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Seller's existing mortgage can be superb marketing tool

When sellers and their agents list a property for sale, they often overlook an item that's a superb marketing tool and that could add thousands - even tens of thousands - of dollars to the value of the house.

That item is the vendor's existing mortgage.

The following is a true story. It took place last month and although the names have been changed, everything else is true.

Brad and Jennifer wanted a property in the trendy Lawrence Ave. E. area between Mt. Pleasant and Bayview. They had been looking for a long time in this year's heated spring market when a house came up for sale in a very popular area subdivision.

Built in 1929, the house is a detached two-storey, three-bedroom, with a sunroom added on at the back. It had been updated with thousands of dollars in renovations.

Under "existing financing" the listing showed "treat as clear," which means the vendors will pay off the existing mortgage from the sale proceeds. Houses like this were in short supply in March of this year, and there were multiple offers. Originally listed in the mid-$400,000s, it eventually sold to Brad and Jennifer for $13,000 higher than the asking price.

The purchasers had a large down payment as they prepared for the closing. They arranged a first mortgage for $240,000 running for five years with interest at 7.25 per cent. When we met in my office a few days before closing, I pointed out to them that the vendors had a $207,000 mortgage at 5.95 per cent.

The vendors were paying off the mortgage on their house and were about to incur a $3,000 penalty to do so. In checking the terms of the vendors' mortgage, I realized that it was assumable - it did not have to be paid off but could be taken over by a new owner.

I asked the purchasers whether they would be interested in taking on the existing 5.95 per cent mortgage rather than keeping their newly arranged mortgage at 7.25 per cent. Since their new mortgage was $240,000 and the vendor's financing was only $207,000, Brad and Jennifer would have to come up with an extra $33,000 in cash, but they said it would not be a problem. Although the existing mortgage had only four years to run instead of five, and there was a certain risk in interest rates being higher during the fifth year, I calculated that the savings in interest over the first four years would exceed $10,000 in after-tax dollars. At the purchasers' marginal tax rates, this saving amounted to more than $20,000 in gross earnings during that period. (A marginal tax rate is the percentage of tax paid on the last or highest dollar of earned income.)

In addition, I pointed out to Brad and Jennifer that if they took over the existing mortgage, it would save the vendors the $3,000 penalty - which they would probably be willing to split with the purchasers. For Brad and Jennifer, this was a no-brainer.

They would have a 5.95 per cent mortgage instead of a 7.25 per cent one, and they could scoop a further $1,500 from a happy vendor.

With a down payment of more than $265,000, being approved by the old mortgagee to assume the mortgage would not be a problem. Although the interest rate was lower, the monthly payments on the vendors' mortgage were about $165 higher than the payments on the newly arranged mortgage. The larger payment (and shorter amortization period) meant that the mortgage balance would reduce much faster on the 5.95 per cent mortgage. At the end of the four year period and with the extra $33,000 in down payment, there would be about $160,000 owing on their mortgage.

If they had taken the 7.25 per cent mortgage, they would still owe $224,000 at the end of four years - a $64,000 difference.

After our meeting, Jennifer spent the entire next day getting approved to assume the existing mortgage, having the vendors released from their obligation to pay off the mortgage, arranging funds for the higher down payment, and canceling the new 7.25 per cent mortgage.

Within 24 hours, everything was in place, including an agreement with the vendors to split the $3,000 penalty they would save.

The transaction eventually closed as scheduled, with the lower rate mortgage. Jennifer complained to her agent that she spent a whole day running around to make the arrangements.

She wanted to know why the potential for assuming the old mortgage hadn't been discovered earlier. The answer, according to the listing agent, was that the vendors never thought of their old mortgage as a benefit to the transaction.

Even though one of the vendors worked at a bank, they regarded the low interest rate mortgage merely as a liability to be discharged on closing, and not an asset.

For purchasers and their selling agents, the lesson to be learned from the story is this: when the listing says "treat as clear," always ask for the terms of the vendor's mortgage and whether it is assumable.

These questions should be asked as early as possible of the agents involved in the transaction, and of the purchaser's own lawyer, who has access to the title search and the payout statement of the old mortgage.

Similarly, vendors and their listing agents should always consider whether the existing mortgage can offer hidden value to a purchaser.

If your house is for sale, and there's an attractive mortgage in place, why isn't it shown in the listing?
