

# Investment and Vacation Property 101



So, you are looking to purchase a second property! Congratulations! This is a great opportunity for you to expand your financial portfolio and ensure stability for the future. However, before you launch into this purchase there are a few things you should know, depending on which type of second property you are looking to purchase.

## **Second Property with Intention to Rent**

Buying a property for the purpose of renting it out to someone else comes with different qualifying criteria and mortgage product options than traditional home purchases.

Before you look at purchasing a rental property, there are a few things to consider:

1. The minimum down payment required is 20% of the purchase price, and the funds must come from your own savings; you cannot use a gift from someone else.
2. Only a portion of the rental income can be used for the qualifying and determining how much of a mortgage you can afford to borrow. Some lenders will only allow you to use 50% of the income added to yours, while other lenders may allow up to 80% of the rental income while subtracting your expenses. This can have a much higher impact on how much you can afford.
3. Interest rates usually have a premium on them when the mortgage is for a rental property versus a mortgage for a home someone intends on living in. The premium can be anywhere from 0.10% to 0.20% on a regular 5-year fixed rate.

## **Vacation Property**

While vacation properties are not always the best investment, they are popular options for people who want to get away from it all! If you're inclined to head down that road, buying a vacation property is essentially like purchasing a second home. The minimum down payment is the same at 5% and you have to go through the same processes as your first mortgage. You would also need to have the same insurance premiums as with a regular home.

If you are considering buying a unit within a hotel as a vacation spot (known as "fractional ownership"), it can be difficult to get financing.

It is important to note that if there is any mention of using your vacation home to provide rental income, you would need to put 20-25% down and it will be treated like an investment property.

### **Secondary Property**

Most people are trained to stay out of debt and don't tend to consider using the equity in their home to buy an investment property, but they haven't realized the art of leveraging. If you're using equity from your primary residence to buy an investment property, keep in mind that the interest you're using is tax deductible. Consider that you're buying an appreciating asset, and if you put a real estate portfolio and a stock portfolio side-by-side, they don't compare.

#### *Who is a good candidate?*

You might be surprised to learn that you don't need to make six figures to get in the game. Essentially, you just have to be someone who wants to be a little smarter with their down payment. Before taking on a secondary property, it is important to remember that the minimum down payment is the same as with a property for rental and will be 20 or 25% of the purchase price. Rental income from the property can be used to debt service the mortgage application, but do bear in mind that some lenders will have a minimum liquid net worth requirement outside of the property. Also, if you do eventually want to sell this property, do note that it will be subject to capital gains tax. Your accountant will be able to help you with that aspect if you do decide to sell in the future.

When it comes to purchasing a secondary property, whether for investment or rental or vacation, it can be a great opportunity! However, do note that most lenders will limit the number of mortgages in a portfolio. If this is only property number two or three, you won't have any concerns, but as you expand your portfolio you may run into limits at five properties (at which point you would be considered a commercial file).

A mortgage broker can work with you and may even be able to find options to increase the number of investment properties should it become necessary.