The Regents of the University of California

COMMITTEE ON COMPENSATION
COMMITTEE ON FINANCE
May 17, 2007

The Committees on Compensation and Finance met on the above date at UCSF–Mission Bay Community Center, San Francisco.

Members present:	Representing the Committee on Compensation: Regents Blum, Coombs, Dynes, Hopkinson, Lozano, Parsky, Pattiz, Schilling, and Varner; Advisory members Brewer and Oakley Representing the Committee on Finance: Regents Blum, Dynes, Gould, Hopkinson, Island, and Parsky; Advisory members Bugay and Oakley, Staff Advisors Brewer and Miller
In attendance:	Regents Johnson, Ledesma, Marcus, Ruiz, and Schreiner, Regent-designate Allen, Faculty Representative Brown, Secretary and Chief of Staff Griffiths, Associate Secretary Shaw, General Counsel Robinson, Chief Investment Officer Berggren, Provost Hume, Executive Vice Presidents Darling and Lapp, Vice Presidents Broome and Foley, Chancellors Birgeneau, Drake, Fox, Kang, Vanderhoef, and Yang, Acting Chancellor Blumenthal, and Recording Secretary Smith

The meeting convened at 12:00 p.m. with Committee on Finance Chair Gould presiding.

RECOMMENDATION FOR REVISIONS AND MODIFICATIONS OF PROGRAM POLICIES FOR UNIVERSITY OF CALIFORNIA MORTGAGE ORIGINATION PROGRAM

The President recommended approval of the revisions and modifications to the Mortgage Origination Program Policies, as detailed in the Attachment.

The Mortgage Origination Program (MOP) was initially approved by The Regents at the July 1984 meeting and serves as the primary mortgage loan program supporting the recruitment and retention needs of the University. The University also administers the Supplemental Home Loan Program, which was approved by The Regents at the March 1993 meeting and designed to provide greater loan term flexibility to the campuses to address many unique circumstances that arise in the course of recruiting and retaining top faculty and staff.

An overview of both programs describing their general structure, loan products, and utilization was presented at the July 2006 meeting. That overview included a brief description of several categories of approvals that have been authorized by The Regents for the making of loans for purposes, or with attributes, differing from certain specified standard program policies. A mailing to The Regents in November 2006 provided further written background information on each of these authorized approval categories, including authorized procedures for granting the approvals and statistics on utilization. At the March 2007 Regents meeting, a discussion item was presented detailing proposals for either maintaining or altering the procedures for approving loans with non-standard attributes as well as program enhancements. Based upon the discussion at that meeting and subsequent consultation with the Academic Senate, only the MOP recommendations are being presented to The Regents at this meeting. Additional consultations are under way to further refine the recommended updates and modifications to the Supplemental Home Loan Program, which will be presented to The Regents at a future meeting.

The following sections recap the recommendations for updates and changes to the MOP policies. The attached policy document also includes proposed editorial changes to clarify ambiguities, reflect ongoing operational practices, and reorganize the Program eligibility and loan specific policies.

Review of and Proposed Modifications to Non-Standard Loan Program Policy Approval Categories

The addition of each of these categories was approved by The Regents in response to needs identified over time to address varying individual situations and local market conditions. The current MOP policies, as adopted by The Regents, designate the process for reviewing and approving each such request. Below is a summary of each approval category, including recommendations for modifications. The proposals for the approval processes strive to strike a balance that facilitates the University's ability to offer timely recruitment and retention packages that are competitive and that address the very high costs of housing near many UC campuses, while maintaining appropriate oversight of sensitive or larger financial transactions.

(1) **Approval of MOP Limited Resource Allocation Loans –** Current approval authority for Limited Resource Allocation Loans under MOP provides that chancellors may designate up to 15 percent of the program funds allocated after June 2000 for the following non-first time purchase situations:

- refinancing existing housing debt secured on the borrower's primary residence.
- receiving a second MOP loan near the same work location replacing a primary residence.
- receiving a MOP loan to purchase a primary residence even though the applicant previously owned a home near the work location within the past 12 months.

Based upon the percentage limitations, a cumulative total of $232.2 million is authorized for these types of resource-limited uses for the program funds allocated through June 30, 2007. As of March 31, 2007, 336 loans totaling $153.9 million have been funded for these purposes.

Action:

- chancellors to retain the approval authority for these limited purposes.
- MOP policy be rewritten to clarify the minimum utilization level for primary purpose loans (e.g., loans for purchase of first home near the work location) is 85 percent, and the maximum allowed usage of allocated funds for the limited resource purposes is up to 15 percent.

(2) **Approval for Program Participation of Positions not Designated as Eligible by MOP Policies –** Current approval authority provides that the President may designate otherwise non-eligible titles for program participation in MOP based upon the recruitment or retention needs and goals of the University (*eligible titles are members of the Academic Senate and the Senior Management Group*).

As of March 31, 2007, only 58 such approvals have been granted for MOP loans (compared to a total of 3,843 MOP loans funded).

Action:

- President to retain approval authority for those positions that do not otherwise require Regents' approval for participation at the time the approval is granted. Regents' approval would be required for positions with cash compensation above the Indexed Compensation Level or employees appointed to positions named by The Regents as requiring compensation approvals.

(3) **Approval of Non-Conforming Loan Terms within Policy Established by The Regents –** Current approval authority provides that the President may approve two types of non-conforming loan terms, either acting alone or with concurrence of the Chairman of the Board of Regents and the Chair of the Committee on Finance. These current authorities are as follows:

- Graduated Payment MOP (GP-MOP) loans: the President is currently authorized to approve a greater than the standard 3 percent maximum initial rate reduction and/or a smaller than the standard minimum.
- 0.25 percent annual decrease in the rate reduction for GP-MOP loans. The standard GP-MOP loan policies provide that the initial interest rate paid by the borrower can be reduced by a maximum of 3 percent from the Standard MOP Rate with a floor rate of 3 percent. Campuses transfer funds to provide the same yield that would have been realized under the Standard MOP Rate. The standard policy also provides that the interest rate reduction amount decreases by 0.25 percent to 0.50 percent annually, until the borrower is paying the Standard MOP Rate, normally over a six to twelve year period. As of March 31, 2007, seven such approvals for non-standard GP-MOP loan terms have been granted.
- Non-Conforming Loan-to-Value Ratios: the President is currently authorized, with the concurrence of the Chairman of the Board of Regents and the Chair of the Committee on Finance, to approve increases in normal maximum loan-to-value ratios (LTV) for MOP loans.

The standard MOP policy provides that MOP loans up to $1,330,000 have a maximum LTV of 90 percent, with any MOP loan in excess of that amount being limited to a maximum 85 percent LTV. The current approved MOP policies authorize increasing the MOP LTV to a maximum of 90 percent for loan amounts in excess of the $1,330,000 amount under the described concurrence procedure (this dollar threshold amount is indexed each April, based upon increases in the "All-Campus Average Sales Price"[1] from an annual zip code study performed by the Office of Loan Programs).

To date, there have been no requests or approvals of an increased LTV for a MOP loan.

Actions:

- GP-MOP: President to retain approval authority for those positions that do not otherwise require Regents' approval for participation at the time the approval is granted. Regents' approval would be required for positions with cash compensation above the Indexed Compensation Level or employees appointed to positions named by The Regents as requiring compensation approvals.
- LTV: President to retain approval authority, with expansion of the concurrence requirement to include the Chairman of the Board of Regents, Finance Committee Chair, and Compensation Committee Chair.

(4) **Approval of Non-Conforming Loan Size within Policies Established by The Regents –** Current approval authority requires that the President, with the concurrence of the Chairman of the Board of Regents, approve the offering of any MOP loans in excess of $1 million.

Unlike other similar MOP limits or thresholds, this loan size threshold was not indexed when adopted in 2000. At that time, the All-Campus Average Sales Price was $446,000. The 2006 All-Campus Average Sales Price was $805,800, or an 80.7 percent increase since adoption of this additional approval requirement. Given the rapid increase in prices of the past several years, it can be anticipated that more loans, or combinations of loans, at or above $1 million will be needed to compete adequately for many good candidates, especially in the professional and medical schools.

Actions:

- increase the MOP size approval threshold to $1,330,000 (to match current indexed loan size limit for 90 percent MOP loans) and annually index this amount based upon the change in the All-Campus Average Sales Price index each April (the value shown reflects the April 2007 index value).

[1] The Office of the President has conducted annual analyses since 1988 of the median cost of housing in zip code areas near each campus where most faculty live or are buying homes. Those numbers are then averaged to produce an average price for the campuses called the "All-Campus Average Sales Price."

- revise the concurrence approval process for any MOP loan in excess of this indexed amount to require approval by the President and expanded concurrence by the: Chairman of the Board of Regents, Finance Committee Chair (*new*), and Compensation Committee Chair.

Program Enhancement

The Regents approved several changes to the University's mortgage loan programs at the November 2001 meeting based upon the work and recommendations of the UC Housing Task Force. The prior program changes included the addition of the GP-MOP loan and authorization to sell MOP loans. The price of residential real estate has continued to escalate since that time, and many highly sought-after appointees are finding the housing markets near their campus to be increasingly challenging. In 2001, the median price of a house in California was $262,350, or 68 percent higher than the national median price of $156,600. By the end of 2006, the California median price had risen to $556,640, or 151 percent greater than the national figure of $221,900. This differential is even more severe when considering the housing markets surrounding the University's campuses where most faculty desire to live. In 2001, the All-Campus Average Sales Price near UC campuses was $489,400 or 213 percent higher than the national median price of $156,600. By 2006, the All-Campus Average Sales Price had risen to $805,800, or 263 percent greater than the national figure of $221,900. Additionally, the All-Campus Average Sales Price increased 65 percent between 2001 and 2006. Historically, approximately 65 percent of all hired faculty are from outside of California.

In light of the continuing housing price situation and issues faced by recently recruited faculty, several program modifications were reviewed for their potential to maintain the University's ability to remain competitive in recruiting and retaining many highly sought-after faculty and administrators. The recommendation presented below represents an enhancement to MOP believed to have the most potential for addressing the problems created by the continued increases in housing prices and growing affordability gap faced by recent hires.

Modify MOP Policies to Provide an Alternative Loan Product Offering an Initial Period of Interest-Only Payments

The rapid and continued increases in home prices near UC campuses over the past two to three years are making it harder for many newly-hired faculty to afford the required monthly payments associated with a home purchase for a house near their campus. This is particularly true for junior faculty, who often are purchasing their first home. Additionally, this situation often discourages more senior faculty being recruited from lower cost areas, given the prospect of a significant differential between the cost for comparable housing near the UC campus and their current situation.

***Action*:**
Create a new MOP loan product that has a temporary interest-only repayment feature for up to 10 years (the interest-only rate would adjust annually) and maximum overall term of 40 years (IO-MOP). Unlike many similar conventional market loan products, these loans would not have negative amortization. During the interest-only period, the interest rate would be a quarter of a point higher than the Standard MOP Rate. At the end of the interest-only period (IO-Period), the fully amortized payment would be calculated using the remaining loan term (always at least 30 years) at the then Standard MOP Rate. The quarter point reduction in rate at the beginning of the fully amortizing period, coupled with a minimum of at least 30 years for amortized payments, reduces the magnitude of the payment increase at the end of the interest-only period.

Advantages:
These loans would (1) provide reduced monthly payments to borrowers in the early years of the loan; and (2) provide easier qualifying for borrowers, reducing monthly income required to qualify for the same loan size or facilitate qualifying for a larger loan; and provide a product type that is common in the conventional marketplace.

Risk Assessment Observations:
(1) There would be no negative impact on the MOP rate of return, as the Standard MOP Rate of interest would continue to track the STIP rate of return as do non-IO-MOP loans; (2) The borrowers would be affected by increased monthly payments when the IO-Period ends, which would be partially mitigated by annually adjusting the IO-Period interest rate, returning to Standard MOP Rate at the end of the IO-Period, and having at least a 30-year amortization period remaining after the IO-Period ends; (3) The borrowers would accumulate less equity during the IO-Period and pay more total interest over the life of the loan than for a fully amortizing MOP loan; and (4) The University would be subject to some increased exposure to principal losses in the event of a market downturn or if a borrower leaves the University or otherwise must pay off the loan in the early years of the loan.

Technical and Editorial Updates to Program Policies

Other minor modifications, editing, and formatting changes were proposed to the MOP policies to clarify ambiguities, reflect ongoing operational practices, and reorganize the Program eligibility and loan specific policies. The following highlights some of those items.

(1) **Eligible Population Definitions –** Update to: (a) include the requirement for Regental approval of certain groups of employees for participation in these programs, and (b) recognize that some appointees are initially hired with non-qualifying academic titles, while waiting for campus approvals of the final eligible title contained in the hiring letter.

(2) **Definition of Eligible Residence –** Update to: (a) clarify that incidental secondary units, often referred to as “grad-flats” or “in-law units,” are allowed to be a part of the property (these types of single family properties are very common near many campuses), and (b) clarify that a participant is not required to occupy the residence during approved leaves.

(3) **Provisions for Continued Program Participation** – Update to clarify that administrative discretion is available in evaluating the enforcement of the payoff requirements in individual cases (in some cases, market conditions, health, other family matters, etc. may warrant temporary forbearance rather than moving to foreclosure or other similar action).

Regent Parsky clarified that the MOP loan program is part of compensation afforded under Regental compensation policies. Any compensation package that required Regental approval, and that included these adjusted loans, would continue to be submitted to The Regents for approval.

Upon motion duly made and seconded, the Committee approved the President’s recommendation and voted to present it to the Board.

The meeting adjourned at 12:05 p.m.

Attest:

Secretary and Chief of Staff