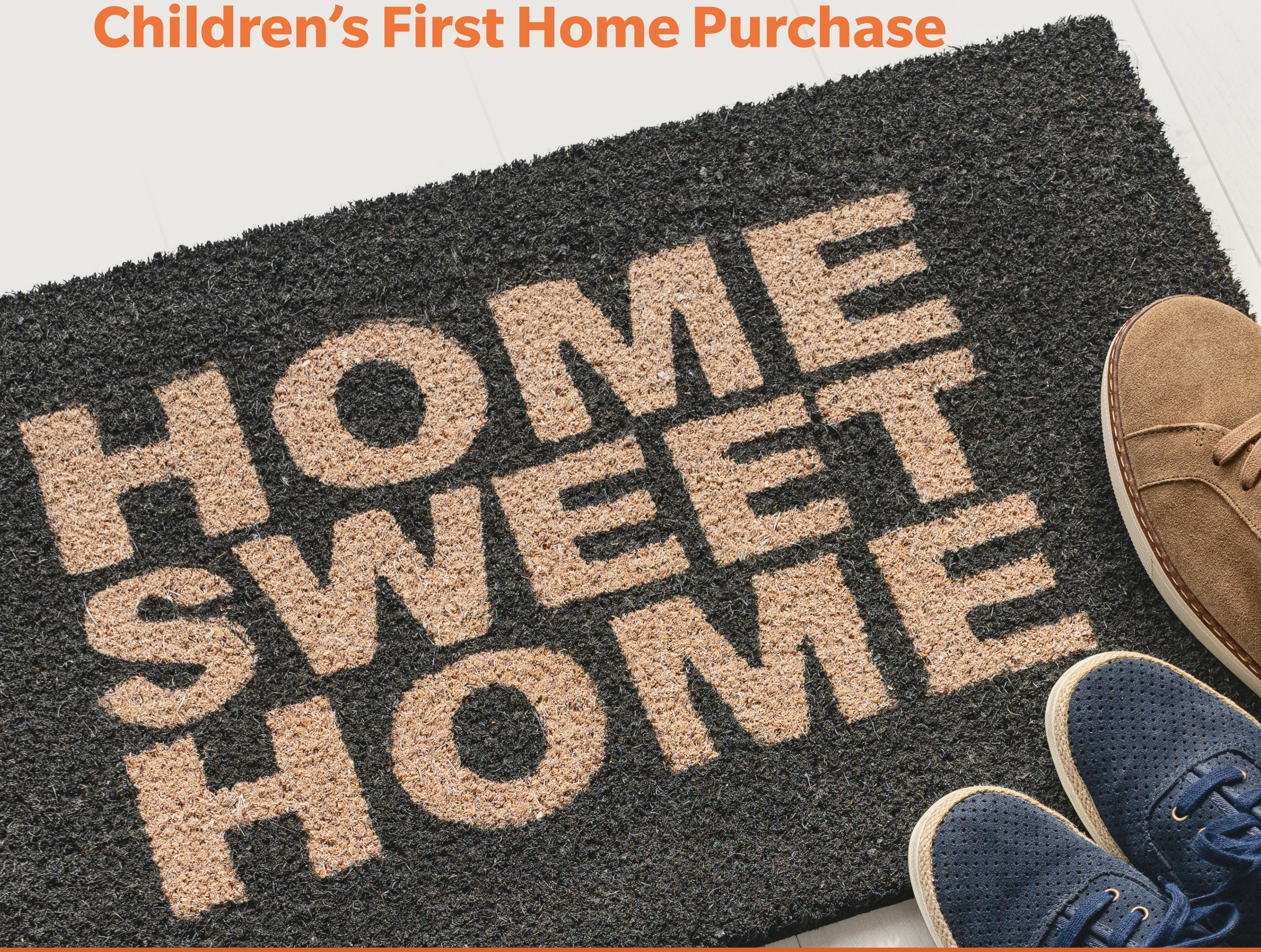
Unlocking Home-Ownership

A Guide for Parents Helping Their Children's First Home Purchase



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Opening Doors to Home-Ownership

Home-Ownership is a symbol of stability and happiness and is a long-term investment that provides security and a solid financial future. That's why most Canadians dream of owning a home. However, getting into the market has become increasingly challenging for first-time buyers because of high home prices, tight supply and the rising cost of living.

The difficulty of achieving Home-Ownership is evident in the changing profile of first-time buyers. The mean age in Canada to buy a first home now stands at 34. The percentage of first-time buyers under the age of 30 has fallen from 28% in 2021 to 24%, and the portion of first-time buyers over the age of 35 is now 43%, with 9% of first-time buyers within that group aged 41-45. (Source: Sagen First-Time Buyer Survey March 2022, conducted by Environics)

The study also found that 68% of homebuyers indicated they were concerned they would miss out on the property they wanted because of a lack of down payment, a noticeable jump from 56% just four years ago.

As parents, we want our kids to have the best opportunities to achieve this goal so the desire to help can be strong. But it can be a significant financial and emotional investment and challenging to determine the best course of action.

Wealth inequality in Canada is not just a story of rich versus poor, it is one of homeowners versus non-homeowners. The average net worth of homeowners born between 1955 and 1964 is now more than $1.4 million. This is 6.3 times that of non-homeowners born during the same time.

Source: TD Economics: Digging Beneath the Surface: Is Housing Perpetuating a Wealth Divide in Canada? Oct 2022.

That's why we've created this Guide - to explore the reality of the Canadian housing market for first-time buyers and provide parents with a practical resource on how to best help their children achieve Home-Ownership while minimizing risk to themselves and ensuring the best outcome.
TMG The Mortgage Group is here to support you every step of the way.

The Challenges of Buying a Home in Canada

Today's first-time homebuyers are confronted with a housing market that has changed significantly since their parents bought their first homes. Understanding these challenges is important because they are complex and difficult to overcome.

First-time buyers face layered difficulty that makes it challenging for them to enter the housing market without parental assistance.

But keep in mind that these same challenges point to a long-term housing market that will continue to see significant upside potential, which is why buying that first home sooner rather than later is an important financial goal. Let's look at the primary housing market challenges:

A Persistent Shortage of Housing Coupled with Strong Immigration

New home development has failed to keep up with demand, resulting in a persistent shortage of housing. In 2022, CMHC noted that Canada needed to construct 3.5 million more homes by 2030 to achieve home affordability for Canadians, which is in addition to the 19 million housing units that were already expected to be completed by 2030. However, according to CMHC data, housing starts are on a noticeable decline, and we may not even reach the original 19 million new housing units by 2030.

At the same time, immigration targets have increased, adding a further strain on the housing market, with 465,000 new permanent residents targeted for 2023, followed by 485,000 in 2024, and eventually 500,000 new arrivals each year starting in 2025.

Statistics Canada reported that the Canadian population reached more than 40 million as of June 16, 2023. This milestone came faster than expected, with 1.050 million people arriving in 2022, the first time our population grew by over 1 million people in a single year, with mostly permanent and temporary foreign workers.

While our population is now growing at a record-setting pace, we don't have the housing infrastructure even though immigration is vital for our job market, economy, and multicultural heritage.

The resulting scarcity from our chronic lack of supply leads to a very competitive real estate market and sometimes bidding wars, creating frustration, and making it very difficult for first-time buyers to find affordable options.

The Great Wealth Transfer – Increasingly Parents Are Helping

This Guide aims to highlight the importance of parental assistance to achieving first-time Home-Ownership, yet this is also a driver of higher real estate prices. Baby boomers are increasingly transferring wealth to their children through Home-Ownership assistance.

According to Sagen's March 2022 First-Time Buyer Survey (conducted by Environics), almost 60% of first-time buyers reported they received financial support from their families so they could buy their homes. Of those who received this assistance:

- 35% received a lump sum payment
- 25% reported getting help with their monthly payments
- 45% said the assistance received was a gift, while 37% indicated that the money is a loan that must be repaid.
- 10% had either a parent or relative co-sign the mortgage with them
- 44% said they would have had to delay purchasing if they didn't receive this assistance, and potentially lose out on property appreciation.

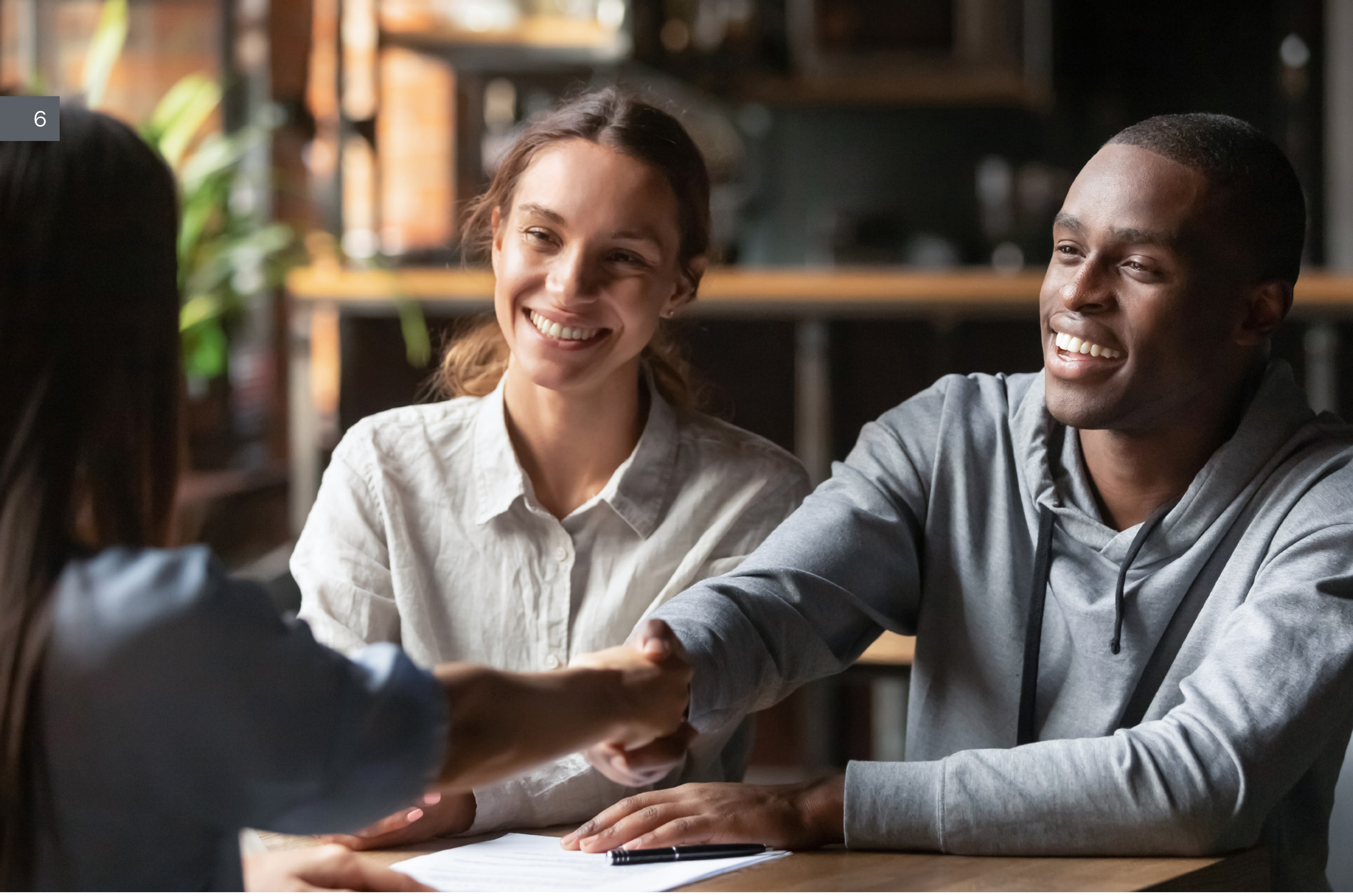
The increasing trend of parental assistance in achieving first-time Home-Ownership brings both benefits and challenges to the real estate market. While it helps aspiring first-time homebuyers, it also is a contributor to higher real estate prices as young people increasingly turn to their parents for a way into an expensive housing market that will likely continue its upward trend. The financial repercussions of not getting into the market are simply too severe over the long term.

Difficulty Saving for a Down Payment

When you consider the current level of home prices, the minimum down payment requirement can be very onerous. Add in inflation, the high cost of rent, and student loan payments and you can see why saving for a large down payment is a growing frustration for first-time homebuyers.

Purchase Price	Minimum Down payment
Less than $500,000	5%
$500K - $1M	5% first $500,000 10% on the balance
$1M or more	20+%

When parents help their children increase their down payment, they are also helping them potentially pay less mortgage default insurance. For down payments between 5% and 20%, mortgage default insurance is required, with the premium based on the mortgage amount. The premium is 4% for a 5% down payment, 3.1% for a 10% down and gradually decreasing to 2.8% for a 15% down payment. However, at a 20+% down payment, there is no need for default mortgage insurance. While this premium is amortized over the life of the mortgage, being able to minimize the amount paid offers first-time buyers a sizeable long-term benefit.



Strategies for Assisting Your Children

There are several ways you can support your child's Home-Ownership dreams. Here is an overview of each with some tips to help you decide on the best strategy.

You will also want to look at concerns surrounding property law if your child is married. Additionally, if you are selling non-registered assets there could be capital gains tax implications.

Gifted Down payment

A gifted down payment involves contributing funds to cover some or all of your child's down payment and closing costs. This option can significantly decrease the financial burden on your child and increase their eligibility for a mortgage. It also can significantly help your child enter the housing market sooner, allowing them to benefit from the property's appreciation in value.

It's important to note that the lender will require a gift letter stating that the funds are indeed a gift and not a loan. The lender may also want to see evidence of the source of funds from the person who is gifting the money.

It's important to consider property law if your child is in a common-law relationship or married. Understanding spousal rights and various separation scenarios can help safeguard everyone's interests. Seek expert counsel from a family lawyer focused on real estate matters for valuable guidance.

Assisting with Monthly Mortgage Payments

Helping your child with their monthly mortgage payments may be an easier way to budget your assistance if you have the regular cash flow to help. This way you don't have to come up with a large lump sum and have to sell any assists. Here again, the money becomes your child's property, which means separation from their spouse could have property law implications.

Structuring Your Assistance as a Loan

Opting for a loan instead of a direct gift has its advantages. You can structure it as an interest-free loan, or a loan with a set interest rate, and place a lien on the property. If applicable, the loan agreement will protect those funds from creditors in the unfortunate event of a small business failure.

Additionally, a documented loan can be more beneficial in situations of divorce. A gifted down payment can be subject to a 50% division of the matrimonial home. If structured as a loan, the loan can be repaid when the home is sold and used to assist your child once again in purchasing a new one.

One of the downfalls of structuring your assistance as a loan is that the loan agreement is considered a liability by lenders, which can affect debt servicing ratios and the ability of your child to qualify for the mortgage.

Becoming a Co-Signor

Becoming a co-signor for your child's mortgage helps the applicant qualify for a mortgage, get favourable loan terms and possibly expand their borrowing capacity because the co-signor's financial position strengthens the application. In fact, your finances will be under the same scrutiny by the lender as your child's finances. You may need to show a stable income, limited debt and a good credit score.

As a co-signor, you go on title with the applicant(s) and are responsible for the mortgage payments if your child can't pay.

The primary benefit to co-signing is that you don't have to come up with a large lump sum or have a monthly cash outlay. But even though you aren't contributing funds, you are still making a financial commitment because your financial situation is attached to the child's mortgage and your credit score and future ability to borrow may be impacted. That's why having candid discussions about financial duties and fall-back plans is vital, and parents should assess their credit scores, financial position and goals before agreeing to co-sign.

It's also important to note that co-signing may limit future ability to get additional mortgage financing or purchase another property, so before co-signing, consult a professional. Additionally, some parents wonder if they can be a guarantor instead of a co-signor which means not going on title and having ownership risk, but still guaranteeing that payments will be met. In most cases, you will need to become a co-signor because not all lenders will allow for a guarantor.

The Stress Test has increased the need for a co-signor! The stress test requires that applicants prove they can afford mortgage payments at the greater of 5.25% or the contract rate plus 2%. Payments are still based on the contract rate, but qualifying must be done at this higher rate. In a rising rate environment, mortgage qualifying becomes a more difficult task to accomplish. When parents co-sign, their income is added to the application, which makes it easier to pass this test. It also helps when the applicant has poor credit or a lack of credit history.

Reverse Mortgage

With so many challenges facing first-time buyers, a reverse mortgage allows older generations to use their home equity to provide down payment assistance. It's an opportunity to spend their money when it can make the most difference and when they can see and participate in the joy it can bring.

Essentially, with a reverse mortgage, the homeowner borrows money against the equity of their home, with no repayment required if they continue to live in the home. This can provide an influx of cash for a parent or grandparent to give to the child to assist with a down payment or other expenses associated with buying a home. Additionally, since no payments are required with a reverse mortgage, there may be additional disposable income to assist the child in other ways, such as helping with mortgage payments or providing additional financial support.

However, it's important to note that reverse mortgages can come with certain risks and fees, so it's important to thoroughly research the pros and cons before deciding.

Protecting Parental Financial Well-Being

Certainly, parents want to protect their own financial security before helping their children buy a home, particularly as they approach retirement. Life is unpredictable, and unexpected events such as medical emergencies, job loss or economic downturns can significantly impact financial stability. Parents must be equipped to handle such situations, which is why an emergency fund and a strong retirement financial plan are important.

By considering their own financial well-being, parents can safeguard their retirement plans, maintain their standard of living and not become a burden on their children later in life. Ultimately, parents should strike a balance between helping their children achieve their Home-Ownership dreams while maintaining their own financial well-being.

Federal Government Programs for First-Time Homebuyers

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First-Home Savings Account

The FHSA allows qualified first-time homebuyers to contribute $8,000 per year for 5 years into a tax-free savings account for a total of $40,000 or $80,000 for a couple. Like an RRSP, contributions are tax-deductible and, like a TFSA, all withdrawals which include investment income are non-taxable. Additionally, there is no requirement to repay as there is with the RRSP Home Buyer's Plan (HBP).

Unused contribution amounts can be carried forward to the next year, but you can only catch up by $8,000 in any given year.

If the funds aren't used for a home purchase, there is the option of making a taxable withdrawal or transferring tax-free to an RRSP, so the plan holder is never locked out from accessing these funds.

For parents thinking about supporting their child's home-buying journey in the future, this is a fantastic way to do it. You can contribute up to $8,000 per year ($40,000 in total), giving your child the contributions to their plan and a bonus tax deduction for the amount you contribute, which can significantly boost their down payment savings - a big win for their future home buying plans!

RRSP Home Buyers' Plan

Certainly, parents want to protect their own savings. The Federal Home Buyers Program (HBP) allows first-time homebuyers to access up to $35,000 ($70,00 for couples) tax-free from their RRSPs if the funds have been inside the registered retirement plan for at least 90 days – repayable over 15 years. It's a great way to get a jumpstart on Home-Ownership! And great news – the HBP can be used in conjunction with the FHSA!

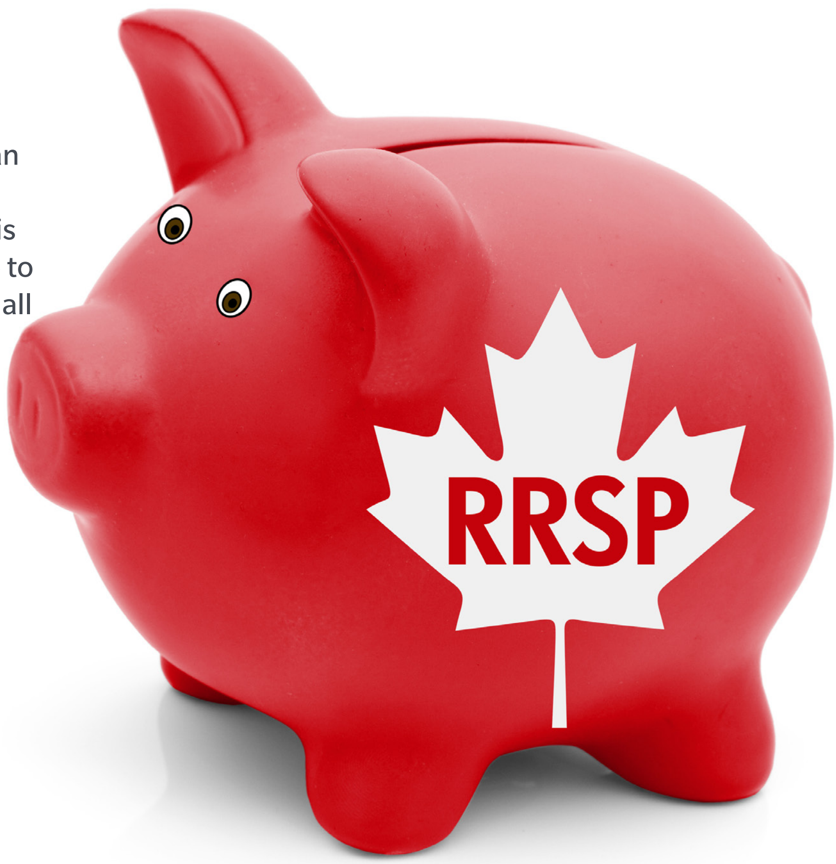
If contribution room is available, there's an opportunity to potentially increase the available funds for the down payment. When savings are deposited into the RRSP before the March 1st deadline, the resulting tax refund can further bolster the down payment amount or help with closing costs. The funds can be withdrawn after being in the account for 90 days. Important to note that the withdrawn amounts need to be repaid according to a repayment plan over 15 years, or the funds become taxable.

First-Time Home Buyer Tax Credit

Remember this at tax time! First-time buyers can claim a portion of their home purchase on their personal tax return for the year of purchase. This $10,000 tax credit can give first-time buyers up to $1,500 in federal tax relief, which can help with all kinds of first-home expenses.

First Time Buyer Incentive Program

This shared equity program with the federal government helps first-time buyers get into the market by providing 5 percent of the cost of an existing home, or 10 percent of the purchase price of a new home. The incentive must be paid in full after 25 years, or whenever the home is sold. The full amount can be paid voluntarily at any time. This program hasn't been very popular because people are reluctant to share equity gains with the government, especially if they undertake renovations.



Other Important Considerations

In today's complex mortgage landscape, a lot goes into a successful mortgage application. Here are some important steps that should be considered before your child embarks on a home search.

Importance of a Pre-Approval

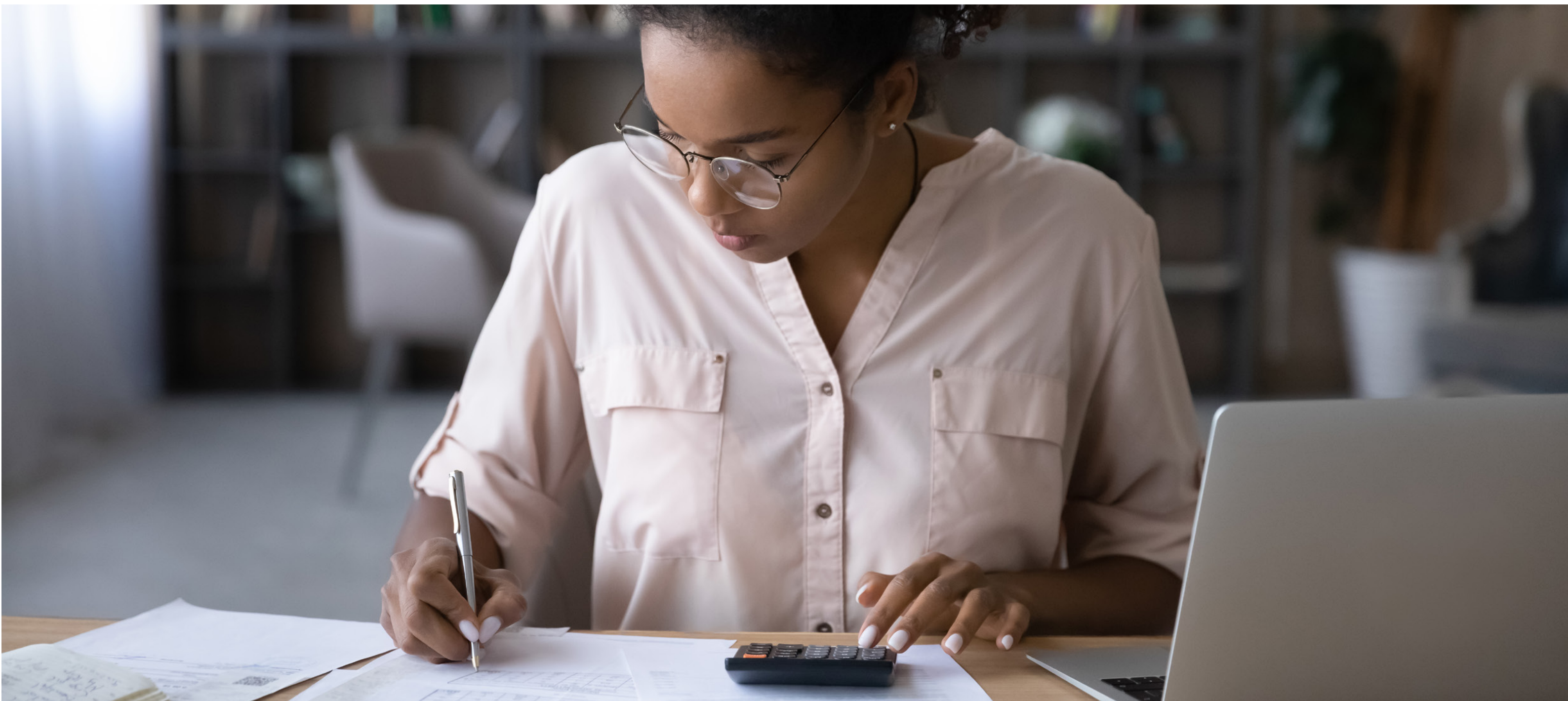
Getting a mortgage pre-approval before house shopping is a wise move. A pre-approval provides the exact amount the applicants will qualify for and what the monthly payment will be. An interest rate is also guaranteed for a set period such as 90 to 120 days. The pre-approval will not be an actual mortgage approval or guarantee of financing since the lender will need to assess the property and verify the applicant's financial situation and down payment at the time of an accepted offer.

Credit Score Monitoring

First-time buyers often aren't aware of how important it is to monitor their credit score prior to submitting a mortgage application. Lenders use credit scores to assess how responsible the applicants are as borrowers. Credit scores range from 300-900; with anything above 680 considered excellent. The most important behaviour to ensure good credit is paying bills on time, all the time. A bill should never go past due. Credit scores can be ordered online from Equifax or TransUnion, but be cautious to have your mortgage professional review your credit because the scores available through online free credit checks, can sometimes differ from the ones banks use.

Preparing a Budget

Having a detailed budget will help ensure there are no surprises down the road. It should not only cover the monthly mortgage payments but also other costs like utility bills, home insurance, property taxes, strata/condo fees, ongoing maintenance, etc. Closing costs are an important part of the final home purchase costs and include legal fees, appraisal fee, home inspection, title insurance, disbursements, adjustments, land transfer taxes and more. About 2-4% of the home's purchase price should be budgeted for closing costs. The lender will want to see that money has been set aside for these costs.



Having a Strong Team

Establishing a capable away team is essential to ensure a professional and efficient home-buying experience. Your team should comprise a Mortgage Broker, Realtor, Home Inspector and Lawyer.

Mortgage Broker

Your TMG Mortgage Broker has access to over 50 lenders, including major Banks, credit unions, and national, local and private lenders. Having this choice is the only way you can be sure to get the best deal from the mortgage marketplace. If you just go to the Bank, you only get their line of mortgage products to choose from.

Your Broker also has expertise in navigating the mortgage application process and will negotiate on your behalf to secure better rates and terms, potentially saving thousands of dollars over the long term. You also get invaluable advice like making sure offers to purchase include a financing condition, which ensures there are a few days to finalize the mortgage with the lender and be 100% confident financing is secured.

Getting a mortgage is a big financial commitment. Using the services of a mortgage broker is the best way to ensure full confidence in your decision-making process. It's a sensible choice that can benefit your child for years to come.

Realtor

An experienced real estate agent well-versed in the local area can offer valuable guidance throughout the home buying journey. Your Realtor will offer advice on suitable properties to view, navigate the purchase documents, negotiate the best price, and protect the interests of all involved.

Home Inspector

Securing a professional home inspection is crucial to detect any underlying issues with the property. Neglecting this significant step might lead to unexpected and costly repairs in the future. If the home inspection reveals major issues, you can get out of the deal if your offer was subject to a home inspection.

Lawyer

Having a good lawyer to close your home is necessary to protect your legal rights and ensure that the transaction is completed in compliance with all relevant laws and regulations.

If you need a referral to top-notch professionals in your area, your TMG Mortgage Broker can help.

Securing Dreams: Achieving Home-Ownership Success!

Becoming a homeowner in Canada has become increasingly challenging for first-time buyers.

Parents are playing an increasingly important role in supporting their children's first home purchase, and this guide has provided practical tips for how parents can provide that help while minimizing risks. By considering options such as gifted down payment, structuring assistance as a loan, or becoming a co-signor, parents can help their children enter the market sooner and benefit from property appreciation.

However, it is essential for parents to prioritize their own financial well-being and seek expert advice to ensure a balanced approach that safeguards both their future and their children's Home-Ownership aspirations.

Together, parents and children can navigate the challenges of the Canadian housing market so that both can enjoy a prosperous and secure future. In some cases, it's the only way Home-Ownership success can be achieved by the next generation!

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