

Accessory Dwelling Units – Introductory Brief

This brief begins with highlights and main points taken from a review of recent literature and research on the topic of Accessory Dwelling Units before providing more detailed analysis on the highlighted topics. A companion document called, “Exploring ADU Regulation Discussion Points and State Practices,” examines regulations in nine states that have passed statewide legislation broadly allowing ADUs and is also available on the Virginia Housing Commission website. It will be updated as state laws evolve.

Highlights Based on Recent Research and Literature

- Accessory Dwelling Unit (ADU) and Affordable Dwelling Unit are two separate terms used in different policies. An accessory dwelling unit does not have to be affordable and is not required to be in any state that has passed statewide legislation broadly permitting ADUs.
- ADUs increase housing stock in neighborhoods previously limited to standalone single-family homes and provide lower-cost options for renters in that area compared to traditional single-family homes. Many believe increasing stock may eventually lead to more affordable homes as higher inventory decreases market competition.
- The rate of ADUs constructed often increases in states and localities that have implemented legislation or ordinances broadly permitting ADU construction compared to years prior to enacting those changes.
- The increase in construction of ADUs in states that have implemented statewide legislation is varied across localities. This suggests location and other local factors separate from permitting are determinants in ADU construction rates.
- The literature shows generating income is the largest motivating factor among homeowners interested in building an ADU.
- The existing literature and research lacks evidence to support the claim that ADUs are effective at producing housing stock for low-income households and little evidence of ADUs being affordable for those at or below the area median income. Much of the literature concludes that ADU affordability is often limited to tenants who are related to the property owner.
- To address the lack of affordable ADUs, many localities throughout the country are crafting policies and programs to encourage or ensure affordability to those making less than the area median income.
- There is more research that shows ADUs typically rent at above market rates and are not a lower-cost alternative to other types of rental units nearby. Factors like location, size, privacy, familiarity with the tenant, and age of the constructed unit factor into rental pricing. Rents vary widely in different localities.
- Most of the research studied concluded that ADUs are more commonly built in affluent communities compared to more low-or-moderate- income communities. ADUs as a function for generating equity and wealth for low-or moderate- income communities is not supported by the breadth of current research. Many states and localities are creating pilot programs, often construction grants, to bridge this gap.
- Financing an ADU is challenging and usually done through taking advantage of home equity or through substantial cash savings, making financing easier for homeowners with higher incomes or home values. Cost is a significant barrier to entry for homeowners interested in constructing ADUs.
- Across all levels of income, most ADUs are used to provide affordable housing rather than an accessory to the primary dwelling, but higher-income households are more likely than other households to use an ADU for a non-housing function.
- A commonly provided reason among homeowners as to why they do not want to rent an ADU to a non-family member is a reluctance to house a “stranger.” This suggests that once an ADU is vacated by a familial tenant, it is not guaranteed to enter the rental market.
- ADUs, like all smaller homes, have less of an environmental impact than the average single-family home and are considered a “green,” housing option while the existing inventory of smaller homes remains scarce.

Definitions: Affordable Dwelling Unit vs. Accessory Dwelling Unit

In this policy area there is often confusion over what constitutes an ADU. Many getting affordable dwelling units confused with accessory dwelling units. An affordable dwelling unit is a unit of affordable housing that meets established affordability parameters. An accessory dwelling unit does not have to be affordable; it is a smaller housing unit that is an *accessory* to a primary single-family dwelling unit. This section will expand further on these definitions:

According to the Code of Virginia, "Affordable" means, as a guideline, housing that is affordable to households with incomes at or below the area median income, provided that the occupant pays no more than 30 percent of their gross income for gross housing costs, including utilities.

ADU in this discussion is used as an acronym for accessory dwelling unit. An accessory dwelling unit is an accessory to a single-family primary dwelling unit on the same property. They can be attached or detached to the primary dwelling unit and are most often considered a separate living space. An accessory dwelling unit does not have to be affordable.

In Virginia SB 305, 2024, ADU is defined as an independent dwelling unit on a residential dwelling lot with its own living, bathroom, and kitchen space.

Evidence Shows ADUs Increase Housing Stock in Neighborhoods with Fewer Rental Options, but are Not Necessarily Rented at Below-Market Rates or Attainable for Lower-Income Households

While ADUs Have Been Proven to Increase Much Needed Housing Stock, they are Not Found to be Affordable for Lower-Income Households.

Despite commonly made assertions in ADU policy discussions, guaranteed affordability, or below-market rental rates of ADUs is not supported by a lot of data. ADUs increase housing stock in areas more commonly limited to single-family zoning and provide more affordable rental options in those areas compared to renting a traditional single-family home. They are not typically a lower-cost alternative to other types of rental units nearby. The Virginia Department of Housing and Community Development (DHCD) Published a report in 2021 called, "State of Market and Local Policy: Accessory Dwelling Units in the Commonwealth of Virginia," that found there lacks evidence to support the claim that ADUs increase the stock of affordable housing to low-income households.

In terms of impacting affordability, it is commonly asserted that ADUs have the potential to influence affordability as they increase the overall market supply of housing options. Many industry experts theorize that higher inventory will reduce market pressure and increase affordability among all housing types. Most ADU regulations are too new to properly study this type of long-term impact on the current market.

According to *AARP* market-rate rents for ADUs tend to be slightly more than for similarly sized apartments, but that is still considered an affordable rental choice in single-family neighborhoods that typically contain few one-bedroom housing options.

UCLA conducted a survey in 2020 after California's statewide ADU law was changed in 2017. The survey conducted rental cost analysis in Los Angeles and found that for housing tenants with no relation to the landlord, the average rent for an ADU was higher than the average rent for a similarly sized apartment. It concluded that rental rates for ADUs are higher on average than other rental housing across the city. While Los Angeles is broadly considered a success story in terms of the number of ADUs constructed after the 2017 changes, it is important to highlight that while more housing was produced, this housing is not necessarily considered affordable to lower-income households who typically need below-market rates.

The Rental Cost of an ADU is Unpredictable but Most Determined by Relationship with the Tenant, Location, and Size of the ADU. Affordable Rent is Mostly Provided to Acquaintances and Family Members.

The rental cost of ADUs is determined by each individual property owner, which makes predicting affordability unreliable. This is why differentiating affordable dwelling units from accessory dwelling units is important when examining this policy area.

Much of the literature finds that ADUs can provide affordable housing stock when rented to acquaintances and family members, but that same affordability does not commonly exist outside those circumstances. Research suggests that the key determinant of rental price is the relationship between tenant and owner.

The affordability of an ADU is unpredictable as rents are offered in a wide range of dollar amounts. In the states that have passed statewide ADU permitting legislation, there are no required provisions concerning the affordability of an ADU. The rental price of an ADU is determined by the owner of the property usually by taking factors such as location, square footage, and familiarity with the tenant into account. When browsing websites dedicated to providing advice on constructing an ADU, most recommend to potential ADU owners that they price their ADU above local apartment rates due to perceived positive factors like privacy and outdoor space.

There is Limited Research Finding ADUs Rent at Below-Market Rates

A survey conducted in 2017 by the Turner Center at UC Berkeley stated that 58% of ADUs surveyed in Portland, Seattle, and Vancouver rented for below market-rates, with 40% of those units occupied by family or friends. The Turner Center also concluded that overall affordability varies significantly by locality. This study partially contradicts a larger number of surveys and studies pointing to ADUs not directly adding to the supply of below-market rate rental housing but supports the idea that rental pricing of ADUs is mostly unpredictable. It also may be more representative of a different market with lower home prices and rental rates than today's housing market. However, most studies also conclude that ADUs successfully add inventory to the market in neighborhoods with few other rental options. The amount of inventory varies significantly among localities within the same state.

Many Localities and Research Groups Find Additional Intervention May Be Necessary to Generate Affordable ADUs

Research conducted by the Brookings Institute puts forth policy suggestions for “affordable ADUs,” such as rental subsidies, and voucher programs targeted to older adults. However, one of the strongest selling points of constructing ADUs, generating income for the homeowner, is a challenge when it comes to owners accepting the restrictions that often come with housing subsidies. Brookings suggests that newly built ADUs will require substantial subsidies for renters making less than 80% of area medium income.

California created a \$100 million grant program for low-and moderate-income households to cover up to \$40,000 in planning and permitting costs. The program quickly reached capacity and is expected to receive an additional \$50 million this fiscal year. That money is pending as the state financing agency investigates other sources of funding for the program. The additional \$50 million may depend on the support of private-sector resources. Many localities in California have developed their own pilot programs to subsidize the construction of ADUs separate from the state. Passaic, New Jersey allows ADUs with 20-year deed restrictions to maintain affordability. Vermont created a grant program that allows up to \$50,000 for the creation of Accessory Dwelling Units.

The report published by the Virginia DHCD identified several local programs in other states that seek to encourage and preserve the affordability of ADUs for households making below the area median income. However, these programs and imposed covenants concerning ADU affordability are rare.

ADUs are Commonly Built in More Affluent Communities with More Financing Options than Low- or Moderate-Income Communities

ADUs Generate More Wealth for the Homeowner. However, Research Points to ADU Construction Being Concentrated in More Affluent Communities, Most Likely Due to the Cost of Construction. ADU Generated Wealth Building Among Lower-Incomes is Rare

While constructing an ADU might be out of reach for households not in a high-income bracket, these findings support the conclusion that ADUs are increasing housing stock in neighborhoods zoned exclusively for single-family homes. ADUs as a function for generating equity and wealth for low-or moderate- income communities is not supported by the breadth of current research.

The Turner Center at UC Berkely's research concluded that ADUs are generally built in affluent communities and surmised that ADUs are not accomplishing the goal of building wealth and equity as well as policymakers intended. Research points to ADUs benefiting wealthier homeowners than low- and medium income homeowners who can't afford to construct an ADU or navigate the complicated building process.

According to the National Association of Realtors, properties in the largest metros with ADUs are priced an average of 35% higher than homes without one. This demonstrates an ADUs ability to generate wealth for participating households and promotes ADUs as a potential investment choice.

Stronger Financing Options are Typically More Available to Higher-Income Households

Households with higher incomes and home values are more able to take advantage of their home's equity to finance an ADU. Additionally, a homeowner can't obtain a mortgage for an ADU like those for single-family homes. The report published by the Virginia DCHD concluded while ADUs can bring additional income to homeowners, building an ADU has higher financial barriers compared to building a typical family home.

FreddieMac Consumer Research found ADUs are more likely to be financed by leveraging personal savings and later collecting future rent from tenants. Turner Center at UC Berkely research points to ADUs being financed mostly by cash savings or taking out equity from your home, and both of those are options more common among affluent homeowners.

The current market lacks lending products specifically designed for ADUs, making the barrier to entry more difficult for lower-income households. Construction loans are an ADU financing option, but often come with 20% or more downpayments, difficult approval processes, and large balances due once construction is completed.

The Cost of Building an ADU Depends on a Variety of Factors, but Can be Several Hundred Thousand Dollars

The cost of building an ADU ranges from around \$120,000 to over \$400,000 depending on factors like square footage and whether an ADU is attached or detached. According to the National Association of Realtors, the average cost of an ADU is \$180,000 but can be much higher depending on where you live. Typically, constructing an attached ADU, like converting a garage, costs less than a detached ADU.

Where ADUs Are Built, Job Rich Areas and Wealthier Neighborhoods - Examples from California

San Francisco has allowed ADUs since 2014. Data reported by the San Francisco chronicle found that the 622 units built from 2014-2022 were in the city's wealthier neighborhoods.

A study conducted on the results of California's ADU policy showed that ADUs are more likely to be built in coastal counties in job-rich areas. A separate study found that ADUs in Los Angeles (LA) were more likely to be built close to commercial districts, light rail stations, and educational institutions than LA's higher-income areas. Research provided by the National Home Builders Association found that being within walking instance of amenities such as transit, retail, and food services is more important than lot size to tenants.

ADUs Can Be Used for a Variety of Purposes Outside of Housing, but Most are Used to Provide Housing

Research Shows Most ADUs are Used for Housing Across All Incomes, but Higher Incomes are less Likely to Use ADUs to Provide Housing than Other Income Brackets

Not all homeowners who build ADUs do so to provide housing. Many use their ADUs to function as an extension of the primary residence as an office, guest room, or additional hosting space. However, most of the research finds that more ADU owners construct the unit to provide housing than those who do not. The UCLA survey of Los Angeles homeowners who constructed a permitted ADU on their property found that 67% of ADU owners use their ADUs for housing. However, that percentage changes for those in the top household income category. The survey found that a third of households making over \$150,000 use an ADU as a non-residential extension of their primary dwelling.

Creating Housing for Family Members is a Commonly Given Motivation for Constructing an ADU, but Research Shows Gaining Additional Income is the Most Common Motivation for Building ADUs.

Several studies have found that these homeowners who build ADUs to function as more housing are typically driven by either the need to house a relative, caregiver, or friend, or a desire to generate more income. While the desire to house family members is common, the literature on ADUs points to generating income as the most substantial motivation when a homeowner is considering building an ADU.

Reluctancy to House Strangers May Prevent ADUs from Joining the Rental Market Once Vacated

UCLA also found that for participants who do not use their ADU as a residence for strangers or housing in general, the most common reason provided was that they do not want to share a space with strangers. This is a common sentiment provided throughout ADU policy discussions. This suggests that if a family member or caregiver moves out of the unit, it will not automatically join the rental market.

Additional ADU Discussion Topics

ADUs Used as Short-Term Rentals Could Lessen the Intended Impact on the Availability of Affordable Housing

According to reporting done by ShelterForce in 2022, a publication centered on affordable housing topics, officials in Tampa, Florida anecdotally claimed that most ADUs they inspected and assumed would be used to house family members were being turned into short term rental properties. To mitigate the use of ADUs as short-term rentals in favor of ADUs being used to increase housing stock, many localities have prevented the use of ADUs as short-term rentals. In the states that have passed legislation broadly allowing ADUs, the various laws all provide localities with the ability to restrict and regulate the use of ADUs as short-term rentals.

ADUs Have Less of a Negative Environmental Impact Compared to Standard Single-Family Homes

Evidence shows that size is one of the greatest contributors to the environmental impact of new housing. Depending on the size of ADUs, which typically range between 600 and 1,200 square feet, they are less likely to have large environmental footprints. They are often marketed as a "green," housing option by builders and

environmental advocates. ADUs also require fewer resources to transport, build, and maintain compared to traditional homes and use less energy for heating and cooling. The Sightline Institute reported that ADUs cut lifetime CO2 emissions by as much as 40% when compared with medium sized single-family homes. The same Sightline reporting stated that only 3% of new single-family homes have been under 1,000 square feet since 1956, making smaller homes, which have less of an environmental impact, scarce. A report provided by the National Association of Homebuilders found that previously long-held resistance to smaller lot sizes is being reconsidered, which may indicate more potential interest in constructing smaller units like ADUs.

Renting a Detached ADU to a Non-Family Member Could Require Landlord Insurance Which Could Serve as an Additional Cost Barrier to Using a Detached ADU to Provide Housing

If a tenant of a detached ADU is a relative, some insurance carriers cover the ADU structure under the existing homeowner’s insurance. However, those renting out a detached unit to a non-family member may be required to purchase landlord insurance. The Insurance Information Institute estimates that a landlord insurance policy costs around 25% more than a standard homeowners policy for the same type of unit. Detached ADUs typically cost more than internal or attached ADUs, and this added insurance could further impact a household’s budget and serve as an additional cost barrier to entry. A homeowner may not be required to purchase landlord insurance for an ADU but is more likely to be required to do so if the ADU is financed or mortgage to protect the lender’s investment.

Results of Statewide ADU Permitting – ADU Construction Increases in States with Laws Broadly Permitting of ADUs, but Results Vary Across Localities

Across the country, it appears the number of ADUs constructed increased in states and localities that have implemented legislation or ordinances broadly permitting ADU construction compared to prior to enacting those changes. However, it is important to note that there has been little detailed *statewide* data or analysis conducted for or by states that have implemented statewide legislation, other than in California. Most reporting has been done on a local level. The National Association of Home Builders reported that during the first quarter of 2019 across the U.S., 20% of home renovation projects included converting an existing space to an ADU.

The Results of Broad Statewide ADU Permitting Is Varied Throughout Localities Which Suggests Location and Other Local Factors Separate from Permitting are Significant Determinants in ADU Construction Rates.

In California, one estimate shows that roughly 1 in 7 new home constructions are ADUs. While all studied states are experiencing increases in the number of ADUs constructed, the numbers vary widely even among states that have passed similar provisions in their ADU bills. Since California’s ADU legislation was passed in 2017, the bulk of studies examining the impact of statewide legislation investigate California rather than states that have enacted statewide legislation in more recent years.

A study conducted on the results of California's ADU policy showed that ADUs are more likely to be built in coastal counties in job-rich areas. The study also concluded that ADU permitting varies widely by region and will likely have different effects across a state when implemented (Marantz, Elmendorf, and Kim). The figure below demonstrates how different cities permitted ADUs at different rates after California's 2017 legislation was enacted.

California's 2017 ADU reform boosted permit applications in several cities.

City	2015	2016	2017
Los Angeles	299	257	3,818
Long Beach	0	1	42
Oakland	33	99	247
Sacramento	17	28	34
San Diego	16	17	64
San Francisco*	41	384	593
San Jose	28	45	166

Source: Temer Center for Housing Innovation and City of Los Angeles

*San Francisco data through Q3 2017



Conclusion

While ADUs increase housing stock in neighborhoods with zoning restrictions, the research points to ADUs being unlikely to help increase the stock of affordable housing. Market rents for ADUs tend to be higher compared to similar housing structures. With individual owners able to determine the rental costs of their ADUs, affordability is not guaranteed and mostly limited to owner acquaintances and family members. Additional intervention is often seen as necessary to generate affordable ADUs and many localities and a few states are implementing grant programs to incentivize affordable ADU construction.

ADUs are also unlikely to generate wealth for homeowners outside of affluent communities. The cost of constructing an ADU is high, and financing is difficult without large cash savings or significant equity. This prevents non-wealthy homeowners from constructing an ADU and generating the extra wealth often provided through rental income and an increase in property value.

ADU generated wealth is the strongest motivating factor among homeowners who construct ADUs, and housing family and friends is the second strongest motivating factor. Likely due to those motivations, most ADUs are used for housing rather than as an extension of the primary dwelling unit. Research supports ADUs as a function for increasing housing stock in neighborhoods with few options outside of single-family dwellings. The size of that stock increase significantly varies depending on local factors.

While ADUs increase housing supply, the research does not support ADUs as a solution to increase affordable housing and impacts to local housing stock vary in states that have implemented statewide legislation broadly allowing the construction of ADUs.

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