6 mortgage terms you should know

1. Fixed and variable

With a fixed rate mortgage, your interest rate and payments won't change for the term of your contract. Because the rate is guaranteed, it's usually higher than the variable mortgage rate over the same term.

With a variable rate mortgage, the interest rate changes according to your bank's mortgage prime rate. When the interest rate drops, more of your payment goes towards the principal (your original borrowed amount). When the interest rate increases, more of your payment goes towards interest. If your payments no longer cover the required interest, your payment amount will go up.

2. Term

Your mortgage term is the length of time your mortgage details are guaranteed. Shorter terms generally offer lower rates, but you'll have to renew earlier (when rates might be higher).

3. Open and closed

With a closed mortgage, it's difficult (and expensive) to pay off your mortgage early or switch lenders before your term is up—but you will receive a better rate for your commitment. With an open mortgage, your rate is usually higher but you can make extra payments, pay off your mortgage entirely, or switch lenders at any time.

4. Amortization

Amortization is how long it will take you to pay back your full mortgage (the original borrowed amount plus interest). In Canada, the maximum amortization period is 25 years.

The longer your amortization period, the lower your mortgage payments will be—but the more you'll end up paying in interest.

For example, using a $200,000 mortgage at 5% (per annum):

Amortization (assuming the same interest rate over the entire period)	Monthly payment	Total interest costs (over the life of your mortgage)	Interest saved
15 years	$1,576.65	$83,724.57	$65,238.42
20 years	$1,314.25	$115,420.02	$33,542.97
25 years	$1,163.21	$148,962.99	N/A

5. Payment schedule

You can make your mortgage payments monthly, semi-monthly (twice a month), bi-weekly (every two weeks), or weekly. Semi-monthly and bi-weekly may seem like the same thing, but in reality, bi-weekly payments can save you thousands in interest and help you pay off your mortgage years earlier. This is because, with semi-monthly payments, you'll make 24 payments a year (two per month); with bi-weekly, you make 26 payments a year (half of the year's 52 weeks). That's two extra payments every year—which can add up to thousands in savings.

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Using a $200,000 mortgage at 5% (per annum):

Payment frequency	Payment	Actual amortization (years)	Total interest costs (over the life of the mortgage)	Interest saved
Monthly	$1,163.21	25	$148,962.99	N/A
Accelerated bi-weekly	$581.60	22	$124,094.94	$24,868.05

6. Portability, blending and extending, skip payments, and pre-payments

These are a few options that may be available to you, depending on your mortgage.

Portability: If you decide to move before the end of your term, you may have the option to transfer your existing rate, loan balance, and maturity date to your new home without paying any penalties.

Blending and extending: Another option if you're planning on buying a new home or renewing your mortgage early, blending and extending allows you to blend your current rate with a new rate, while adding your new mortgage term on the end of your current term.

Skip payments: Some lenders allow you to skip one or two months of mortgage payments every year, a good option if your income fluctuates.

Pre-payments: You may have the option of increasing your payments by a certain per cent each year or prepaying up to a certain per cent of your loan each year, making a big dent in your principal.

Again, using a $200,000 mortgage at 5% (per annum):

Pre-payment choices	Standard 25-year amortization	Increase mortgage payments once by 20% and increased payment maintained	Make payment of 20% ($40,000 at end of 1st year only)
Mortgage repaid in months	300	228	216
Total interest cost (over the life of the mortgage)	$148,962.99	$107,070.11	$81,239.37
Interest saved vs. standard 25-year amortization	N/A	$41,892.88	$65,236.20

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