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MINISTRY OF MUNICIPAL AFFAIRS AND HOUSING
HOUSING DIVISION

Social Housing *mortgage news*

Inside this issue

Welcome to the first edition of the social housing mortgage newsletter, prepared by the Housing Funding and Risk Management Branch of the Ministry's Housing Division.

The Housing Funding and Risk Management Branch provides advice on various social housing finance elements including:

- coordinating the mortgage renewal process for social housing projects;
- engaging in policy influence with federal government;
- working closely with Service Managers to provide advice and guidance on asset management, asset leveraging, financing of social housing and ministerial consent requirements;
- undertaking financial administration and risk management activities.

Through this newsletter, the branch intends to keep Service Managers in Ontario informed about recent news and developments in the area of social housing mortgages.

If you have any questions regarding articles in the newsletter, please contact Erich Freiler, Manager, Housing Funding and Risk Management Branch at (416) 585-6193 or Erich.Freiler@ontario.ca.

The Ins and Outs of Ontario's Competitive Financing Renewal Process

Mortgage payments are one of the largest monthly expenditures for housing providers. Increase in mortgage costs will increase costs for subsidies that Service Managers flow to housing providers.

This article will provide a brief overview of Ontario's Competitive Financing Renewal Process (OCFRP) and will inform readers about recent changes to the National Housing Act Mortgage-backed Securities Program.

The objective of Ontario's Competitive Financing Renewal Process, administered by the Ministry of Municipal Affairs and Housing, is to create a transparent bulk mortgage renewal system, and to obtain the least costly sources of funds for social housing mortgages.

Every month, social housing mortgages provided by lending institutions (capital market lenders) that come up for renewal are placed in "group terms" and offered for tender to National Housing Act-approved lending institutions.

The Ministry of Municipal Affairs and Housing and the Ontario Financing Authority (OFA) work together to oversee the mortgage tender process. Service Managers and housing providers determine the renewal terms. Lending institutions submit bids and the OFA selects the winning tender with the lowest interest rate. Service Managers and housing providers are then notified as to who the lender for the renewed mortgage is and the new interest rate.

So, what do some lending institutions do with these mortgages? Under the National Housing Act Mortgage-Backed Securities Program, lending institutions can combine individual mortgages with similar characteristics in a pool and sell them to investors as securities. Securities issued under the National Housing Act Mortgage-Backed Securities Program are guaranteed by Canada Mortgage and Housing Corporation (CMHC) making them attractive to investors.

- The National Housing Act Mortgage-Backed Securities Program has a number of different pools (e.g. Social Housing, Homeowner, Multiple-family, etc.).

On August 1, 2013, CMHC announced a dollar cap on providing guarantees for the new securities issued under the National Housing Act Mortgage-backed Securities Program.
It was expected that following the announcement, the number of lending institutions submitting tenders to renew social housing mortgages would decrease, resulting in lesser competition and higher mortgage costs on renewed mortgages.

The Ministry of Municipal Affairs and Housing communicated these concerns to Canada Mortgage and Housing Corporation. The Ministry also engaged in conversations with the Province of British Columbia who has a similar mortgage renewal process to Ontario's.

On August 30, 2013, Canada Mortgage and Housing Corporation issued additional instructions to lending institutions stating that the cap on <u>does not</u> apply to pools containing social housing mortgages (see attachment).

This is good news for Service Managers and housing providers because many large lending institutions will continue to participate in the Ontario's Competitive Financing Renewal Process and will continue to provide cost-efficient funds for renewing social housing mortgages.

Refinancing Social Housing Mortgages – Matters to Consider

As the administrators of Ontario's social housing stock, Service Managers work closely with housing providers to optimize existing resources, find operating efficiencies and ensure the long-term sustainability of the social housing portfolio.

In these efforts, some Service Managers and housing providers may ask themselves if refinancing existing social housing mortgages is an option for them.

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Refinancing Social Housing Mortgages – Matters to Consider

- Refinancing refers to the replacement of an existing mortgage obligation with another mortgage obligation under different terms, possibly including a higher mortgage amount and a longer repayment schedule.

Existing social housing mortgages fall into two broad categories: 1) provided by CMHC as a direct lender; and 2) provided by lending institutions.

Approximately 28% of social housing mortgages are currently provided by CMHC and 72% are provided by private lending institutions.

Refinancing existing mortgages can make good financial and business sense in some cases and not in other cases.

Below are matters Service Managers and housing providers should consider:

<u>Original mortgage agreement</u>
Read the mortgage document. Understanding rules and provisions for existing mortgages is important. For example, mortgage documents may provide for early payout.

<u>Mortgage renewal timing</u>
Like a homeowner, knowing when a mortgage is being renewed is essential. It makes a good sense to pay out a mortgage on the day of renewal as this will not trigger a prepayment penalty. Note that some CMHC-provided mortgages have long terms and do not renew (e.g. Section 26 and Section 27 mortgages with 50-year terms).

<u>Rationale for mortgage refinancing</u>
Determining the purpose for refinancing is an essential part in the decision making process. Is refinancing being considered for the purposes of generating capital to undertake capital renovations? Or is refinancing being considered for some other reason?

<u>Eligibility for federal funding</u>
In certain circumstances, refinancing existing social housing mortgages can affect a project's eligibility to receive further federal subsidies. For example, once a Section 95 mortgage is fully retired, the project operating agreement automatically nullifies itself, ending CMHC's obligation to provide a subsidy. Service Managers and housing providers should talk to Ministry staff to determine federal funding implications.

<u>Ability to repay</u>
Refinancing an existing mortgage may be the best option to achieve a stated objective (e.g. regeneration). However, can the housing provider afford it? Will the housing provider be able to demonstrate to the lender a solid financial record and the necessary revenue stream (cash flow) to service the new stream of debt payments?

<u>Mortgage portability</u>
Porting a mortgage means taking a current mortgage and any additional collateral pledges (e.g. rents and leases), with its rates and terms, and moving it to another property. Porting a mortgage can help a housing provider to save money when the existing mortgage rate is lower than the current rate. Furthermore, porting an existing mortgage can allow the housing provider to save on prepayment penalties. Note that some lenders allow porting and some do not.

Generally, porting CMHC provided mortgages is easier then porting capital market lender provided mortgages that are part of a mortgage-backed securities pool.

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Refinancing Social Housing Mortgages – Matters to Consider

Secondary financing

Secondary financing refers to a second loan on a property that already has a mortgage. Secondary financing can be used when the borrower doesn't want to refinance their existing first mortgage. One example of secondary financing is a non-performing second mortgage, a mortgage where payments commence once the first mortgage is paid in full.

The first mortgage has a priority over a second mortgage and a lender of the first mortgage has to agree to secondary financing. A second mortgage forms a second encumbrance against the property. Usually, the interest rate associated with secondary financing is higher. Housing providers should look at their specific circumstances and consider all financial and non-financial implications before deciding if secondary financing is an option for them.

Timing and Ministerial Consent Considerations

Once the decision to pay out the existing mortgage and to refinance is made, significant staff and time commitments will be required to implement the decision. Consider starting the process early and allow for 6-12 months before a proposed transaction date to find a suitable new lender, prepare the necessary documents and complete legal review.

Previously, Service Managers had to seek Ministerial consent for financing and other changes to social housing properties. As Service Managers have the experience to make locally relevant decisions, they now have the authority under *the Housing Services Act* to make consent decisions on provider mortgage financing. Service Managers should notify the Housing Funding and Risk Management Branch within 10 days of making such a decision on refinancing/remortgaging. Note that Ministerial consent is still required if Service Managers and housing providers want to sell or transfer social housing properties developed under provincial, federal or federal/provincial programs.

Housing Funding and Risk Management Branch staff will happily assist housing providers and Service Managers who are looking to make informed decisions about financing options.

Please send your enquiries to Erich Freiler, Manager, Housing Funding and Risk Management Branch at Erich.Freiler@ontario.ca.

Appendix A

Allocation Methodology for New Guarantees of Market NHA MBS (attached)