Report to the Provost

of the

Ad Hoc Committee on the Design of the Faculty Housing Program

February 25, 2005

Committee Members:

Robert Armstrong, Lotte Bailyn, Tanya Baker, Claude Canizares (chair), Lorna Gibson, William Heitin, Jamie Lewis Keith, Philip Khoury, Doreen Morris, Gareth McKinley, Israel Ruiz, Carl Wunsch

Charge to the Committee

This committee was charged by Provost Robert A. Brown to define the detailed implementation of a new faculty housing assistance plan. The plan should incorporate the recommendations of the May 2003 report of the Ad Hoc Committee on Senior (Tenured) Faculty Housing Benefits. The charge enumerated a sample of policies that need to be put in place as part of the implementation:

1. *Defining the group of faculty and the type of housing purchase for which the program is applicable. If the program is meant to assist faculty in buying primary residences and to moderate the high cost of Boston area housing, issues of when the faculty bought the house (alternatively, when the faculty member received tenure) and where the primary residence is located should be considered. Questions about the definition of the primary residence and whether the mortgage program can be used for other types of property will come up.*
2. *Defining the program for junior (untenured members) of our faculty and the transition between the programs for tenured and untenured faculty once tenure is granted.*
3. *Define the terms and conditions for closing out mortgage if the faculty member leaves MIT before the full term of the loan.*

Motivation

The recent steep increase in the already high cost of housing in the greater Boston area is a major factor in the recruitment and retention of both senior and junior faculty at MIT. Furthermore, a recent faculty survey found a high level of concern about housing prices and their effect on faculty quality-of-life. Research also shows a general dissatisfaction with the existing faculty housing assistance program. Peer institutions in similar housing markets (e.g. Harvard and Stanford) have more generous housing assistance programs, putting MIT at a competitive disadvantage. There is a consensus among Department Heads, Deans and central administration that housing assistance is a high enough priority to warrant a significant investment of Institute resources.

Challenge

The challenge to this committee was to take the results of the previous Ad Hoc Committee on Senior (tenured) Faculty Housing Benefits and define detailed programs for both senior and junior faculty that are effective, attractive, competitive, fair & equitable, defensible, affordable and manageable. The Committee is well aware of the near impossibility of achieving all these objectives, some of which pull in opposite directions. Instead, it accepted the challenge of trying to find the best way to achieve balance among them.

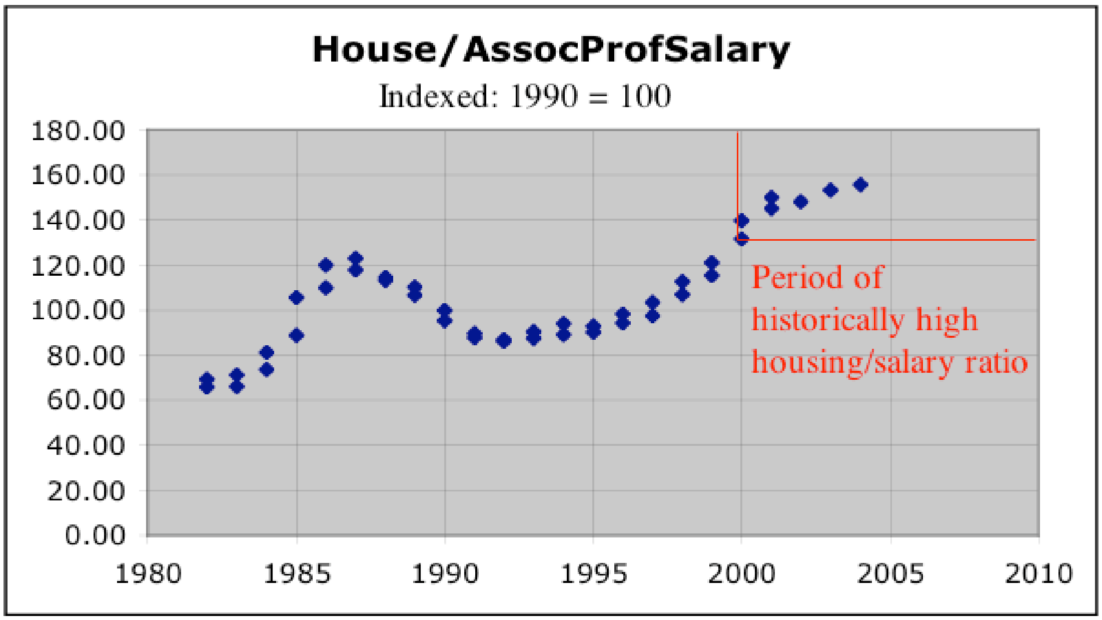
Eligibility

The key and potentially most contentious question is the definition of who will be eligible for this benefit, and conversely, who is not eligible. The Committee spent considerable time and effort on this issue, recognizing first, that a housing benefit represents effective additional compensation, and second, that any dividing line may be perceived as arbitrary and open to challenge.

Our recommendation is to make the new housing benefit available to those faculty who entered the local housing market in or after July 2000, which is approximately the time when the ratio of median housing price to average MIT salary for Associate Professors first reached historically unprecedented high values (where they persist today; see Figure 1). The Committee recognized that there is considerable dispersion in this ratio caused by variations in housing prices, faculty housing needs or preferences, and market-driven variations in salaries within and across schools. The Committee felt that it was not appropriate to try to take those myriad factors into account, but rather chose to use the simple criterion based on the average ratio to define the population that has been uniquely disadvantaged by the rapid housing price increases. It also chose to set the eligibility criteria and the size of the benefit in a uniform manner for each rank (untenured or tenured) across the Institute. The criteria take into account both a steady-state eligibility window for newly hired or promoted faculty and a special eligibility window that opens further to capture the population of faculty who were uniquely disadvantaged.

Elements of the Proposed Program

Beyond the question of eligibility the committee dealt with numerous details that need to be specified for both the untenured and tenured faculty programs. We benefited greatly from the work of the prior *ad hoc* committee, the experience MIT has gained over the years with the present housing assistance program, and comparison with what is known about programs at peer institutions. The details of the proposed program are spelled out in the attached document and summarized briefly here.



Data courtesy Prof. H. Pollakowski & L. Snover

Figure 1. Ratio of the median sales price of a home in a local community to the average salary of an Associate Professor at MIT indexed to 100 in 1990. Note that both this and the previous Ad Hoc committee reviewed data for both single-family homes and condominiums in many local communities and found very similar trends. (Note that, for some years, data for half-year intervals are plotted together.)

For senior faculty, the primary instrument is a 30 year, $300,000 Contingent Interest Mortgage (CIM), which provides a tax-efficient, low interest second mortgage. Some of the interest is “contingent” on the rate of appreciation of the value of the property over the term of the loan. This CIM will significantly increase the buying power of faculty newly hired or promoted into tenured positions.

For junior faculty, we propose two instruments, a 5 year, $50,000 No-Interest Fully Amortizing Loan (NIFAL, which is forgiven incrementally over the five year period) plus a 10 year, $50,000 CIM. Together, these provide both buying power and funds for down-payments to meet the needs of junior faculty, most of whom will be first-time home buyers.

Recommendations

Recommendation 1: The Committee recommends that MIT establish a new Faculty Housing Assistance Program (FHAP) for senior (tenured) faculty and junior (untenured) faculty. All the details are contained in the attached document entitled A Proposed Faculty Housing Assistance Program. We recommend that the program should begin on July 1, 2005.

Recommendation 2: Once the overall fiscal feasibility of the program is established, the Committee recommends that the Provost bring this proposal to the attention of the faculty and solicit their comments and suggestions regarding its particulars. The Provost may then choose to adjust the details of the program if appropriate. The Committee is prepared to assist in explaining the program to the faculty and, if necessary, to reconvene in order to assess the comments and recommend any adjustments.

Recommendation 3: The Committee recommends that the Provost conduct a periodic assessment of the state of the housing market and the effectiveness of the FHAP in meeting the original goals of the program. If conditions change significantly, he should consider altering or terminating the program as described in the proposal. It may be appropriate to establish another Ad Hoc faculty committee for this purpose.

The Committee considered two related issues that, it concluded, lie outside its purview. These are (i) whether or not any parts of the proposed FHAP should be made available to selected senior administrative and/or research staff, and (ii) whether or not MIT should find ways to provide some affordable, rental properties near campus for new junior faculty.

Respectfully submitted on behalf of the committee,

Claude R. Canizares (Chair)

Proposed Faculty Housing Assistance Program

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Summary:

The MIT Faculty Housing Assistance Program (FHAP) has been established to support junior faculty and recently tenured faculty purchasing a primary residence in the local housing market. The program is a significant enhancement over the current Housing Assistance Loan Program (HALP). It is being established in recognition of the sharp increase in Boston-area housing prices that occurred over the past five years. In the year 2000, the ratio of median regional housing prices to average faculty salaries began exceeding its historic values.

The initial program is designed to assist those faculty members hired or tenured during this period of historically high housing costs and who, therefore, are -- or were -- constrained in their ability to purchase a home. Following a one-year start up, the program will be available to faculty hired or tenured in the prior three fiscal years. The details of the programs for untenured and tenured faculty differ, as described below.

Since the primary motivation for the FHAP is to help compensate for the recent, rapid increase in housing prices, in future years the program may be altered on a going forward basis in any and all respects or may be terminated entirely depending on changes in the local housing market. The terms of any then outstanding loans, however, would continue to be governed by their existing loan documents.

Program for Senior (Tenured) Faculty:

Contingent Interest Mortgage Program for Senior Faculty (CIMP-SF)

The CIMP-SF is a tax-efficient, minimum interest, second mortgage program to assist recently tenured faculty in purchasing a home in the expensive local area housing market. The interest rate is capped at the long-term Applicable Federal Rate in effect when the loan is made, which is the lowest tax efficient rate allowed by the IRS. One-half of the interest is due over the course of the loan, paid in monthly installments. The other half is accumulated and added to the principal, and is due upon maturity or early termination of the loan. This deferred interest is contingent on the appreciation of the property, as described below. Paying some of the interest during the loan term will reduce the size of the balloon payment owed at maturity of the loan (making its payment or refinancing easier).

<u>Term of loan</u>: 30 yrs

<u>Maximum Loan Amount</u>: lesser of $300,000 or 40% of the applicable value of the property. The applicable value is the fair market value of that portion of the property that constitutes the principal residence of the faculty member, as such value is appraised by the first mortgage lender or is determined by the real estate tax assessor, whichever is greater.

<u>Interest Rate:</u>

> <u>Annual interest charge</u>: one half of the long-term Applicable Federal Rate (AFR) at the time the loan is made.
>
> <u>Contingent Interest</u>: the <u>lesser of</u> one-half the long-term Applicable Federal Rate (AFR) at the time the loan is made or the difference between the average percentage appreciation of the property since the inception of the loan, and one-half the AFR, if this difference is greater than zero. Appreciation is calculated to exclude appreciation attributable to capital improvements made after the loan is made, and, therefore, not funded by the loan from MIT.

<u>Eligibility</u>: This program is available <u>one time only</u> (for purchase, or, if eligible, for refinancing or major renovation) to all faculty hired into a tenured position or promoted to a tenured position at any time during the current MIT fiscal year (FY) or during the preceding three MIT fiscal years (e.g. in MIT FY 2006, which begins July 1, 2005, all faculty hired into or promoted to tenure on or after July 1, 2002 are eligible; in MIT FY 2007, all faculty hired into or promoted to tenure on or after July 1, 2003 are eligible). Faculty promoted to tenure at any time on or after July 1, 2006 who have outstanding loans under the CIMP-JF program must terminate those loans before or as they join the CIMP-SF program.

<u>Special Eligibility</u>: <u>Only</u> during MIT FY 2006 (the period July 1, 2005 through June 30, 2006), those faculty hired into or promoted to a tenured position during the period July 1, 2000 through June 30, 2002 and who have not already received other housing assistance from MIT will also be eligible if they were first-time buyers of a qualifying residence on or after July 1, 2000 or if they are first-time buyers of a qualifying residence during MIT FY 2006. Tenured faculty who meet the above criteria but who have already received other housing assistance from MIT are generally not eligible; when the additional other assistance consists of a CIM issued under the current Housing Assistance Loan Program,

they are eligible to convert their existing CIM into the CIMP-SF for a term equal to 30 years minus the expired portion of the term of the original loan.

Qualifying residence: The CIMP-SF is only applicable to a faculty member's purchase of a "principal residence" within a 50-mile radius of MIT. "Principal residence" is defined by the IRS, under Section 121 of the Internal Revenue Code, using a facts and circumstances standard and considering, among other facts, where the faculty member resides most of the time, the address listed on the faculty member's tax returns, voter registration, driver's license, and automobile registration, the faculty member's billing address and the faculty member's principal dwelling throughout the academic year. Vacation homes, investment properties, and income properties are not qualifying residences. Single-family residences, condominiums, and cooperatives qualify. Faculty may request approval to purchase a multi-family property so long as the faculty member's residence constitutes 50% or more of the appraised value; only the applicable value of the portion of such a property that is occupied by the faculty member as his or her principal residence may be taken into account in determining the Maximum Loan Amount for a CIMP-SF loan.

Refinancing an existing loan: This program may not be used to refinance an existing mortgage except as follows: (i) faculty hired into a tenured position or promoted to a tenured position at any time during the current MIT fiscal year (FY) or during the preceding three MIT fiscal years and who were first-time buyers of a qualifying residence on or after July 1, 2000 may refinance an existing, qualifying residence; (ii) only during MIT FY 2006 (the period July 1, 2005 through June 30, 2006), those faculty hired into or promoted to a tenured position during the period July 1, 2000 through June 30, 2002 and who were first-time buyers of a qualifying residence on or after July 1, 2000 may refinance the qualifying residence. In all cases, any loan origination expenses must be borne by the borrower. Using the program to refinance is also permissible in connection with major renovations (see below).

Financing Major Renovations: The program is available on a one-time basis to qualifying faculty who undertake a major renovation of an existing, qualifying residence in lieu of using the program to buy a new qualifying residence. A major renovation is defined as "a major capital addition or renovation to the faculty member's principal residence in connection with which a certified public accountant has signed and delivered a letter to MIT confirming that the design and construction contracts, and related legal and consulting costs, for the capital improvements (as defined under generally accepted accounting principles) to the faculty member's current principal residence equal or exceed $150,000." The faculty member must either refinance the first mortgage loan on the residence in conjunction with entering into a CIM for a major renovation, or will be assessed a fee to cover MIT's cost to have an outside contractor undertake additional reviews (e.g., relating to the construction) required for this type of loan. For refinancing, the maximum loan amount is the lesser of $300,000 or 40% of the applicable assessed value including the added value of the renovation.

Refinancing this loan: The outstanding balance of a loan can be refinanced at the prevailing AFR for a term equal to the remaining term of the original mortgage one time during each 10 year interval of the mortgage. Loan transaction expenses must be borne by the borrower.

Termination: Principal and outstanding interest are due on the earliest of (i) the date of sale of the property, (ii) the date when the property is no longer the faculty member's principal residence, or (iii) the date of termination of employment as a faculty member at MIT. Faculty who retire and who maintain the property as their principal residence have the option to retain the loan as a demand loan with all other terms and conditions unchanged.

Mortgage Life Insurance: Faculty are required to obtain mortgage life insurance for the principal and accrued contingent interest.

Programs for Junior (Untenured) Faculty:

Eligible junior faculty may select either or both of the following programs.

Contingent Interest Mortgage Program for Junior Faculty (CIMP-JF)

The CIMP-JF is a tax-efficient, minimum interest, second mortgage program to assist recently hired untenured faculty to purchase a home in the expensive local area housing market. The interest rate is capped at the long-term Applicable Federal Rate (AFR) at the time the loan is made, which is the lowest tax efficient rate allowed by the IRS. Unless the faculty member elects to defer all of the interest, one-half of the interest is due over the course of the loan, in monthly payments. The other half is accumulated and added to the principal, and is due upon maturity or early termination of the loan. This deferred interest is contingent on the appreciation of the property, as described below.

Term of loan: 10 yrs

Amount of loan: $50,000.

Interest Rate:

> Annual interest charge: one half of the long-term Applicable Federal Rate (AFR) at the time the loan is made (unless the junior faculty member elects to defer all interest until loan maturity or termination). If the junior faculty elects deferral, interest will be accumulated as owed each year, but payment will be owed at loan maturity or termination. Interest that accrues on interest will not be tax deductible and this option is not as tax efficient as paying interest annually.
>
> Contingent Interest: the lesser of one-half the long-term Applicable Federal Rate (AFR) at the time the loan is made or the difference between the average

percentage appreciation of the property since the inception of the loan, and one-half the AFR, if this difference is greater than zero. Appreciation is calculated to exclude appreciation attributable to capital improvements made after the loan is made, and, therefore, not funded by the loan from MIT.

Eligibility: This program is available one-time only to all junior (untenured) faculty hired in the current MIT fiscal year or the previous three MIT fiscal years (e.g. in MIT FY 2006, which begins July 1, 2005, all junior faculty hired on or after July 1, 2002 are eligible; in MIT FY 2007, all junior faculty hired on or after July 1, 2003 are eligible).

Special Eligibility: Only during MIT FY 2006 (the period July 1, 2005 through June 30, 2006), those junior faculty hired during the period July 1, 2000 through June 30, 2002 will also be eligible if they were first-time buyers of a qualifying residence on or after July 1, 2000 or if they are first-time buyers of a qualifying residence during MIT FY 2006.

Qualifying residence: same as CIMP-SF

Refinancing an existing loan: This program may not be used to refinance an existing mortgage except as follows: only during MIT FY 2006 (the period July 1, 2005 through June 30, 2006), those faculty hired into a junior faculty position during the period July 1, 2000 through June 30, 2005 and who were first-time buyers of a qualifying residence on or after July 1, 2000 may refinance the qualifying residence. In all cases, any loan transaction expenses must be borne by the borrower.

Refinancing this loan: This mortgage may not be refinanced.

Termination:
a) Principal and outstanding interest are due on the earliest to occur of (i) sale of the property, (ii) date of termination of employment as a faculty member at MIT, or (iii) the date when the property is no longer the faculty member's principal residence.
b) Upon award of tenure, the CIMP-JF may be continued so long as the faculty member remains eligible and the property remains qualifying. Faculty promoted to tenure who have outstanding loans under the CIMP-JF program must terminate those loans before or at the time they join the CIMP-SF program.

Mortgage Life Insurance: Faculty are required to obtain mortgage life insurance for the principal and accrued contingent interest.

No-Interest, Fully Amortizing Loan (NIFAL) Program for Junior Faculty

The NIFAL is a program to assist recently hired junior (untenured) faculty to purchase a primary residence in the local housing market. The terms of the loan are similar to those in the current Faculty Relocation Loan Program, except that it is now available to all qualifying junior faculty. The loan will be secured by a mortgage on the property.

Eligibility: All full-time, junior (untenured) faculty hired in the previous three MIT fiscal years (e.g. in MIT FY 2006, which begins July 1, 2005, all junior faculty hired on or after July 1, 2002 are eligible; in MIT FY 2007, all junior faculty hired on or after July 1, 2003 are eligible). Only during MIT FY 2006 (the period July 1, 2005 through June 30, 2006), those junior faculty hired during the period July 1, 2000 through June 30, 2002 will also be eligible if they purchased a qualifying residence on or after July 1, 2000 or if they purchase a qualifying residence during MIT FY 2006. Note that the tax implications of this loan for the faculty member are different depending on whether or not he or she meets the IRS definition of a relocating new employee of the Institute.

Qualifying residence: same as CIMP-SF

Term: The loan will be for a period of 5 years, with one-fifth of the principal becoming due on each anniversary of the date on which the loan was made. See "Forgiveness" below.

Amount of Loan: $50,000.

Interest rate: This loan will be interest free.

Termination: The entire amount of the loan outstanding becomes due on the earlier of (i) the date of sale of the property, (ii) the date when the property is no longer the faculty member's principal residence, or (iii) the date of termination of employment as a faculty member at MIT.

Forgiveness: On each 12-month anniversary of the original date of an outstanding loan, the Institute will forgive one-fifth of the original principal of the loan.