

Insolvent Debtors - Mortgage Lending Choices

To see if there is a trend in mortgage lending products used by insolvent debtors, and if this trend has any added insolvency risk for borrowers or lenders, we reviewed our Joe Debtor data for the years 2011-2012 and 2013-2014. We looked at the amount of secured debt included in the Statement of Affairs for real property. This is a small data set, and only looks at the types of mortgage loans used by insolvent debtors, not borrowers as a whole. This also reflects claims filed in a bankruptcy or consumer proposal for debt existing at the time of insolvency, not new lending.

We segregated mortgage creditors into 5 major mortgage lending options:

1. Group A: Consisting of Canada's 5 largest traditional banks.
2. Group B: Includes all other banks.
3. Group C: Traditional non-bank financial institutions that offer broad based lending products – trust companies, credit unions, life insurance and financing companies. For example, Home Trust Company, Meridian Credit Union, Citi Financial, HSBC and London Life Insurance Company.
4. Group D: Brokerage based or mortgage market lenders consisting of mortgage financing companies and MIC's. For example, First National Financial, MCAP and FirstLine Mortgages.
5. Group E: Individuals and other secured claims. This may include individual private lenders, vendor take-backs, guarantors, service & other credit related liens, and other secured charges.

Our data does not allow us to identify 'private' lenders. Large MIC's will primarily be included in Group D, however, individuals included in Group E may include small private lenders. For our review, we focused primarily on Groups A through D.

Findings

	Percentage of All Claims	
	2013-2014	2011-2012
Group A: Top 5 Banks	51.6%	55.3%
Group B: Other Banks	8.7%	7.6%
Group C: Non-bank Financial Companies	11.2%	10.0%
Group D: Mortgage Market Lenders	26.0%	25.0%
Group E: Individuals, Liens & Other	2.5%	2.1%

- Canada's 5 major banks have experienced a slight decline in the share of claims filed.
- In contrast, other lending sources have seen small increases in claim shares.

What is more interesting is looking at the average mortgage size by lending group:

	Average Secured Mortgage Claim (% of Average Joe Debtor)		
	2013-2014	2011-2012	Change
Average Joe Debtor (homeowner)	\$197,137	\$208,070	(5%)
Group A: Major Banks	\$169,020 (86%)	\$192,300 (92%)	(12%)
Group B: Other Banks	\$189,720 (96%)	\$186,220 (89%)	2%
Group C: Non-bank Financial Companies	\$134,523 (68%)	\$140,625 (68%)	(4%)
Group D: Mortgage Market Lenders	\$201,825 (102%)	\$203,532 (98%)	(1%)
Group E: Individuals, Liens & Other	\$71,898 (36%)	\$83,205 (40%)	(14%)

- The major banks have experienced the most significant decline in mortgage size when compared to the average Joe Debtor mortgage. This may be indicative of tightening in mortgage lending practices by the top 5 banks along with regulatory changes to mortgage lending rules (although the impact of these later changes will take time to filter through insolvencies).
- Brokerage based mortgage market lenders have the highest average claims of all lending groups
- Smaller banks were the only group to see an increase in the average mortgage claim size.

Effectively, the traditional large banks appear to have deleveraged their exposure to high risk consumers, forcing high risk borrowers to seek alternative mortgage lending providers.

Primary vs Secondary Sources of Cash

	% All Debtors with Mortgage Product	% of those with another mortgage
Group A: Major Banks	13%	6%
Group B: Other Banks	2%	14%
Group C: Non-bank Financial Companies	4%	30%
Group D: Mortgage Market Lenders	6%	9%

In our 2015 study, only 1 in 4 debtors owned a home and carried a mortgage. Unsurprisingly, the majority of those held a mortgage with a major Canadian bank. However, the second most likely mortgage option among indebted homeowners was a mortgage market lender.

Both of these groups have a relatively low instance of creditors holding multiple mortgages. In the case of estates with a mortgage owing to a large Canadian bank, only 6% held another mortgage elsewhere, while only 9% of those with a mortgage market loan had two or more mortgages at the time of their insolvency.

In contrast, we know that 30% of debtors with mortgages held by traditional non-bank financial institutions (trust companies, credit unions etc.) also carried a mortgage from another lender while 14% of small bank mortgage borrowers held multiple mortgages.

It seems that smaller banks, credit unions, and other traditional financing companies are much more likely to be used by debtors as a source for second mortgages and consolidation loans.

Relative Risk

We can also look at the data to see if there is a difference in relative risk levels among insolvent homeowners across mortgage options. To do this we reviewed:

- Unsecured debt characteristics by lending group; and
- Mortgage encumbrance rates.

	Joe Debtor (homeowner)	Group A Major Banks	Group B Other Banks	Group C Non-Bank Financing Co	Group D Mortgage Market
Personal Loans	\$25,841	\$29,074	\$25,123	\$18,773	\$23,086
Credit Card Debt	\$29,378	\$28,653	\$30,186	\$27,593	\$31,451
Other	\$12,826	\$12,070	\$12,332	\$14,805	\$10,218
Total Unsecured Debt	\$68,045	\$69,797	\$67,641	\$61,171	\$64,755
Total Secured Debt ⁽¹⁾	\$197,137	\$191,785	\$213,075	\$201,173	\$217,237
Total Debt	\$265,182	\$261,582	\$280,716	\$262,344	\$281,992
Average % Real Property Encumbered on SOA	90%	90%	89%	90%	91%
Debtor Income	\$2,829	\$2,862	\$3,050	\$2,947	\$2,771
Total Debt to Income Ratio	781%	762%	767%	742%	848%
% With a Payday Loan	9%	9%	12%	18%	8%

(1) Total secured debt for debtors with loans within the category, but including second and third mortgages.

In terms of overall debt risk:

- Insolvent homeowners who hold a mortgage with a traditional bank (large or small) tend to have the highest overall unsecured debt. In particular, they had higher instances of personal loans. This may be due to their relationships with broader financial institutions allowing them access to a broader array of lending products.
- Insolvent homeowners with a brokerage based mortgage market loan tend to have higher secured debt (i.e. larger total mortgages) and experience a marginally higher overall encumbrance rate on their real property. When combined with the relatively lower rate of multiple mortgages, this may indicate that borrowers using alternate mortgage market lenders tend to borrow more than the large banks will approve.
- Insolvent debtors who borrow through brokerage based mortgage market lenders also carry the highest credit card debt of all mortgage groups. Our experience has been that individuals who are mortgage heavy - that is where their mortgage payment utilizes a higher proportion of their disposable income - often turn to credit card debt to meet other living expenses. With a combination of larger, high ratio, mortgages and higher unsecured debt, debtors who utilize mortgage market loans have the highest debt to income ratio of all mortgage groups.

- It is also important to note that insolvent homeowners are as likely as the average Joe Debtor to use payday loans (9%). However, it seems that debtors who utilize Group B & C lenders are the most likely to take out a payday loan. This is consistent with the fact that these lenders are also the lenders of choice for second mortgages & debt consolidation loans. Insolvent debtors often pile debt on top of debt in order to maintain their primary debt payments for as long as they can.

Conclusion

From our review it is apparent that there are some inherent differences in debtor behavior and mortgage lending options:

- In recent years, the top 5 large Canadian banks have seen a slight decline in insolvency claims relative to other mortgage lenders. It would appear they have reduced their exposure to high risk mortgages.
- Traditional non-bank financing companies and smaller bank lenders are more often the lender of choice for second mortgages and consolidation loans.
- Mortgage market lenders have the highest exposure to risk. Mortgage market insolvent debtors, on average, take out larger mortgages, have a higher encumbrance rate (the highest high ratio mortgages), and have the highest total debt to income ratio.

Regardless of lending choice, our data still clearly shows that any high ratio mortgage, when combined with other unsecured debts, significantly increases an individual's risk of filing insolvency.