

## Mortgage Penalty -Interest Rate Differential (IRD)

The IRD is a compensation charge that may apply if you pay off your mortgage prior to the maturity date, or pay the mortgage principal down beyond the amount of your prepayment privileges.

The IRD is based on:

- The amount you are pre-paying; and,
- An interest rate that equals the difference between your original mortgage interest rate and the interest rate that the lender can charge today when re-lending the funds for the remaining term of the mortgage.

Most closed fixed-rate mortgages have a prepayment penalty that is the higher of 3-months interest or the IRD. Variable-rate mortgages do not have IRD penalties. They always are based on 3 months interest rate. (much less penalty)

Here is a calculator that let's you estimate your mortgage penalty:

Current Mortgage Balance = B

Original Interest Rate = O

Current Interest Rate (for remaining term) = C

Remaining Term (in months) = R

IRD Penalty =  $B \times (O - C) / 100 \times R / 12$

3 Month Interest Penalty =  $B \times O\% / 4$

\* For fixed-rate mortgages the penalty is typically the greater of 3-months interest or the IRD. These are rough estimates and will not precisely match your actual penalty.

- The above penalties are approximate. This calculator is a rough guide only.
  - Each lender has its own formula for calculating penalties.
  - Some lenders use posted rates for their IRD calculation and some use discounted rates.
  - Some lenders round up to the next longest term when determining comparable IRD interest rates. Some round down.
  - The Interest Act prohibits IRD penalties on terms over 5 years, after five years has elapsed. In such cases, a maximum 3-month interest penalty may apply. For example, someone who has been in a 6-year mortgage for 60 months or more would pay a 3-month interest penalty (maximum) to break it before maturity.
  - A small number of lenders prohibit breaking a mortgage early—regardless of the penalty—unless in the case of an approved bona fide sale.
  - The moral: Always contact your lender directly for an exact penalty quote.
- Meanwhile I can make a request to your lender to ask for exact amount of your penalty.