

City of Cambridge
Community Development Department

**Affordable Homeownership
Program Review – Proposed
Recommendations**



What is the program review?

- Looking at program terms to make improvements
- Terms have not changed in ~30 years
- Focus on “**resale formula**” and **inheritance policy**
- The **resale formula** is how affordable homes increase in value over time
- **Inheritance** is the option to pass ownership to a beneficiary who will live in the unit

What are the goals of the review?



Increase the
return on
affordable
homes



Make the
resale formula
easier to
understand



Preserve
affordability
for the long
term



Keep the
program
financially
sustainable



Explore
options for
inheritance

Process to Date

Affordable Housing Trust Process

Process introduced at Trust meeting March 2022

Homeowner Survey findings shared September 2022

Listening Session and Applicant Survey findings shared December 2022

Trust Working Group developed proposed recommendations for discussion

Trust voted to move forward with proposed recommendations April 2023

Program Review Process Engagement

Survey for all current owners completed July 2022

Listening sessions for current owners through October 2022

Survey for applicants waiting for housing completed December 2022

Housing Committee hearing January 2023

What is happening now?

- Information shared with all current owners
- Hard copy and/or translated presentation by request – email homeownership@cambridgema.gov
- Opportunities to share feedback on proposal:
 - Survey link will be sent – respond through 12/21/23
 - Written comments submitted to homeownership@cambridgema.gov through 1/4/2024
 - Information & Feedback sessions through 12/14/23

Information & Feedback Sessions

- Invitation to register for one of four sessions in December
- Registration information in letter to owners and here:
<http://www.cambridgema.gov/HomeownershipProgramReview>
- Session size is limited
- Held remotely on Zoom
- Session agenda:
 - Presentation
 - Q & A on proposed recommendations
 - Owner comment period

Resale Formula

Where are we starting from?

- Current resale formula for most is “Return on Equity”
- Each year, value increases by $\text{Equity} \times \text{Treasury Bill rate}$
- Equity is downpayment and principal paid on mortgage
- Treasury Bill rate is published by Federal Reserve
- Return is only on equity, not on entire value

“Return on Equity” Formula Details

- Affordable Value = Purchase Price + Return on Equity
- Equity = down payment + all principal payments made on mortgage loans
- Not included in equity:
 - Closing costs
 - Interest or fees paid on mortgages
 - Condo fees and property taxes
 - Capital improvement value
- **Return on Equity** = Equity * Treasury Bill Rate
- Treasury rates used are 10, 20 or 30 year, depending on restriction, published monthly by the Federal Reserve
- Return on Equity is calculated for anniversary month of purchase, prorated for partial years

Current Formula – Simplified Example

Years Owned	Starting Equity	Equity Paid	Total Equity	Treasury Rate	Return on Equity
1	\$3,000	\$2,000	\$5,000	2.30%	\$115.00
2	\$5,000	\$2,100	\$7,100	2.60%	\$184.60
3	\$7,100	\$2,200	\$9,300	2.36%	\$219.48
4	\$9,300	\$2,300	\$11,600	1.64%	\$190.24
5	\$11,600	\$2,400	\$14,000	2.91%	\$407.40
6	\$14,000	\$2,500	\$16,500	2.07%	\$341.55
7	\$16,500	\$2,600	\$19,100	0.73%	\$139.43
8	\$19,100	\$2,700	\$21,800	1.52%	\$331.36
9	\$21,800	\$2,800	\$24,600	3.14%	\$772.44
10	\$24,600	\$2,900	\$27,500	3.75%	\$1031.25
TOTAL		\$24,500	\$27,500		\$3,732.75
Original Price:	\$100,000.00				
Return on Equity:	\$ 3,732.75				
RESALE PRICE:	\$103,732.75				

Return on Equity Formula

- Average annual return $\sim .25\%$
- Formula is complex and unpredictable
- Rewards higher down payment and ability to pay more on mortgage = more assets and income
- Penalizes taking out equity; using home equity will slow the price increase
- Annual increase is typically higher in later years

Priorities from stakeholders

- Owners want more return to build assets, use home equity, move on to other housing options, and maintain home
- Both owners and applicants waiting for housing feel strongly that these homes should remain affordable and available to those who need them
- City/Trust also needs to balance increasing costs of affordable homeownership program with limited public resources and needs for all types of affordable housing



Recommendation:
2.5% Annual
Increase

- Value increased by 2.5% of the original “affordable purchase price” each year
- “Affordable purchase price” = purchase price less any subsidy for price reduction (such as HomeBridge)
- Increase is simple interest, not compounding
- Same \$\$ for each year of ownership
- Retroactive to time of purchase

Example – Purchase Price of \$100,000

Years of Ownership	Annual Increase	Value at Year End	Total % Increase
1	\$2,500	\$102,500	2.5%
2	\$2,500	\$105,000	5%
3	\$2,500	\$107,500	7.5%
4	\$2,500	\$110,000	10%
5	\$2,500	\$112,500	12.5%
6	\$2,500	\$115,000	15%
7	\$2,500	\$117,500	17.5%
8	\$2,500	\$120,000	20%
9	\$2,500	\$122,500	22.5%
10	\$2,500	\$125,000	25%

Example #2 – Purchase Price of \$200,000

Years of Ownership	Annual Increase	Value at Year End	Total % Increase
1	\$5,000	\$205,000	2.5%
2	\$5,000	\$210,000	5%
3	\$5,000	\$215,000	7.5%
4	\$5,000	\$220,000	10%
5	\$5,000	\$225,000	12.5%
6	\$5,000	\$230,000	15%
7	\$5,000	\$235,000	17.5%
8	\$5,000	\$240,000	20%
9	\$5,000	\$245,000	22.5%
10	\$5,000	\$250,000	25%

Benefits of Proposed Resale Formula:

10X increase in annual return
compared to current average

No risk of value decrease

Predictable increase allows for long-
term planning for owners and program

Taking out equity does not impact price

Resale Formula
Comparison – Case
Study #1

Original Purchase Price = \$145,500
Sale in Year 10

Resale Formula Type	Value at Resale	Total \$ Increase	Total % Increase	Annual % Increase
Return on Equity	\$148,688	\$3,688	2.2%	.22%
2.5% Annual	\$181,875	\$36,375	25%	2.5%

Resale Formula
Comparison – Case
Study #2

Original Purchase Price = \$224,986
Sale in Year 12

Resale Formula Type	Value at Resale	Total \$ Increase	Total % Increase	Annual % Increase
Return on Equity	\$230,457	\$5,471	2.4%	.20%
2.5% Annual	\$292,482	\$67,496	30%	2.5%

Who may not see a higher price?

- Small number of oldest restrictions have a different formula that may be higher
- Some owners who have paid most or all of their mortgage balance(s) and have a high Treasury Bill rate
- **No one will be required to change to a different resale formula**

Capital Improvements

- Currently a cap of 1% per year of affordable purchase price
- Recommendation – change to \$5,000 per year cap
- Other terms will not change:
 - Wide range of work
 - Depreciated based on age and standard useful life
 - Documentation required
 - Only work that adds value
 - Not maintenance or repair
 - Can request waiver of cap for large projects
 - Only reviewed at time of sale

“Circuit Breaker”: Limit on Maximum Price

- Price may not become “unaffordable” to next buyer at the maximum income limit for the unit
- Based on Area Median Income (AMI) for maximum household size for unit – 2 people for a 1, 4 for a 2, 6 for a 3
- “Unaffordable” means **housing costs** would be more than 30% of monthly income at that AMI limit
- Housing costs include: mortgage principal & interest; condo fee; property taxes; and homeowner’s insurance

Affordability Examples – Two Bedroom 80% AMI Limit

Value at Resale	Mortgage P & I at 7%	Condo Fee	Insurance	Property Taxes	Monthly Costs	AMI for 4 people
\$225,000	\$1,452	\$450	\$25	\$9	\$1,936	52% AMI
\$400,000	\$2,581	\$250	\$25	\$9	\$2,865	77% AMI

What would trigger “circuit breaker”?

- Costs for home increase more than income limits:
 - Interest rate increases (and decreases)
 - Condo fee increases
 - Increases to taxes or typical owner insurance
- Not new - there is a “circuit breaker” in the current restriction

Inheritance

Where are starting from?

- Upon death of owner, unit must be sold to an income-eligible buyer
- Heir(s) receive sales proceeds
- Non-owner spouse may occupy home for their lifetime
- Other occupants have at least one year to relocate
- CDD practice has been to work with family members living in home to see if they can purchase

Priorities from stakeholders

Current owners:

- Option for family members to stay in Cambridge is important
- For some owners, stability of family in home is more important than value increase
- Many owners want the opportunity to be available to others who need it – not a “closed system”
- Children/family raised in the home are priority for inheritance

Applicants waiting for housing:

- Positive view of inheritance, but more important to keep homes opportunities available to all

Trust/City: Need to balance stability for current owner families, opportunities for others, and regulatory requirements



Recommendation: Inheritance Policy

- Allow inheritance as owner-occupant for certain heirs
- Income eligibility requirement **must remain**
- New owner must enter into new Affordable Housing Covenant
- If not eligible or interested, Covenant sales process followed

Inheritance Policy Concept

- Transfer through inheritance for income-eligible heirs added to allowable transfers
- Eligibility requirements included in restriction
- Heir must be income-eligible at time of transfer
- City does not determine heir
- City restriction only – other restrictions may be in place

Proposed Recommendations – Key Questions

- Should the option to inherit as an owner-occupant have any limits on heirs?
- If there limits, who should be included?
 - Only immediate family members
 - Extended family
 - Only people who have lived in Cambridge
 - Other?
- Understanding that homes must stay affordable, does the proposed recommendation for a resale formula work well? What would you change?
- Should there be a value decrease for units in poor condition?

All comments are welcome – your input is greatly appreciated.

What Happens Next?

- Owner feedback period:
 - Sessions through 12/14/23
 - Written comments through 1/4/24
Submit to homeownership@cambridgema.gov
 - Survey through 12/21/23
- Trust discussion of owner feedback
- Trust vote on changes
- Implementation

Implementation Steps



Development of new
Affordable Housing
Covenant



Information to owners on
new Covenant terms and
differences from previous
restriction



Each owner decides if they
want to sign new Covenant



Covenant must be signed
and recorded at Registry of
Deeds