

How do mortgage payment deferrals work?



If COVID-19 and the resulting lockdown are affecting your employment situation and therefore your finances, you may be feeling strapped for cash with less money to make your payments. We understand and are here to offer you solutions.

If you have a mortgage and are having a hard time making ends meet, you might want to think about asking for a payment deferral on your loan. You're not alone and you wouldn't be among the first to do this. Several hundreds of thousands of mortgage payment deferrals have already been requested at banking institutions across Canada," says Darren King, one of our experts.

Before submitting a request, here are a few explanations of what's involved. You'll see, it's not complicated and if you have any questions, feel free to contact us.

Deferring mortgage payments 101

First of all, deferring mortgage payments is nothing new. While the scope of the phenomenon is unprecedented, payment deferrals have been granted in the past, particularly when natural disasters, like floods, have occurred in certain regions.

The idea is rather simple. For a certain period, let's say 3 to 6 months, you won't have any mortgage payments (principal and interest). You take a break, then start again. The payments that would normally have been made are deferred to a later date. The good news: more money in your pocket right now.

However, interest continues to accrue during these months of "relief."

During the relief period, debt is repaid at a slower pace than planned, which means additional interest. Of course, when you negotiate your next term, the amount you owe will be greater than you may have expected, so the payments will increase even if the interest rate stays the same.

If you owe \$10,000 and your payment is \$500 per month, for example, this \$500 may be split in two. You pay \$250 in interest (what it costs to borrow) and \$250 in principal (the portion that repays the debt). So, $\$10,000 - \250 (the portion that repays the debt) = $\$9,750$, the amount still owing. For your next payment, interest will apply on $\$9,750$.

Since you're not repaying any principal because you obtained a deferral, interest on the next payment will be calculated on \$10,000 rather than \$9,750. Given that the amount you owe is higher, you'll have to pay a bit more interest.

Example: 3% of \$10,000 is \$300 and 3% of \$9,750 is \$292.50, which is lower.

Deferring mortgage payments: why is interest still charged?

Having to pay more interest is never good news. So why do we continue to charge it?

It's simple. We have no choice but to continue charging interest. It's as simple as that. "If we stopped," explains Mr. King, "our loans would be considered non-performing and we would have to keep more money in our vaults. If we did that, we would take liquidity out of the market and wouldn't be able to lend to as many people." That would be a very bad idea at a time when we need to invest to support the economy.

What's more, you benefit from this. If interest continues to accrue, your credit score won't be affected, and we won't charge interest on interest during the deferral period.

Deferring mortgage payments: how to get "back to normal"

If your financial situation improves, you can increase your payments to up to twice their initial amount (principal and interest) to speed up repayment of your mortgage loan," explains Jonathan Haziza, another one of our experts.

This option is revocable at any time, so you can always change your mind! You could also make a large lump-sum payment on principal or even increase the frequency of your payments. A number of options exist to reduce the burden of your debt.

Deferring mortgage payments: it's not a vacation, but it's not the end of the world either

Let's be clear: it's always better to repay a debt as soon as possible. However, if your financial situation has deteriorated, deferring your mortgage payments could be a good way to help you pay your basic expenses. "Before declaring bankruptcy or submitting a consumer proposal, ask to defer," says Darren King. "Just remember that it's not a vacation. The money will have to be repaid eventually."

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