Senator Buckwold: But you would still maintain, I presume, the guarantees that you have on those mortgages that are given and handled by private corporations?

Mr. Wilson: Absolutely, and I would expect that the FMEC would deal pretty extensively, but not exclusively, with the NHA insured loans.

Senator Buckwold: Because you really have the guarantee of the government behind them, so there is no risk in buying the mortgage, as against an individual mortgage that may be carried out between buyer and seller.

Mr. Wilson: Well, there certainly is a standardization of the quality of risk, if you like, with an insured loan, that you do not get with an ordinary, conventional loan.

The Acting Chairman: And to the extent that the FMEC purchases mortgages or mortgage instruments from CMHC then, to that extent also, the CMHC will have additional funds available for the general purposes of the corporation.

Mr. Wilson: That is not quite correct, because our corporate setup with Finance requires that where a mortgage is prepaid or where we sell a mortgage, then we must in turn repay the debenture debt we owe to the government, so that it would go back into government funds and would be subject to control by government, and, of course, by Parliament before we could take that money and lend it again. We do not have a revolving fund.

Senator Phillips: You mentioned that you would be transfering certain mortgage portfolios to the FMEC. What type of mortgages would you be transferring, the subsidized ones or NHA?

Mr. Wilson: They would be direct loans made by the corporation. I would think it would be highly unlikely that we would sell mortgages at sub-market interest rates at the time they were made. Although theoretically, it would be possible for us to sell mortgages that we are writing today at 7 per cent, because of the fact that these are subsidized rates and we have special arrangements with the borrower to withdraw subsidization as his income changes, it would be virtually impossible for us to move that business into the private sector. I would think we would have to deal with that particular part of our portfolio which was made on private sector terms and carries no unusual mortgage or tied contractual relationships.

Senator Phillips: And the interest rates on those mortgages at the present time would be 9 to 10 per cent?

Mr. Wilson: We have no mortgages at 10 per cent. Our current rate for a loan on the private sector type of transaction is $9\frac{1}{2}$ per cent. We have very few of that type made. Our rate has varied over the past three or four years and has gone as high, I think, as $9\frac{1}{4}$ per cent and as low as $8\frac{3}{4}$ per cent. That is the type of portfolio we would have. Of course we would have some older portfolios at lower rates.

Senator Phillips: But nobody would buy them.

Mr. Wilson: Oh, at a discount, yes, but they would obviously have to be priced for today's market.

Senator Buckwold: Who would take that loss? Let us say that there is a mortgage that you have on your portfolio at 8 per cent and in order to move it through the exchange you would have to pay 9 1/2 per cent, who will pay the extra contractual interest rate?

Mr. Wilson: The details would have to be worked out between ourselves and the Department of Finance and FMEC. Obviously, the FMEC would have to get that mortgage money on their balance sheet at a market rate, so whether the loss is absorbed by the corporation or the Department of Finance will be a matter of dispute between the two of us.

Senator Phillips: That is the situation I anticipated from the start, so I want to ask you this. If you have a mortgage at the 9 1/2 per cent rate while the present NHA rate is higher than that, and you try to sell it, what discount are you offering?

Mr. Wilson: In selling mortgages to a private market and not just to a market lender, the market looks basically for a net yield, and that means the coupon rate of the mortgage less a service or administering charge for the administration of that mortgage. The coupon yield is normally anywhere from 1/10 of 1 per cent to 3/8 of 1 per cent higher than the net yield. So if you were selling today on a net-yield basis, you would have to discount to produce a net yield on the current market, from what I am told, of somewhere in the neighborhood of 9 1/2 per cent or slightly less.

Senator Buckwold: Well, then, somebody is picking up a loss here. Why would Central Mortgage dispose of its portfolio of lower interest rates? Granted that is all you are getting, and you may say, "Well, we will lose in any case because we should be getting more money for it," but would you be inclined to take that loss?

Mr. Wilson: Looking at it from the point of view of the straight capital position of the corporation, it would not be particularly in our interest to do so. However, the purpose of doing so, if, in fact, this were done and we rather suspect it would be desirable to do so—would be basically to put FMEC in a trading position at the outset, and it might well be worthwhile for government, whether it be in the corporation's balance sheet or in the broader sense, to absorb a capital loss on the basis of the book value of that asset now for the purpose of doing this. As you know, we have in the past sold mortgages in an attempt to develop a secondary market, and some of these were sold at a discount and some at a premium. So I think it might be desirable, not merely to keep us a prudent investor, but rather for the purpose of developing a secondary market which, in the long run, is still in the interest of housing generally, to take some capital loss in respect of some of those mortgages.

Senator Phillips: Mr. Chairman, the situation that disturbs me is this. The CMHC disposes of a mortgage to FMEC, and there was mention of 9 1/2 per cent as a possibility. In turn, FMEC, when they go to sell, I presume, are going to run into certain fees, commissions and so on, so there is a possibility of a further discount. Who will absorb this loss?