

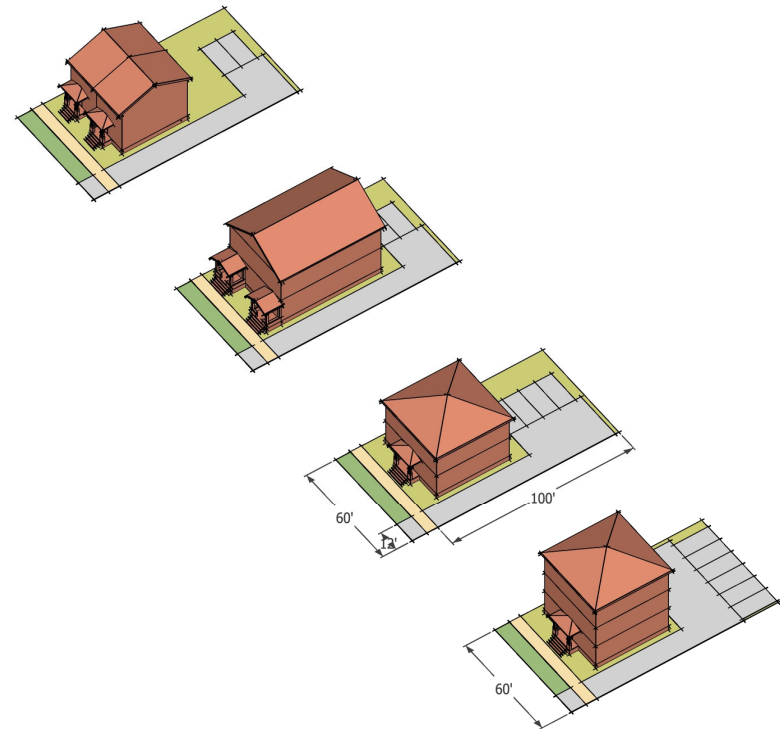
Santa Rosa Missing Middle Housing Feasibility Study Methodology and Findings

Overview of Analysis

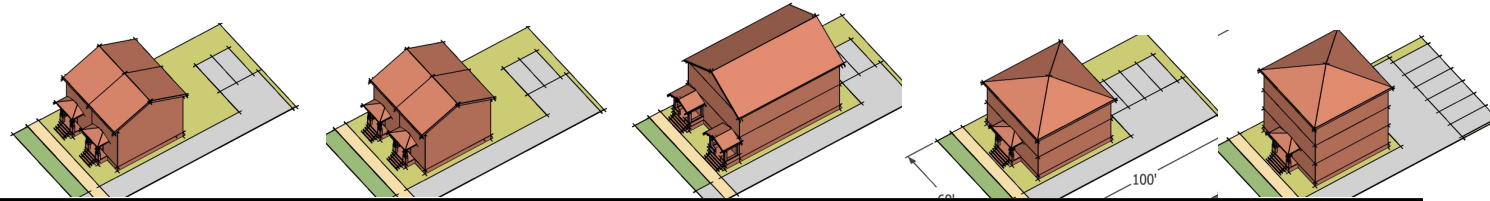
- Strategic Economics assessed the financial feasibility of various Missing Middle Housing types
 - Entails estimating project revenues and all development costs to determine likelihood that a private developer will undertake the project
- “Missing Middle Housing” (MMH) is defined as:
 - Multi-family buildings with between two and 19 units (in the “middle” of single-family homes and larger-scale multi-family buildings)
 - Can be rental apartments or for-sale units
 - MMH refers to the **building type**, and does **not** refer to the household income categories to which the units are affordable

Approach and Overview of Prototypes

- A static pro forma model was used to measure the financial feasibility of prototypes using the “land residual” method
 - If the residual land value is lower than the market value of land in Santa Rosa, the prototype is not feasible
- All prototypes reflect buildings that could be constructed on a 6,000 square foot lot with one parking space per unit
 - Small Duplex
 - Large Duplex
 - Fourplex
 - Sixplex
- Tested both rental and for-sale products depending on unit size (tenure was based on developer input and review of housing built in Santa Rosa)



Basic Prototypes Information



	Small Duplex (Rental)	Small Duplex (Condo)	Large Duplex (Condo)	Fourplex (Rental)	Sixplex (Rental)
Dwelling Units per Acre	15	15	15	29	44
Stories	2	2	2	2	3
Unit Type	2-BR	2-BR	4-BR	1-BR	1-BR
Unit Size	1,440	1,440	2,200	720	720
Building Efficiency	100%	100%	100%	90%	90%
Parking Type	Surface	Surface	Surface	Surface	Surface
Total Parking Spaces	2	2	2	4	6

Developer Interview Summary

- 6 multifamily developers, one architect, one small-scale, high-end single-family home developer, all of whom are active in Sonoma County
- Conducted between July and November of 2021
- Supplemented with relevant findings from MMH analyses Strategic Economics prepared for other another Bay Area city.

DBC

Revenue Assumptions

- Revenue assumptions reflect variation in unit value by area of Santa Rosa
- Feasibility tested in 3 different areas (“tiers”) to reflect market variation in home values across the City
- Tiers defined based on developer input, multifamily rental data from Costar, and single-family/townhome sales prices from Redfin
 - Tier 1: East of Hwy 101, north of Hwy 12
 - Tier 2: East of Hwy 101, south of Hwy 12
 - Tier 3: Everything west of Hwy 101
- Sales price/rent estimates for each tier developed using comps both inside and outside Opticos’ “MMH Transition” areas

Revenue Assumptions

Revenue Summary	Tier 1	Tier 2	Tier 3
2-BR Duplex Units			
Rent (per month)	\$3,250	\$3,250	\$3,000
Sales Price	\$706,000	\$634,000	\$562,000
4-BR Duplex Units			
Sales Price	\$946,000	\$836,000	\$726,000
1-BR Fourplex and Sixplex Units			
Rent (per month)	\$2,300	\$2,300	\$2,100

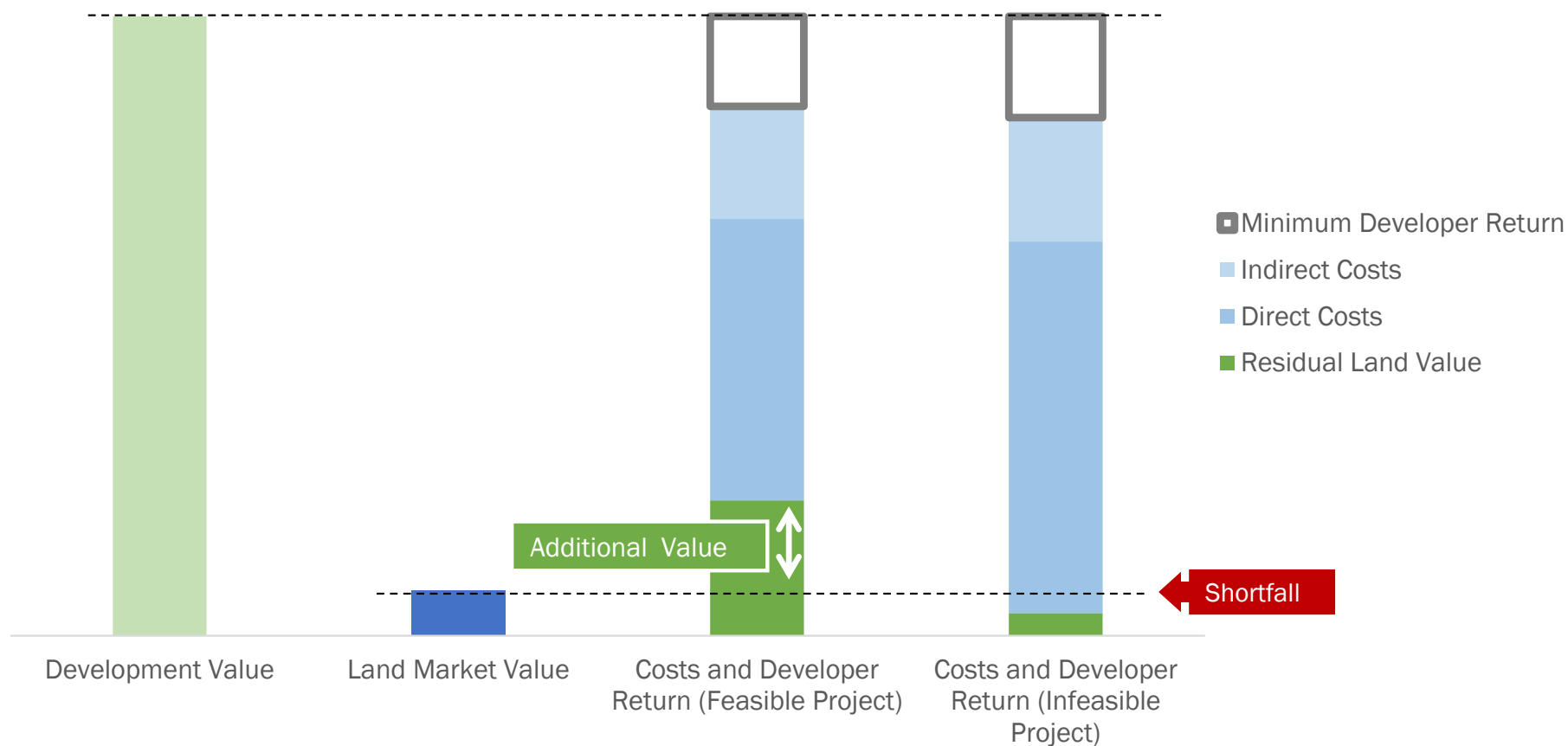
Note: All prices reflect monthly rent / total sales price per unit.

Source: Strategic Economics, 2021

Construction Costs: Definitions

- **Site Acquisition Costs:** The cost of acquiring land for development, including either land that already has an existing structure or vacant land
- **Hard Costs (aka Direct Costs):** Includes all building materials and construction labor costs associated with building the vertical structure
- **Soft costs (aka Indirect Costs):** Includes fees charged by consultants, such as architecture and engineering fees; City fees; and marketing costs (for condos only)
- **Developer return:** The estimated profit expectations that developers have when determining whether to pursue a project

Project Revenue versus Project Costs in a Residual Land Value Approach



Site acquisition cost assumptions

- Site acquisition costs reflect that an existing home would likely need to be acquired for MMH development
- Acquisition costs therefore primarily defined using sales prices of homes that are:
 - Older (pre 1970s)
 - On lots between 5,500 and 6,500 square feet
 - Used lowest quartile of sales prices for homes meeting these criteria
- While there are few vacant infill parcels available in Santa Rosa, acquisition costs were also developed for vacant land

Tier	Older home acquisition cost	Vacant land acquisition cost
Tier 1	\$540,000	\$225,000
Tier 2	\$540,000	\$215,000
Tier 3	\$444,000	\$200,000

Hard Cost Assumptions

- Costs of fourplex and sixplex are significantly higher than duplexes due to additional plumbing and fixtures
- Construction costs assumed to be higher for condo duplexes than for rental duplex due to:
 - Higher costs associated with premium finishes
 - Limited number of builders have construction liability insurance needed to build for-sale multi-family buildings

Prototype	Hard Costs per Gross Building Sq. Ft.
Small Duplex (Rental)	\$300
Small Duplex (Condo)	\$325
Large Duplex (Condo)	\$325
Fourplex (Rental)	\$400
Sixplex (Rental)	\$400

Soft Costs: City Fees

- Several major City fees categories are prorated by square feet in each unit
- As a results, per unit fees are considerably lower for higher density prototypes than for lower density prototypes and single-family homes

Prototype	Total Fees	Fee Per Unit
Small Duplex (Rental)	\$78,528	\$39,264
Small Duplex (Condo)	\$78,528	\$39,264
Large Duplex (Condo)	\$92,598	\$46,299
Fourplex (Rental)	\$91,812	\$22,953
Sixplex (Rental)	\$131,350	\$21,892
<i>Example 2,880 sq ft house</i>	<i>\$63,169</i>	<i>\$63,169</i>

Other Cost Assumptions

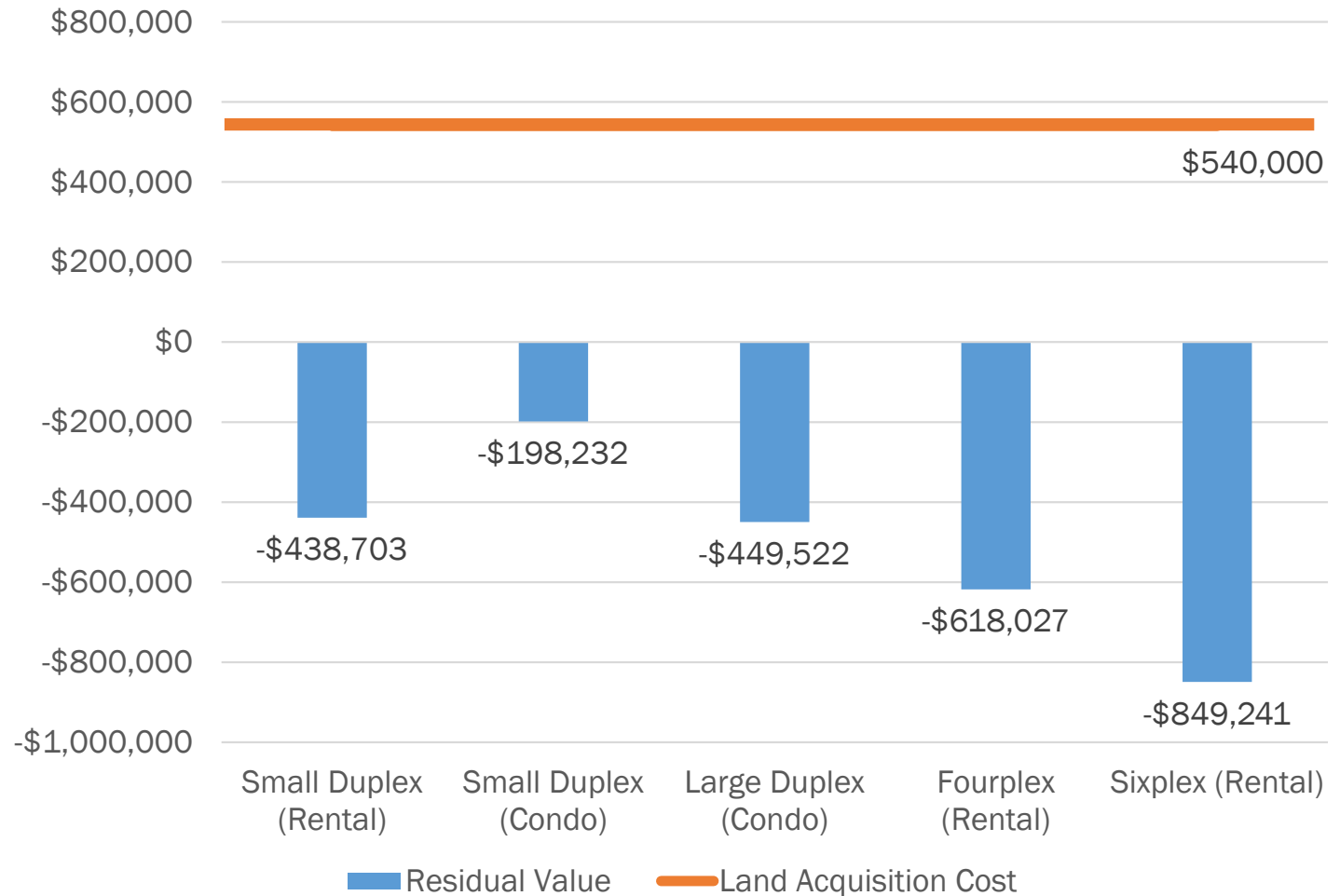
Cost Category	Value
Hard Costs	
Site Prep, Demolition	\$10 per land sq. ft.
Hard Cost Contingency	5% of hard costs
Soft Costs (excluding financing and fees)	
Architecture, Engineering, Developer Overhead	\$50,000 per project
Marketing Costs for Condos	4% of sales value
Other Soft Costs (a)	8% of hard costs
Developer Return	
Minimum Yield on Cost (Rental Prototypes)	6.00%
Minimum Return on Cost (For-Sale Prototypes)	20%

Source: Strategic Economics, 2021

Results – Tier 1 (Northeastern Santa Rosa)

Residual Value
Relative to
Land
Acquisition
Costs

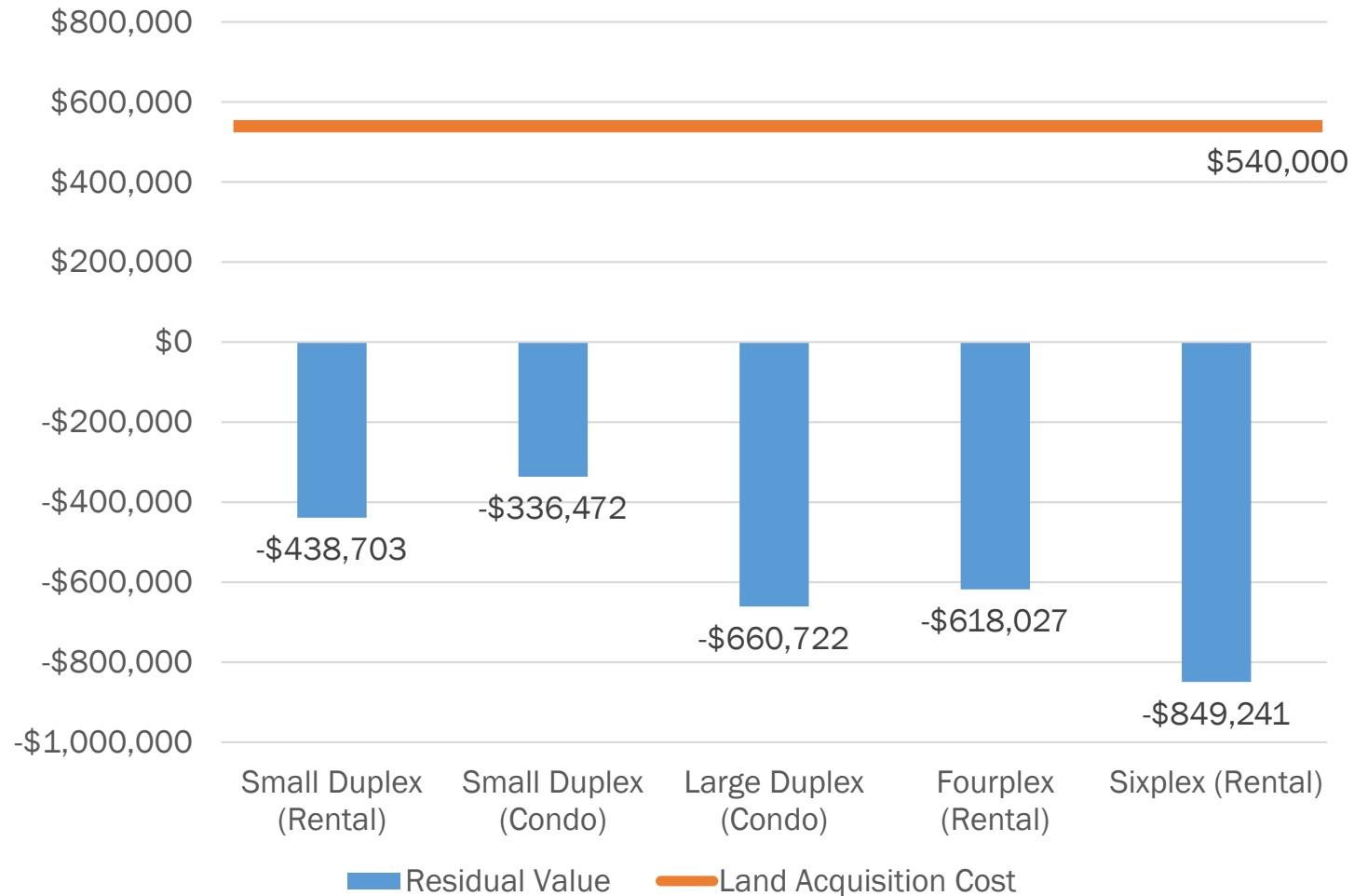
Shortfall
ranges from
\$738,000
(Small Duplex
Condo) to \$1.4
million
(Sixplex)



Results – Tier 2 (Southeastern Santa Rosa)

Residual Value
Relative to
Land
Acquisition
Costs

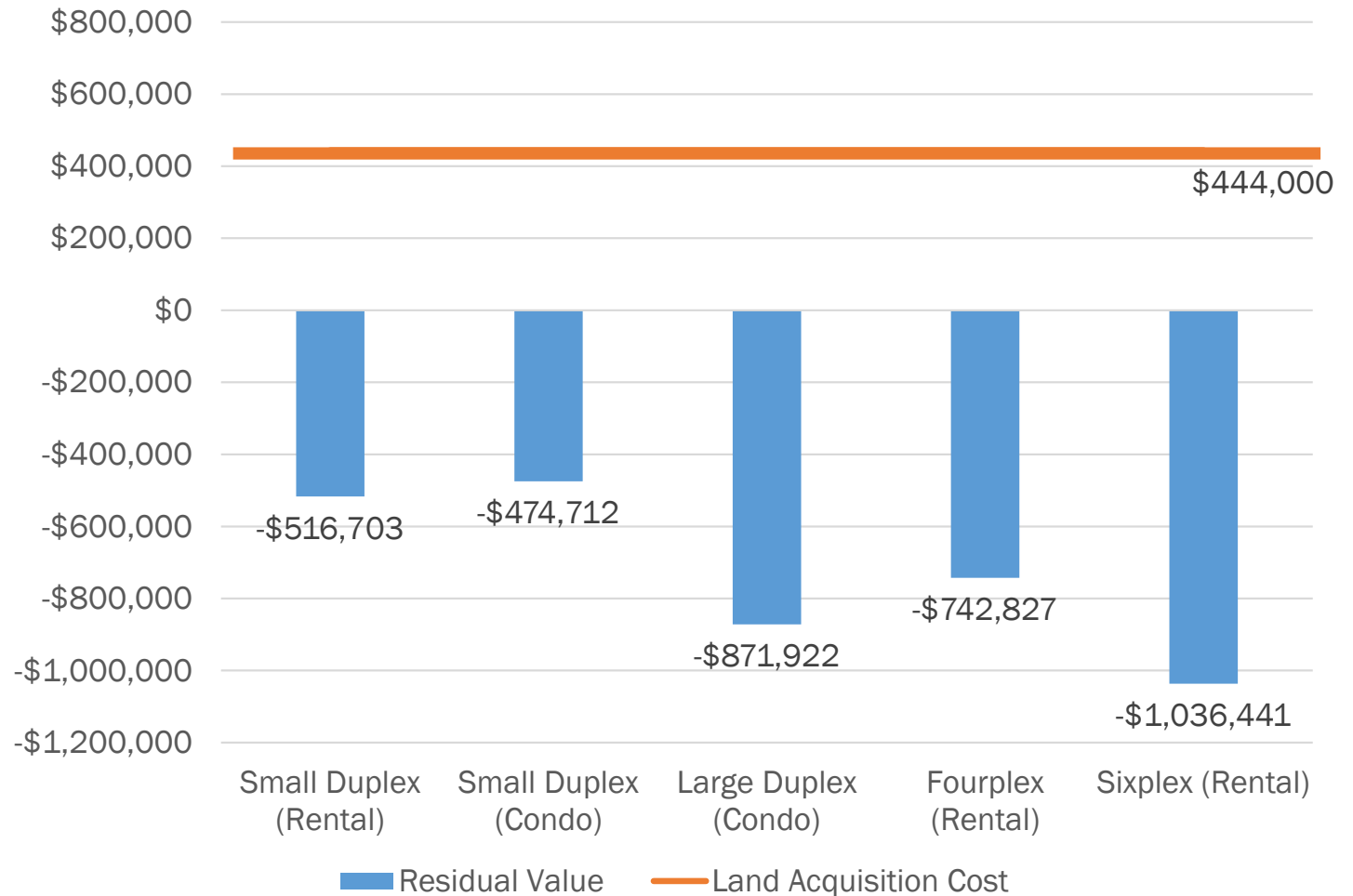
Shortfall
ranges from
\$876,000
(Small Duplex
Condo) to \$1.4
million
(Sixplex)



Results – Tier 3 (Western Santa Rosa)

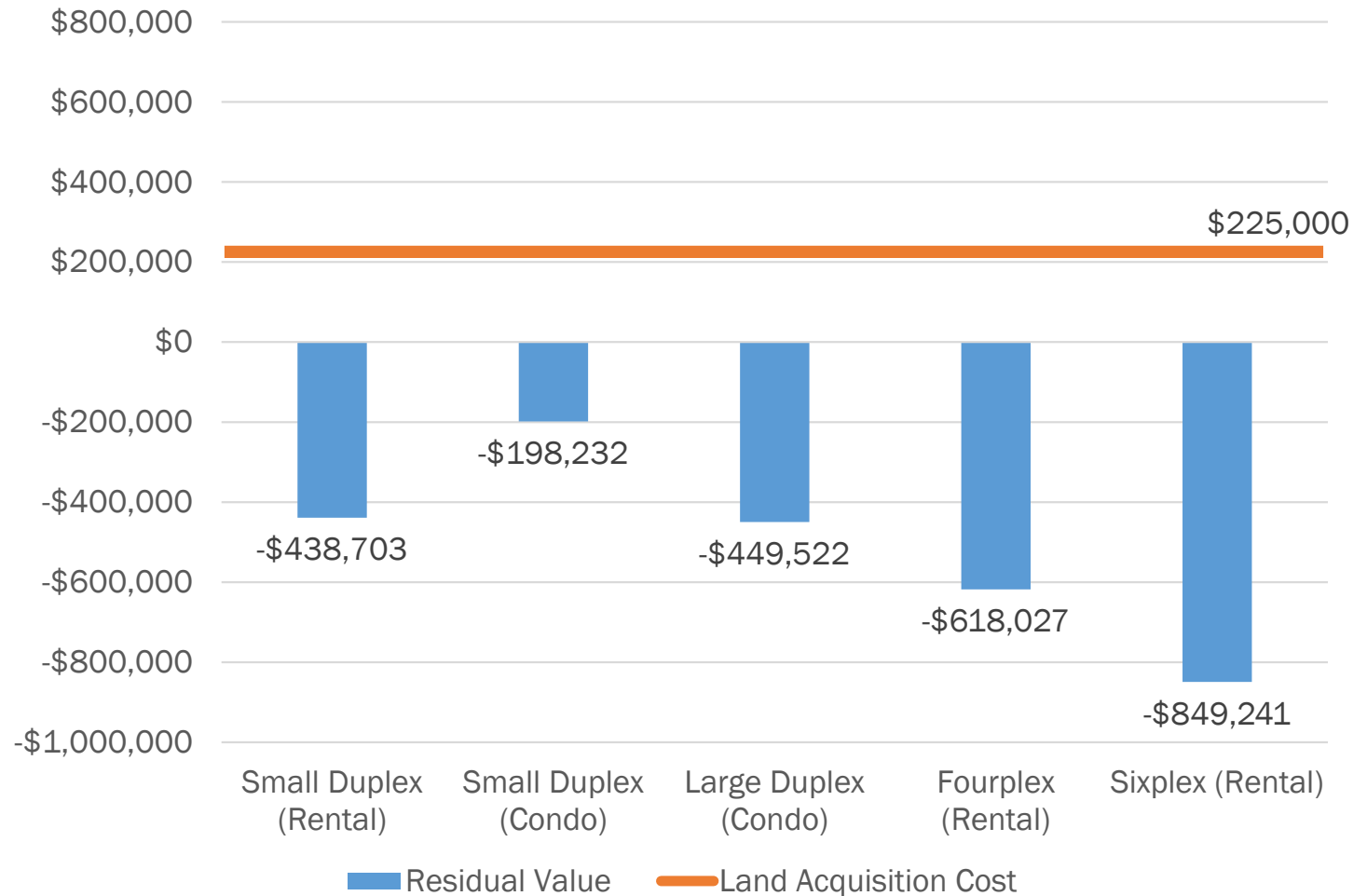
Residual Value
Relative to
Land
Acquisition
Costs

Shortfall
ranges from
\$919,000
(Small Duplex
Condo) to \$1.5
million
(Sixplex)



Results – Vacant Land Acquisition (Tier 1)

Even assuming vacant land acquisition costs, shortfall is between \$423,000 and \$1.1 million for Tier 1 properties



Findings

- Standard market mechanisms driven by investment return expectations are not likely to deliver MMH in the short run.
- Today, MMH might only be delivered by mission-driven developers with low investment return expectations and/or single-family homeowners who could build projects on their property without paying land acquisition costs
- Construction costs are, conservatively, 20% higher in Sonoma County than the inner Bay Area because of scarcity of available builders in the area/distance from construction labor pool
- Santa Rosa rents/sales prices for MMH product types are currently not high enough to cover construction costs, even in Tier 1 areas
- City fees are already prorated according to unit size/project type and are not a major barrier to feasibility

Findings (Continued)

- If missing middle projects were feasible, units in these projects would likely be priced similarly to existing market-rate units (and would not be “naturally” more affordable)
- Affordable housing developers are largely unable to build MMH
 - To be competitive for tax credit financing, most projects need include at least 35 units DB0
 - Small-scale, scattered-site projects pose difficulties for operations & maintenance unless sites are geographically co-located
- Well-managed street parking is critical in areas where the City seeks to attract DB1 MMH housing

Findings (Continued)

- Several commonly utilized strategies for improving feasibility (reducing parking requirements, adding additional density, allowing smaller units) will not improve short-term financial feasibility for MMH in Santa Rosa
- However, innovations in modular construction could significantly decrease MMH construction costs within the next 5-10 years and could potentially be a game-changer for MMH development
- Laying the policy groundwork for MMH now will allow the City to capitalize on emerging opportunities to expand the housing supply if/when construction costs decrease

Recommendations for Encouraging Missing Middle Housing (MMH)

- Support efforts to grow the construction labor force in Sonoma County (apprenticeship programs, business incubators, etc.)
- Maintain prorated City fee structure for multi-unit buildings, and maintain predictability in City fee schedule
- Facilitate and manage street parking in areas desired for Missing Middle housing development
- Explore utilizing a larger (2-3 acre) city-owned parcel that is unsuitable for higher-density development as a pilot project site for MMH to provide “proof of concept” for MMH’s viability

Recommendations for Encouraging Missing Middle Housing (Continued)

- Establish an information campaign for the housing development community about MMH products to facilitate MMH development if/when construction costs drop and development becomes feasible
- Establish a similar information campaign for property owners who might want to build duplexes in their back yards
- Explore option to identify “fee developers” who could manage the duplex construction process for individual property owners
- Work with other cities to explore options to create an alternative loan pool for small scale developers and/or individual homeowners who want to build MMH projects but can't get financing. This loan pool could be managed through a community development finance institution or financial institution

Appendix: Detailed Prototypes Information and Assumptions

Detailed Prototypes Information

	Small Duplex (Rental)	Small Duplex (Condo)	Large Duplex (Condo)	Fourplex (Rental)	Sixplex (Rental)
Parcel Size (Sq. Ft.)	6,000	6,000	6,000	6,000	6,000
Gross Building Sq. Ft.	2,880	2,880	4,400	3,200	4,800
Net Building Sq. Ft.	2,880	2,880	4,400	2,880	4,320
Building Efficiency	100%	100%	100%	90%	90%
Number of Units	2	2	2	4	6
Unit Density (Dwelling Units per Acre)	15	15	15	29	44
Stories	2	2	2	2	3
Unit Type	2-BR	2-BR	4-BR	1-BR	1-BR
Unit Size	1,440	1,440	2,200	720	720
Parking Type	Surface	Surface	Surface	Surface	Surface
Parking Spaces	2	2	2	4	6
Parking Ratio	1.00	1.00	1.00	1.00	1.00

Detailed Cost Assumptions

	Unit of measure	2-BR Duplex, 2 Units (Rental) Prototype 1A	2-BR Duplex, 2 Units (Condo) Prototype 1B	3-BR Duplex, 2 Units (Condo) Prototype 2	Fourplex (Rental) Prototype 3	Sixplex (Rental) Prototype 4
Hard Costs						
Site Prep/Demo	per square foot	\$10	\$10	\$10	\$10	\$10
Vertical Hard Costs						
Main Structure	per gross sf	\$300	\$325	\$325	\$400	\$400
Hard Cost Contingency	% of vertical costs	5%	5%	5%	5%	5%
Soft Costs						
Architecture, Engineering, Developer Overhead	overall	\$50,000	\$50,000	\$50,000	\$50,000	\$50,000
Soft Costs	% of hard costs	8%	8%	8%	8%	8%
Municipal Fees		\$78,528	\$78,528	\$92,598	\$91,812	\$131,350
Marketing Costs for Condos	% of sales value		4%	4%		
Financing						
Total Cost	% of hard+soft costs	3.5%	3.5%	3.5%	3.5%	3.5%
Developer Return						
Minimum Yield-on-Cost	NOI / (TDC+Land)	6.00%			6.00%	6.00%
Minimum Return-on-Cost	Net Revenue / (TDC+Land)	20%	20%	20%	20%	20%

Detailed Revenue Assumptions

	Unit of measure	Tier 1	Submarket Tier 2	Tier 3
Rental Monthly Rents				
2-BR Duplex				
Unit size	nsf	1,440	1,440	1,440
Per nsf	per nsf	\$2.26	\$2.26	\$2.08
Per unit	per unit	\$3,250	\$3,250	\$3,000
1-BR Fourplex or Sixplex				
Unit size	nsf	720	720	720
Per nsf	per nsf	\$3.19	\$3.19	\$2.92
Per unit	per unit	\$2,300	\$2,300	\$2,100
For-sale Prices				
2-BR Duplex				
Unit size	nsf	1,440	1,440	1,440
Per nsf	per nsf	\$490	\$440	\$390
Per unit(ROUNDED)	per unit	\$706,000	\$634,000	\$562,000
3-BR Duplex				
Unit size	nsf	2,200	2,200	2,200
Per nsf	per nsf	\$430	\$380	\$330
Per unit	per unit	\$946,000	\$836,000	\$726,000
Other Assumptions				
Vacancy Loss	% of GSI [a]	5%	5%	5%
Operating Expense	% of GSI [a]	30%	30%	30%
Cap Rate	NOI / Proj Value [b]	5.00%	5.00%	5.00%

Pro Forma – Small Duplex Rental

	Tier 1	Tier 2	Tier 3
Revenues			
Annual Gross Scheduled Income	\$78,000	\$78,000	\$72,000
Less Vacancy	-\$3,900	-\$3,900	-\$3,600
Less Expenses	-\$23,400	-\$23,400	-\$21,600
Net Operating Income	\$50,700	\$50,700	\$46,800
Capitalized Value	\$1,014,000	\$1,014,000	\$936,000
Development Costs			
Site Prep	\$60,000	\$60,000	\$60,000
Vertical Hard Costs	\$864,000	\$864,000	\$864,000
Contingency	\$43,200	\$43,200	\$43,200
Soft Costs	\$123,920	\$123,920	\$123,920
Municipal Fees	\$78,528	\$78,528	\$78,528
Financing Costs	\$40,938	\$40,938	\$40,938
Total Development Cost	\$1,210,586	\$1,210,586	\$1,210,586
Minimum Return	\$242,117	\$242,117	\$242,117
Residual Land Value	-\$438,703	-\$438,703	-\$516,703
Typical Site Acquisition Cost	\$540,000	\$540,000	\$444,000
Shortfall	-\$978,703	-\$978,703	-\$960,703

Pro Forma – Small Duplex Condo

	Tier 1	Tier 2	Tier 3
Revenues			
Gross Sales Revenue	\$1,412,000	\$1,268,000	\$1,124,000
Less Marketing Costs	-\$56,480	-\$50,720	-\$44,960
Net Sales Revenue	\$1,355,520	\$1,217,280	\$1,079,040
Development Costs			
Site Prep	\$60,000	\$60,000	\$60,000
Vertical Hard Costs	\$936,000	\$936,000	\$936,000
Contingency	\$46,800	\$46,800	\$46,800
Soft Costs	\$129,680	\$129,680	\$129,680
Municipal Fees	\$78,528	\$78,528	\$78,528
Financing Costs	\$43,785	\$43,785	\$43,785
Total Development Costs	\$1,294,794	\$1,294,794	\$1,294,794
Feasibility Summary			
Net Revenue Less Development Costs	\$60,726	-\$77,514	-\$215,754
Minimum Return	\$258,959	\$258,959	\$258,959
Residual Land Value	-\$198,232	-\$336,472	-\$474,712
Typical Site Acquisition Cost	\$540,000	\$540,000	\$444,000
Shortfall	-\$738,232	-\$876,472	-\$918,712

Pro Forma – Large Duplex Condo

	Tier 1	Tier 2	Tier 3
Revenues			
Gross Sales Revenue	\$1,892,000	\$1,672,000	\$1,452,000
Less Marketing Costs	-\$75,680	-\$66,880	-\$58,080
Net Sales Revenue	\$1,816,320	\$1,605,120	\$1,393,920
Development Costs			
Site Prep	\$60,000	\$60,000	\$60,000
Vertical Hard Costs	\$1,430,000	\$1,430,000	\$1,430,000
Contingency	\$71,500	\$71,500	\$71,500
Soft Costs	\$169,200	\$169,200	\$169,200
Municipal Fees	\$92,598	\$92,598	\$92,598
Financing Costs	\$63,815	\$63,815	\$63,815
Total Development Costs	\$1,887,113	\$1,887,113	\$1,887,113
Feasibility Summary			
Net Revenue Less Development Costs	-\$70,793	-\$281,993	-\$493,193
Minimum Return	\$377,423	\$377,423	\$377,423
Residual Land Value	-\$448,216	-\$659,416	-\$870,616
Typical Site Acquisition Cost	\$540,000	\$540,000	\$444,000
Shortfall	-\$988,216	-\$1,199,416	-\$1,314,616

Pro Forma - Fourplex

	Tier 1	Tier 2	Tier 3
Revenues			
Annual Gross Scheduled Income	\$110,400	\$110,400	\$100,800
Less Vacancy	-\$5,520	-\$5,520	-\$5,040
Less Expenses	-\$33,120	-\$33,120	-\$30,240
Net Operating Income	\$71,760	\$71,760	\$65,520
Capitalized Value	\$1,435,200	\$1,435,200	\$1,310,400
Development Costs			
Site Prep	\$60,000	\$60,000	\$60,000
Vertical Hard Costs	\$1,280,000	\$1,280,000	\$1,280,000
Contingency	\$64,000	\$64,000	\$64,000
Soft Costs	\$157,200	\$157,200	\$157,200
Municipal Fees	\$91,812	\$91,812	\$91,812
Financing Costs	\$57,855	\$57,855	\$57,855
Total Development Cost	\$1,710,867	\$1,710,867	\$1,710,867
Feasibility Summary			
Minimum Return	\$342,173	\$342,173	\$342,173
Residual Land Value	-\$617,840	-\$617,840	-\$742,640
Typical Site Acquisition Cost	\$540,000	\$540,000	\$444,000
Shortfall	-\$1,157,840	-\$1,157,840	-\$1,186,640

Pro Forma - Sixplex

	Tier 1	Tier 2	Tier 3
Revenues			
Annual Gross Scheduled Income	\$165,600	\$165,600	\$151,200
Less Vacancy	-\$8,280	-\$8,280	-\$7,560
Less Expenses	-\$49,680	-\$49,680	-\$45,360
Net Operating Income	\$107,640	\$107,640	\$98,280
Capitalized Value	\$2,152,800	\$2,152,800	\$1,965,600
Development Costs			
Site Prep	\$60,000	\$60,000	\$60,000
Vertical Hard Costs	\$1,920,000	\$1,920,000	\$1,920,000
Contingency	\$96,000	\$96,000	\$96,000
Soft Costs	\$208,400	\$208,400	\$208,400
Municipal Fees	\$131,350	\$131,350	\$131,350
Financing Costs	\$84,551	\$84,551	\$84,551
Total Development Costs	\$2,500,302	\$2,500,302	\$2,500,302
Feasibility Summary			
Minimum Return	\$500,060	\$500,060	\$500,060
Residual Land Value	-\$847,562	-\$847,562	-\$1,034,762
Typical Site Acquisition Cost	\$540,000	\$540,000	\$444,000
Shortfall	-\$1,387,562	-\$1,387,562	-\$1,478,762