



Mr. Jeremy Rudin
General Director
Finance Canada
FSP - Assistant Deputy Minister's Office
140 O'Connor Street
Ottawa, Ontario
K1A 0G5

April 28, 2008

Dear Mr. Rudin,

RE: FEDERAL GOVERNMENT REVIEW OF THE SCOPE OF THE MORTGAGE INSURANCE GUARANTEE

This letter is a follow up to your recent discussions with the credit union system's National Lenders Committee (NLC) in regard to the Federal Government review of the mortgage insurance guarantee. We wish to thank you for the opportunity to discuss this issue with you and we submit the following comments for consideration by the Department of Finance as it proceeds with its work. The comments outlined below do not address every issue raised in our discussions but reflect the issues of most concern to members of the NLC.

Credit Union Central of Canada (Canadian Central) agrees that it is prudent to review the scope and parameters of the current mortgage insurance guarantee given that (a) the Canadian market has recently seen the entrance of the new private mortgage insurance companies (b) the recent innovation in the mortgage market and (c) the current difficulties being experienced in the U.S. mortgage market. Furthermore, we agree that it is appropriate, when carrying out such a review, to consider parameters such as acceptable loan to value (LTV) ratios, allowable amortization periods, appropriate documentation and the use of structured instruments.

However, having considered the issues raised in our recent discussions, Canadian Central recommends that the Federal Government proceed cautiously with any changes to the government's current mortgage insurance guarantee framework. In our view, it may be too early to determine the impact of new players and new products on the mortgage market and currently there is little evidence that that recent changes have significantly increased the overall financial risk in the market¹. Furthermore, we are not aware of any evidence that there has been the questionable mortgage

¹ In fact, the April 2008 IMF *World Economic Outlook* indicates that Canada's outstanding mortgage debt as a percentage of GDP has grown in a relatively moderate fashion since 1983 and is in line with the averages for most OECD countries. See: International Monetary Fund. (April, 2008) *World Economic Outlook: Housing and the Business Cycle*. p. 105. The same paper indicates that Canada's current housing market is one of the least vulnerable to a housing market price correction in the OECD since price rises are in line with other economic fundamentals (see p. 113).

administrative practices in the Canadian market that has been recently revealed in the United States (e.g. the “liar loan” phenomenon). That said, Canadian Central is concerned that, if the Federal Government decides to significantly restrict the coverage of the current government mortgage guarantee and introduce further administrative procedures for the program, the mortgage market may be disrupted and access to affordable housing financing could be curtailed for some Canadians.

The possibility of restricting the government guarantee in regard to mortgages with longer amortization periods (30 to 40 years) is of particular concern to credit unions. As you know, recent innovations have introduced these products into Canada and they have proven to be popular with Canadian homebuyers – especially first time home buyers. In fact, of all mortgages taken out in Canada in 2007, 37 per cent had an amortization longer than 25 years. In a context where in some locales (e.g. Vancouver and Toronto) housing prices have been increasing faster than household incomes, the availability of longer term amortizations has been of great assistance to first-time homebuyers. Average amortization periods longer than 25 years are also seen in a number of European countries and the United States and are not unusual nor apparently a source of concern.² If the Government of Canada were to remove the mortgage guarantee from such longer term amortizations it is likely that, in some markets, many first time home buyers would face significant difficulties purchasing a residence particularly if such financing was made available at a significantly higher cost.

Canadian Central is of the view that a legitimate area of concern may relate to situations where the government mortgage insurance guarantee is supporting speculative purchasers taking out longer term amortizations for very high ratio mortgages with a view to “flipping” properties in an active market. Canadian Central recognizes that it is not an appropriate role for government policy and could expose the government to significant liabilities in a downturn. However, rather than remove the guarantee from longer term amortizations, it may be possible to innovate in this area and seek to link the length of amortization with a maximum allowable LTV ratio. For example, a homebuyer seeking to purchase a home with a 40 year amortization may be restricted to a maximum 95 per cent LTV if they are to benefit from the government guarantee. Mortgages with longer term amortizations and above the 95 per cent LTV ratio would not then be eligible for government mortgage insurance backing. Such restrictions would require that purchasers seeking longer amortizations put more of their own money at risk and this would likely dampen speculation tied to high LTVs and long amortizations.

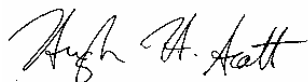
Finally, in our discussion, the issue of adequate and appropriate loan documentation was raised. This appears to have been raised seemingly with a view to developments in the United States where a certain category of mortgages (low document or no documentation) have been abused and are now frequently termed “liar loans”. In the United States, on certain low-documentation loan programs, such as stated income/stated asset (SISA) loans, income and assets are simply stated on the loan application. On other loan programs, such as no income/no asset (NINA) loans, no income and assets are given on the loan application form. These loan programs have fuelled unethical behavior because the SISA or NINA features create opportunities for abuse when borrowers or their mortgage brokers or loan officers overstate income and/or assets in order to qualify the borrower for a larger mortgage.

² International Monetary Fund. (April, 2008) *World Economic Outlook: Housing and the Business Cycle*. p. 107.

However, such developments do not appear to be prevalent in Canada and, in the absence of evidence to the contrary, Canadian Central is concerned that increased documentation and reporting requirements will merely add to the administrative burden faced by financial institutions. Credit unions are of the view that current loan documentation practices are adequate and credit unions are subject to regular audits by mortgage insurance providers, their Deposit Guarantee Corporation and outside Auditors.

To conclude, Canadian Central wishes to thank Finance Canada for the opportunity to comment on the issues outlined above. Canadian Central would be pleased to participate in any further consultations to further clarify these issues. If you have any questions please contact Rob Martin (Senior Policy Advisor) in Canadian Central's Government Relations Department (6143 238-6747 ext 327).

Regards

A handwritten signature in black ink, appearing to read "Hugh A. Scott". The signature is written in a cursive style with a large initial "H".

Hugh Scott
Director, Government Relations