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# House Bill 2001 Implementation Economic Analysis and Market Research Findings and Recommendations

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## Executive Summary

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Prepared for: Washington County

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# Executive Summary

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## Background

Oregon House Bill 2001 (HB 2001, passed in 2019) requires Washington County and other jurisdictions to allow middle housing—duplexes, triplexes, fourplexes, cottage clusters, and townhouses—in all residential districts that allow single-family detached housing, without restrictions that would create “unreasonable” cost or delay for middle housing development. Washington County intends to develop plan/policy and development code revisions that implement HB 2001 and offer equitable opportunities for middle housing while ensuring that planning for related infrastructure keeps pace. The County contracted with ECONorthwest to inform implementation of HB 2001, including:

- Identifying factors that affect the likelihood that middle housing development may develop (in particular, whether it is financially feasible to develop).
- Evaluating where in unincorporated Washington County middle housing may be more and less economically feasible to develop, to inform subsequent planning.
- Assessing likely impacts of potential County actions on middle housing feasibility, to inform policy decisions.

## About the Economic Feasibility Analysis

ECONorthwest’s analysis tests whether, where, and to what extent middle housing development might be financially feasible if the County implements regulations consistent with “minimum compliance” with HB 2001.

- **The analysis focuses on parts of the urban unincorporated area (UUA) designated for primarily single-family detached dwellings**, as this is where HB 2001 will result in the biggest changes to regulations. It is intended to identify where regulatory changes are most likely to result in new middle housing development that could not have otherwise occurred; it does not provide a comprehensive assessment of all places where middle housing is potentially viable.
- **The analysis does not predict whether or when individual properties will be developed with middle housing.** It estimates how many of the properties within the UUA may be feasible for middle housing development based on site size, current market conditions in that area, and the anticipated costs of middle housing development. Only a small share of properties where development is financially feasible may be available for development in a given year.
- **The analysis uses typical current (2020) costs and rents/sales prices for a given area.** It does not capture all potential circumstances, such as above-average costs for challenging slope or soil conditions, below-average costs due to financial or labor contributions from friends/family, or above-average sales prices due to views. It also does not project how

market conditions, development costs, and financing conditions may change over time, though both construction costs and rents/sales prices have escalated in the months since the data for this analysis was collected. Changes in development conditions over time will change the total amount of development that is potentially feasible, but the general trends of where there is greater development potential and which housing types show greater potential are more likely to hold true over time.

- The analysis is focused on potential development on vacant land and redevelopment on developed properties (replacement of an existing structure with middle housing). **It does not evaluate the potential to convert existing homes to middle housing or to build on undeveloped portions of a lot while retaining the existing home**, as these require much more site-specific assessments. As a result, it likely underestimates development potential in some cases.
- The analysis accounts for differences between land use designations and for stream corridor protections, but it does not address every site-specific physical and regulatory constraint and may overestimate development potential in some cases.

## Key Economic Feasibility Findings

### Overall Financial Feasibility Results

#### **Redevelopment potential is mostly limited to larger lots.**

- Redevelopment is likely not financially feasible on the vast majority of developed lots—especially those under 7,000 square feet—even if middle housing is technically allowed. The average home in a developed subdivision is very unlikely to redevelop with middle housing or new single-family detached housing anywhere in the UUA.
- Vacant lots and large lots with lower-value homes, manufactured homes, or accessory structures are more likely to be financially feasible for middle housing development. For many of these properties, single-family infill development is already financially feasible. While middle housing development may offer greater financial returns in some cases, other factors will likely continue to favor single-family detached development.

#### **Middle housing is feasible throughout the UUA, but on a small fraction of parcels.**

- Overall, less than 3 percent of the parcels included in this analysis are likely to be financially feasible for middle housing (re)development under current financial conditions (roughly 1,500 total parcels out of over 54,000 evaluated). However, if all these parcels were to develop fully with middle housing, they could add capacity for over 20,000 new housing units. This is highly unlikely, but it illustrates that there is substantial development potential for middle housing even on a small share of properties.

#### **New middle housing is more likely to be developed as ownership housing (especially townhouses and plex units that look like townhouses) than rental housing.**

- While rental housing development is financially feasible in some instances, for-sale housing generates greater financial returns in most cases. The number of local investors interested in buying new small-scale rental properties may also be a limiting factor. The most financially feasible form of duplexes, triplexes, and fourplexes is generally side-by-side units similar to townhouses that face the side of the lot rather than the street.
- Townhouses tend to be most financially feasible among the middle housing types. They can be sold “fee simple,” which typically allows for somewhat higher sales prices than condominium units and offers less legal risk for builders. In addition, on larger sites, it is often easier to build more townhouse units than to develop multiple plexes.<sup>1</sup>

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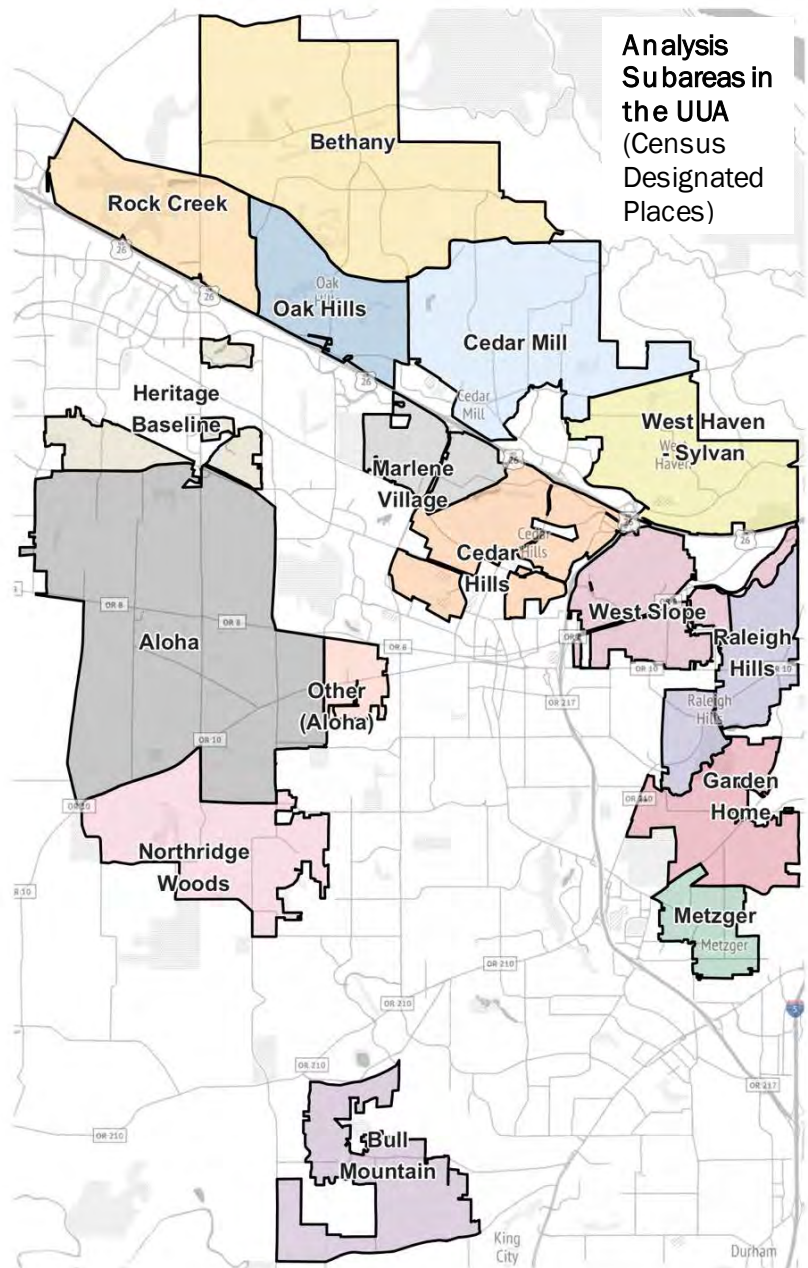
<sup>1</sup> There is legislation pending at the state level (Senate Bill 458) that could change this by requiring jurisdictions to allow a streamlined land division process for middle housing, including plexes, in lieu of condominium creation.

## Area-Specific Feasibility Observations

The subareas on the northern edge of the UUA (**Bethany, Cedar Mill, and West Haven-Sylvan**) have strong potential for both new townhouses and new single-family homes, with many vacant and very large lots and demand for ownership housing. While the market for single-family homes is very strong in these areas, townhouses at lower sales prices (under \$400,000) are roughly equally feasible as high-end single-family housing (estimated to sell for close to \$700,000) due to higher density.

In the north central part of the UUA (**Rock Creek, Oak Hills, Cedar Hills, and Marlene Village** subareas), there is very limited development potential (less than 1 percent of lots in most of these subareas) because the areas are almost entirely developed with single-family subdivisions with lots under 10,000 square feet and the price of new middle housing is not high enough to make redevelopment financially feasible in most situations.

The central subareas (**Aloha, Other/Aloha, and Heritage Baseline** subareas) contain many parcels with potential for middle housing development, but they represent only 1 to 3 percent of the parcels in these areas that were included in the analysis. Heritage Baseline includes a relatively large number of manufactured homes (some on individual lots and others in manufactured home parks) that could be financially feasible for redevelopment.<sup>2</sup> Washington



<sup>2</sup> Note, however, that the analysis does not fully account for redevelopment costs specific to manufactured home communities.



County's Office of Community Development and Department of Land Use and Transportation are collaborating on an inventory and analysis of existing manufactured housing parks. The second stage of their work will identify strategies for preservation because manufactured housing parks provide a unique unsubsidized affordable housing option that is hard to replace.

On the eastern side of the county (**Raleigh Hills and West Slope** subareas), there are some larger lots, but just 2 to 3 percent of the lots in the analysis were identified as economically feasible for middle housing development. The mix of feasible middle housing types is similar to the county overall.

In the southeast (**Garden Home and Metzger** subareas), 3 to 4 percent of lots included in the analysis were identified as having potential for middle housing development, and a range of middle housing types are feasible (though townhouses are still most feasible a majority of the time). These areas have strong demand for moderately priced for-sale homes and a relatively strong rental market, with many lots between 15,000 square feet and an acre, some of which could be feasible for redevelopment.

In the southwest (**Northridge Woods and Bull Mountain** subareas), 3 to 4 percent of lots included in the analysis were identified as having potential for middle housing development, with potential for townhouses on a number of the very large lots that remain in portions of these areas (though there are many reasons why such development may not occur despite being identified as financially feasible).

### Other Considerations

Financial feasibility is an important factor in estimating the potential for middle housing development. However, there are also a range of other factors that affect how much and what types of middle housing are likely to be built. These include:

- **Property owner preference:** Redevelopment of developed properties typically happens when a property is sold to a new owner. Even for infill (without demolition of the existing home) or conversion of homes to middle housing, which are outside the scope of this analysis, major changes are more likely upon sale of the property to a new owner who may buy it with the new development potential in mind. As a result, the pace of middle housing development within existing neighborhoods will be gradual, even where financial feasibility is strong.
- **Developer experience:** Developers, investors, homebuilders, lenders, and others involved in the development process will need to gain comfort with housing types that have seen little recent development in Washington County (triplexes, fourplexes, and cottage clusters in particular). This will likely slow production of these housing types in the near term.

- **Housing type preferences:** Roughly 80 percent of Metro-area residents prefer single-family detached housing.<sup>3</sup> To the extent that people have other alternatives within their desired price range (e.g., older or smaller detached homes, detached homes in lower-cost areas, etc.), this could reduce demand for middle housing. However, some people choose attached homes because they are more affordable, and some prefer new homes over older ones or are looking for certain home sizes or features that are not common in older homes. Housing preferences can also shift over time, which could expand demand for middle housing over the longer term.

## Equity Considerations

Overall, implementing HB 2001 supports equity by **making existing neighborhoods less exclusionary** and restrictive of smaller and attached housing types that tend to be lower cost—one of the key issues that HB 2001 was intended to address. In addition, allowing more housing (of any type) to be built in desirable locations helps **prevent supply shortages from driving up prices**. In addition, **middle housing tends to be less expensive than larger detached homes**: based on 2020 sales data, newly constructed middle housing in Washington County is estimated to sell for between \$220,000 (for a small two-bedroom condominium unit) and \$460,000 (for a larger three-bedroom townhouse), depending on housing type, unit size, and location, while new single-family detached homes are likely to sell for between \$390,000 (for small-lot detached housing) and \$700,000 or more (for larger detached homes on larger lots).

However, **middle housing alone will not solve affordability challenges for many households**—even the lower sales prices that are possible compared to new detached housing are still too high to be affordable to many households in the county. State law prohibits Washington County from *requiring* middle housing to be sold or rented at a particular rate, and the County has limited ability to address regional and national trends impacting housing costs. Furthermore, first-time homebuyers face other challenges to buying a home, including saving for a down payment, meeting mortgage requirements, and competing with buyers able to pay with cash. Still, some affordable housing providers (such as Habitat for Humanity, which focuses on affordable homeownership) may choose to develop middle housing. In addition, the County could consider code and financial incentives, as discussed below, to encourage development of affordable middle housing and to support affordable housing and homeownership opportunities more generally.

Another important equity consideration is displacement risk, primarily for renters in existing single-family homes that could be redeveloped. Displacement risk evaluation centers around renter households because—even after recent changes to state law providing greater protection for renters—renters are still much more vulnerable to changing market conditions and are subject to the decisions of the property owner about redevelopment, remodels, rent increases, etc. An analysis of assessor’s data for properties that are feasible for redevelopment with middle housing (excluding those that would be feasible to redevelop with additional single-family

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<sup>3</sup> Oregon Metro, Residential Preference Study 2014.

<https://www.oregonmetro.gov/sites/default/files/2014/09/02/ResidentialPreferenceStudy-FullReport.pdf>

homes today) found **less than 100 properties in the UUA where renters might be at risk of displacement due to redevelopment that would be newly financially feasible with implementation of HB 2001**. Nearly a third of these are located in the Heritage Baseline subarea discussed above, which has many manufactured homes; the next largest concentration is in Aloha, though only a fraction of a percent of the parcels there are rental homes that are potentially newly at risk. In both areas, existing demographics suggest residents are already vulnerable to housing market changes.

### Infrastructure Considerations

County staff sought input from Clean Water Services (CWS) and Tualatin Valley Water District (TVWD) regarding infrastructure considerations associated with the development potential identified in this analysis. TVWD did not express any concerns. CWS indicated interest in exploring potential stormwater and sanitary sewer infrastructure needs in North Bethany, depending on the extent of middle housing that might occur on areas that have not yet developed, as well as possible stormwater infrastructure issues in Aloha due to existing challenges with topography and soils. County staff is continuing to coordinate with staff from CWS regarding these concerns.

### Policy and Code Options and Considerations

The County is in the initial stages of evaluating how to update the development code to comply with HB 2001 and the corresponding administrative rules. It was not the intent of this project to conduct a thorough review of the Community Development Code (CDC) to identify all needed updates or recommend the best approach to address them. However, ECONorthwest was tasked with evaluating selected regulatory options and affordability strategies from the perspective of how they would affect development feasibility for middle housing.

### Regulatory Options

#### Existing Regulations that Likely Require Updates

The County must update regulations to allow middle housing types outright in districts that allow single-family detached housing, and must ensure middle housing is not held to certain existing code standards that would conflict with HB 2001 or its rules. Examples include the County's existing density and lot size standards, discretionary review processes, and minimum parking requirements. While these may continue to apply to other types of housing, they can't be applied to middle housing. This analysis did not consider the legal or feasibility implications of retaining existing regulations that conflict with HB 2001 minimum compliance.

Implications of changes to two existing regulations were more closely evaluated for their impact on middle housing development feasibility:

- **Land division restrictions in R-5:** Existing restrictions on land division in the R-5 land use district would preclude townhouses on lots under 14,000 square feet. Retaining these regulations may be difficult to justify under state regulations; however, the

overwhelming majority of these lots would not be financially feasible to redevelop with townhouses in any case.

**Street frontage improvement requirements:** The County currently requires street frontage improvements for a lot that will contain a detached house only as part of a land division (partition or subdivision). When a house is built on a lot that is not part of a land division, the County does not require such improvements. To comply with HB 2001, the County must treat a duplex on such a lot in the same way—it cannot require frontage improvements for a duplex if it does not require them for a single-family detached dwelling. The County can require other middle housing types to demonstrate that there is sufficient infrastructure (water, sewer, stormwater, and emergency access) and can require reasonable and proportionate mitigation of localized infrastructure constraints. However, it is not clear whether street frontage improvement requirements can be applied to middle housing types other than duplexes if those requirements do not apply to single-family detached housing. The cost of street improvements particularly impacts development on corner lots, where there is more frontage to improve, especially where the costs are borne by very few units.

There are a number of other existing development standards that may not be precluded by the state rules, but they could affect the ability to develop middle housing in an infill situation that should be reviewed in detail as part of the code drafting process, including setbacks required between different land use districts and outdoor yard area requirements.

#### Additional Policy Choices

There are several additional ways the County can use regulations as policy levers to influence outcomes within the context of HB 2001 implementation, depending on the intended policy direction or outcomes, including those listed below. The County may choose to consider additional regulatory options as part of the code writing process, depending on policy goals, provided that the regulations do not create unreasonable cost or delay.

#### Potential Limitations and Requirements

- **Design standards:** Design standards for middle housing are not required, but if applied, they generally cannot be more restrictive of middle housing than single-family detached housing, and they cannot scale with the number of units (e.g., requiring all units to have entrances facing the street vs. requiring one entrance facing the street). The code currently includes a few design standards for single-family housing. The County will need to consider whether to apply these to middle housing (with modifications to comply with state rules), adopt new clear and objective standards for middle housing, or not apply design standards to middle housing at all. Standards that align with those in the state’s Model Code for middle housing generally will not impose unreasonable costs on development and can prevent design issues that could generate opposition to middle housing.
- **Standards for townhouse development on large sites:** Townhouse development is likely to be more financially feasible than single-family detached development in many cases, and it could result in densities up to four times higher than allowed for single-

family detached housing in some land use districts. If there are concerns with the potential magnitude of townhouse development on large lots in lower-density residential districts, the County could potentially consider options to limit townhouse development on large lots in those land use designations, though this would require meeting additional requirements under state rules. While not specifically addressed in the rules, the County could also explore the possibility of requiring a mix of housing types as part of the land division process, while continuing to allow all middle housing types within that mix.

- **Cottage cluster unit size and development standards:** Jurisdictions' options to regulate cottage clusters are somewhat limited and are primarily related to unit size, open space requirements, and site design. Washington County has existing standards applicable only in North Bethany that will need to be revised; the County will need to decide what standards to apply to the rest of the urban unincorporated area. The core question is whether to structure the standards the County can control for cottage clusters to incentivize or require smaller units, to maximize flexibility and development potential, and/or to emphasize design. Larger "cottage" units, more similar in size to typical detached units, would potentially increase the economic feasibility of this type of middle housing compared to detached housing and townhouses, but townhouses would continue to be at least as financially feasible as larger cottage units in many cases.

The County is also separately considering how to regulate middle housing in undeveloped portions of North Bethany since there are provisions allowing jurisdictions to restrict middle housing on initial build-out of master planned areas if desired, though it is not yet clear if those provisions will apply to North Bethany.

#### Potential Affordability Incentives

- **Incentives for regulated affordable housing units:** While jurisdictions cannot impose affordability requirements on middle housing, they can offer incentives for developments that include affordable units. The County could consider revising an existing discretionary density bonus for affordable housing to apply to regulated affordable middle housing, ideally outside a discretionary process. This could mean allowing up to six units on lots that would otherwise allow a fourplex. This would reduce permitting costs relative to the discretionary process and spread the cost of land and other fixed costs across more units, allowing available subsidies to go further. The County could also further reduce parking requirements for regulated affordable middle housing to complement the density bonus, as the land required for parking can be prohibitive for higher densities on small sites.
- **Incentives for smaller units:** Smaller units tend to be lower cost, but if they are competing with larger units at the same density, ECONorthwest's analysis shows that they are less likely to be financially feasible. There are several incentives the County could consider for development with smaller units, including allowing plexes on smaller lots, allowing additional units (e.g., up to a sixplex) on a single lot, and reducing parking requirements.

- **Housing preservation strategies:** If the County advances strategies to protect residents of manufactured housing parks (through a separate process, as noted above), that may address some of the displacement risk that could be associated with future middle housing development. The County could also consider additional incentives to improve and preserve existing homes. The Office of Community Development administers the County’s existing home preservation and rehabilitation programs, and provides funding and support for nonprofit and community-based organizations doing similar work. We recommend the County consider this option in greater detail as part of a broader evaluation of measures to support housing affordability and stability generally.

## Financial Strategies

The County is also required to consider some financial strategies to increase affordability of middle housing as part of compliance with HB 2001. We recommend the County consider the following options in greater detail as part of a broader evaluation of measures to support housing affordability generally.

- Offer additional **property tax exemptions**<sup>4</sup> for affordable and/or rental middle housing development.
- Offer **TDT waivers or reductions** for regulated affordable middle housing development, and/or change TDT rate structures to incentivize smaller middle housing units (e.g., by scaling fees based on unit size relative to a typical single-family detached home).
- Implement a **construction excise tax (CET)** to generate funding for affordable housing, including affordable middle housing. A CET is a tax imposed on new development and expansions as a percentage of the permit value. It can be applied to commercial and industrial development and/or to residential development (affordable housing and certain public and institutional uses are exempt). Funds are used primarily for local housing programs.

Additional discussion of the rationale and trade-offs associated with these strategies is included on page **Error! Bookmark not defined.** of the memorandum.

## Conclusions and Next Steps

There is potential for middle housing development throughout the urban unincorporated area, though it is not evenly distributed and is generally limited to larger lots (over about 14,000 square feet). If the County chooses to implement HB 2001 through a minimum compliance approach with few additional standards, ownership housing with relatively larger units compared to other middle housing – particularly townhouses – would be the most likely outcome in most affected areas of the County. These may have higher sales prices than other middle housing types, but they will generally still be less expensive than most new detached housing. They can expand ownership opportunities for middle-income households in high-cost

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<sup>4</sup> Rental property affordable to households earning 60 percent MFI and under may currently be eligible for property tax exemption through the existing program administered by the Department of Housing Services: <https://www.co.washington.or.us/Housing/HousingDevelopment/property-tax-exemption.cfm>

areas and help keep housing shortages from driving up costs. However, to further support lower-cost middle housing and address housing equity considerations would require a combination of code incentives, financial incentives, and programs to support equitable homeownership and affordable housing opportunities. While displacement risks are estimated to be relatively low as a result of middle housing redevelopment potential, the County should prioritize displacement prevention efforts for residents of manufactured housing who do not own the land under their home and should consider expanding efforts to improve and preserve existing homes.

In developing regulations for middle housing, ECONorthwest recommends that the County consider and seek feedback from the community regarding the trade-offs of imposing simple design standards, allowing townhouse development on all lot sizes, establishing layout and design standards for cottage cluster housing, and requiring improvements to streets fronting middle housing development. This report and ECONorthwest's analysis are interim steps in the process of considering how to implement HB 2001 in Washington County's urban unincorporated areas. The next step will be to do a more comprehensive evaluation of needed code amendments and expand community engagement related to the available options for implementation.