



BEATING

As sophisticated homeowners search for new ways to get the most from their mortgage strategy, *Sandy Aitken* explains how you can separate yourself from the pack and offer them what was once unthinkable – a tax-deductible mortgage

Since the publication of the *Smith Manoeuvre* six years ago, homeowners have become seduced by the notion of tax-deductible mortgages and lured by the possibility of paying off their mortgages in half the time.

As a result, the tax-deductible mortgage strategy, in its variety of forms, has become a rapidly emerging marketing opportunity – and one that is truly exclusive to mortgage brokers, allowing them to separate themselves from the banks.

The simple fact is that any mortgage strategy that involves leveraged investing and tax advice for the middle class is a tough bundle to sell, and no major financial institution in Canada is currently organized for the challenge.

And given the recent credit crunch, combined with the financial institutions' collective inability to adapt quickly to new product offerings, it's quite possible that this will be an area of growth exclusive to the mortgage broker channel, at least for the next few years.

But before you jump on board, it's important to do your research – both in learning the associated risks of this mortgage strategy, as well as how to identify your ideal client.

The basics

A properly structured mortgage-centric tax strategy has several key elements – the most important of which is a multi-component, re-advanceable mortgage or line of credit.

THE TAXMAN

It's best to have a single charge with at least two components – usually a fixed-term mortgage and an open line of credit – that can track and report interest independently. This is absolutely essential under Canada Revenue Agency (CRA) rules and guidelines.

Second, the strategy must employ conservative leverage-investment techniques – which is why a mortgage broker must team up with a financial advisor in order to comply with federal regulations. The financial advisor should be a Certified Financial Planner (CFP) who is experienced in leveraged investing, and able to actively monitor a homeowner's portfolio on an ongoing basis.



Sandy Aitken

FEATURED PRODUCT

National Bank's All-In-One product is well suited to tax-deductible mortgage strategies because it enables clients to create up to 99 sub-accounts under one main account. These sub-accounts make the transferring of funds easy because, as the funds are separated, clients can reserve the money for investment-related transactions and avoid accidentally violating Canadian Revenue Agency regulations.

If you choose not to partner with an experienced CFP, you run the risk of becoming the de facto financial advisor to the homeowner – and managing the back-end work on your own. Not only is this time-consuming, but it's also not an appropriate situation for the mortgage brokerage.

Due to conflict of interest regulations, CFPs are rarely licensed to sell mortgages as well as investments, so the CFP needs the mortgage agent as much as the mortgage professional needs the CFP – and the homeowner needs the advice of both.

Finding the ideal client

Ideal borrowers for an advanced mortgage and tax strategy are typically professionals or other high-income earners who have owned a home for five to 15 years and have built up substantial equity. They are usually between 35 and 55 years old, and in their peak earning years.

As high-income earners, their total debt-servicing ratio will be quite low and they always have excellent credit (700+ Beacon scores). These borrowers are financially sophisticated homeowners that are keenly interested in establishing a secure financial future and comfortable retirement.

They understand that financial security is more than merely paying off their home – it also involves saving enough cash so that they won't be faced with the prospect of a minimal cash flow when they are 80 years old.

For the most part, they already fully expect to pay off their mortgage before retiring, but saving enough money to retire comfortably is another story. These borrowers are acutely aware that if they don't do something different in their financial plan, they will not have enough money for retirement.

The risks

The financial benefits of a tax-deductible mortgage are irrefutable and justify the risks to the right borrower.

A 40-year-old professional couple, for example, should expect to pay off their mortgage in half the time and generate up to three times the mortgage amount in incremental net wealth over 20 years without changing their cash flow. In addition, the first year's tax refund for an average client is in excess of \$4,000 and these benefits assume that all tax refunds, generated by the strategy, are reinvested.