

# ADUs, SB9 and emerging opportunities for gentle density in Petaluma's neighborhoods

Chris Larson

Know Before You Grow

August 9, 2023

[chris.larson@chilenovalley.net](mailto:chris.larson@chilenovalley.net)

# Overview

- Overview of ADU and SB9 laws, trends
- Where can these new laws drive housing, and what are the limitations?
- How do these projects work here in Petaluma?
- Example projects
- How could we accelerate these trends in Petaluma? (discussion)

# ADUs and SB9 defined

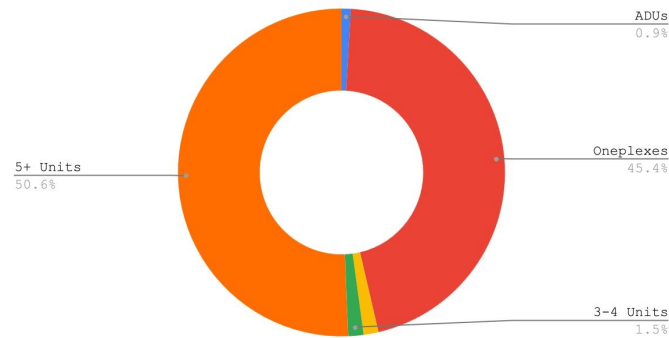
- ADUs:
  - Allowed in all residential zones (inc multifamily) as well as mixed-use zones
  - No owner occupancy requirements until 2025 (possibly never)
  - Cities must allow ADUs up to 800 ft<sup>2</sup> with no min lot size, >4' setbacks, no FAR/lot coverage limits
  - No parking requirements, existing parking can be converted into ADU
  - Impact fees waived <750 ft<sup>2</sup>, reduced between 750-1200 ft<sup>2</sup>
  - Does not count towards allowable density; must be approved even if lot is above allowable density/legal non-conforming
  - Allowed in historic districts, Petaluma has created objective design standards for ADUs in hist. districts; CC&Rs are overridden everywhere
  - <https://www.hcd.ca.gov/sites/default/files/2022-07/ADUHandbookUpdate.pdf>
- SB9:
  - Allowed in R1/R2 zones only
  - Two provisions: (1) two-way ministerial lot split (*owner occupied only*), (2) up to two primary units
  - Lot can be split, and then each new lot can have up to two primary units or one primary + one ADU; if no SB9 lot split, then two primary + ADU
  - Cities must allow SB9 dwellings up to 800 ft<sup>2</sup>, maximum 4' rear and side setbacks
  - Can be denied on health & safety findings; not allowed on environmentally sensitive sites, hazard zones, historic districts
  - Anti-displacement measures: no Ellis Act evictions, rent controlled units, tenant occupied in past 3 years, or deed-restricted affordable housing
  - <https://www.hcd.ca.gov/docs/planning-and-community-development/sb9factsheet.pdf>
- Commonalities:
  - Ministerial approval, no design review, no conditions of approval, no requirements for public improvements/dedications

# State Policy, Local Results

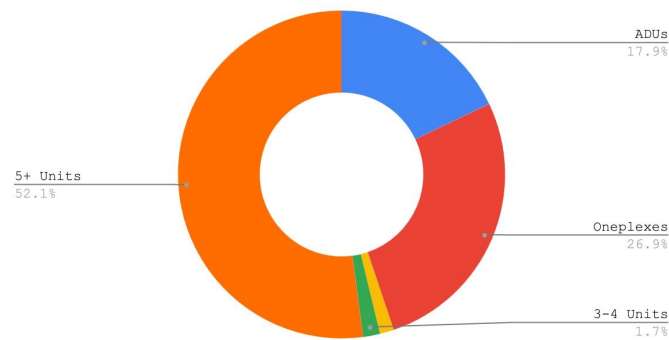
- State law trends: preemption, don't touch CEQA, reforms start small and build incrementally, mitigate greed/remain homeowner centric, reduce parking minimums, factor transit proximity
- What has made ADU successful:
  - Discretionary vs. ministerial approvals (key 2016 reform); reduced impact fees
  - Other key limitations relaxed: setbacks, sprinklers, impact fees, sewer, add density even to 'legal nonconforming', overriding CC&Rs (critical for eastside projects), overriding other local govt limitations (e.g. size, affordability requirements, landscaping, design review)
  - Current legislation = tactical improvements focused on project economics: prohibition on owner-occupancy requirements (AB 976), separate conveyance (AB 1033), no sprinklers < 500 sf, (AB 42), relaxed FAR (SB 294)
- Will SB9 follow ADU law?
  - ADU law tweaked 17 times since 2016! Already seeing SB9 clean-up bills (SB 450)
- <https://turnercenter.berkeley.edu/research-and-policy/2023-legislative-session-preview/>

# Seven Years of ADU Reform = 20% of California Housing Starts

Typologies as a % of all units produced in California, 2013



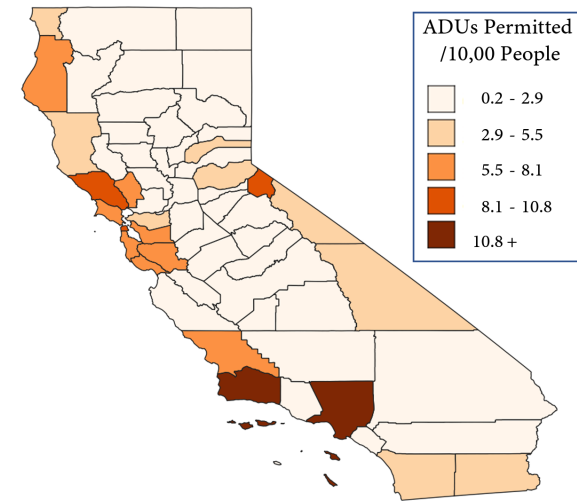
Typologies as a % of all units produced in California, 2022



When "affordable" housing is running \$450K to \$1M (!) per unit, ADUs are averaging \$150K to \$600K per unit in the Bay Area! Median ADU rent in Bay Area = \$2,000/month

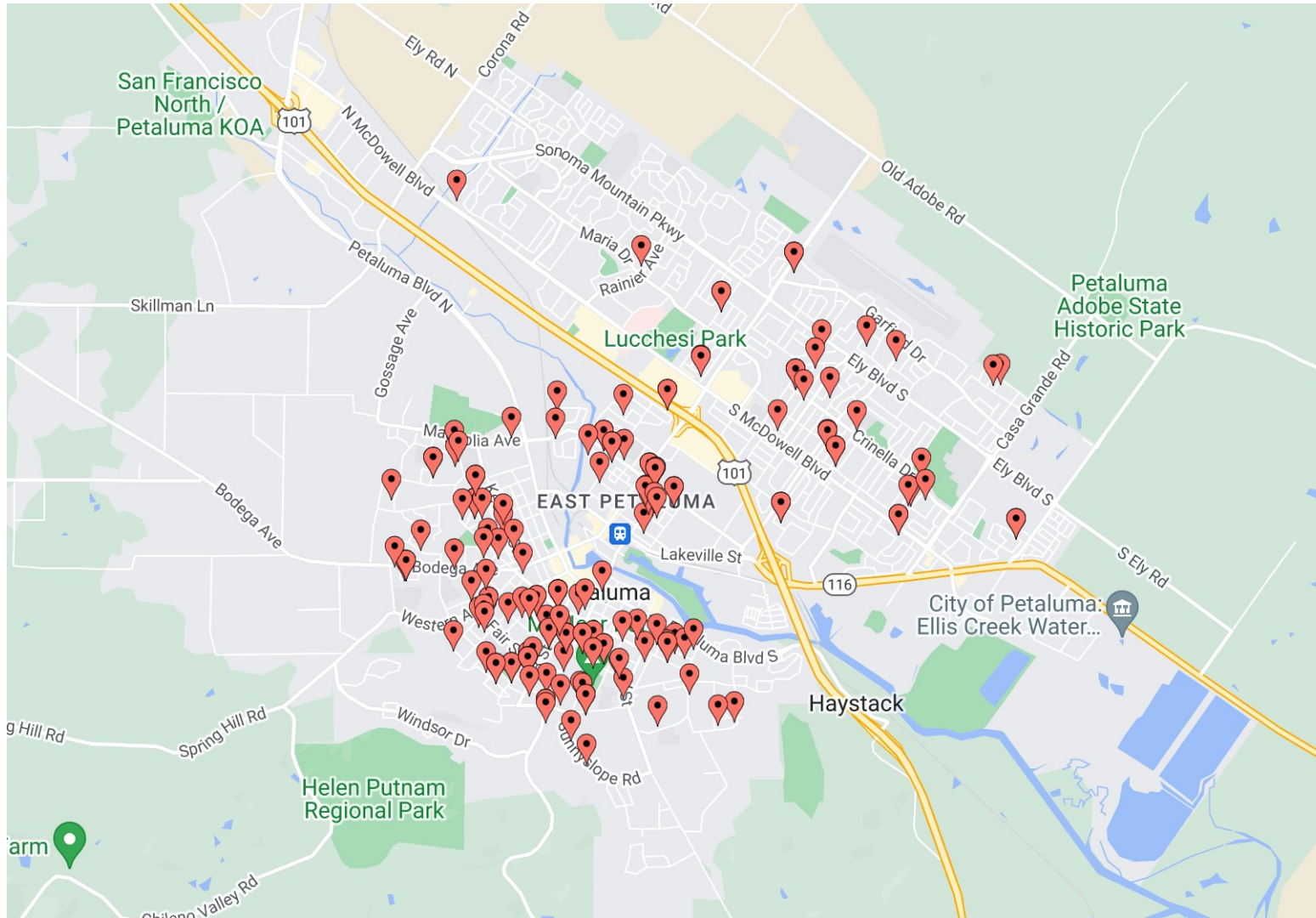
Permitting tripled between 2018-2019 from 6K to 16K, concentrated in LA, Bay Area, SD, mostly in high home value/high rent neighborhoods.

ADU Permits / 10,000 People - Counties (2018-2019)



Source: Calculated by the authors from Annual Production Report data (California Department of Housing and Community Development) and 2018 American Community Survey data (U.S. Bureau of the Census).

# Petaluma City ADU Completions 2018-2022



- Most ADUs in older/core westside, midtown which are generally 4,000-6,000 ft<sup>2</sup> lots (westside), 4,000-10,000 ft<sup>2</sup> lots (midtown)
- Represented 162 units of new housing delivered during this period with no expansion of Petaluma's urban footprint
- Density in affluent neighborhoods, presumably limited displacement

# Opportunities Revealed

- Before ADU & SB9, limited to 'dwelling group' or minor subdivisions
- ADU & SB9 dramatically expand project feasibility: (1) reduced setbacks, (2) reduced impact fees (ADUs), (3) ministerial approval, (4) no density impact
- Implications:
  - Feasible on most residential parcels in Petaluma
  - Supercharges 'stacked' approaches: (1) better economics for minor subdivisions, (2) SB9 lot split + greater density on the two resulting parcels, (3) if enough units, moves into density bonus feasibility
  - Adding density to already affluent areas, does not appear to drive displacement
- Benefits: intergenerational housing, good unit mix opportunities, add density in walkable neighborhoods, limited impact on infrastructure

# Applied locally in Petaluma

- Most projects are homeowner driven; robust modular/turn-key ADU industry + many locally talented ADU architects & builders
- Investor-owned projects happening, especially in Midtown
- Lot of activity on Westside & Midtown. Why? Well-capitalized homeowners, attractive to investors b/c good return on higher rents in these areas, suitable lot configurations
- Eastside: no vehicle access to rear lot areas, irregular lot shapes ('wedges' in cul-de-sacs), but still many opportunities
- Common project types: cottages, over-garage, attached, corner lots





Westside: 3,500-5,000 ft<sup>2</sup> lots, alley access, 19th century street grid, garage often accessed by alley or no garage, some large under-developed lots



Midtown: 4,000-8,000+ ft<sup>2</sup> lots (some already split), many very narrow (<50' width) and deep (>150' depth), some alleys, early 20th century st. grid, garages in rear yard, many large under-developed lots



Eastside: 5,000-7,000 ft<sup>2</sup> lots, often wide, not deep, mid-century cul-de-sac layouts, irregular shaped lots, garage attached, no rear yard vehicle access, consistent development patterns (few large lots)

# Costs & Returns

- Simple rules of thumb:
  - Rents: Maybe \$2.50-3.50/sf, so about \$1000 (studio) to \$2400 (two bed); garages rented separately (\$300)
  - Construction: \$300-500/sf; small units = more per ft<sup>2</sup> (many fixed costs)
  - Simple annual return: 5-12% on cost (plus appreciation, tax benefits!)
  - Until recently, very attractive to build ADU, then re-fi (get >100% of cost back)
  - 1-4 units = residential, not commercial, better loan terms: rate, tenor, terms, LTV
- Big ticket items:
  - Fire sprinklers: cost of sprinkler system PLUS water meters, encroachment
  - Sewer laterals, especially on deep lots where lift pumps may be required
  - Impact fees (especially with SB9)

# Impact Fees

|                       | 750 square foot dwelling (2br) |                 | 1200 square foot dwelling (3br) |                  |
|-----------------------|--------------------------------|-----------------|---------------------------------|------------------|
|                       | SFR / SB9                      | ADU             | SFR / SB9                       | ADU              |
| City Facilities       | \$ 7,551                       | \$ -            | \$ 7,551                        | \$ 2,590         |
| Open Space            | \$ 531                         | \$ -            | \$ 531                          | \$ 182           |
| Park Land Acquisition | \$ 2,259                       | \$ -            | \$ 2,259                        | \$ 775           |
| Park Land Development | \$ 7,472                       | \$ -            | \$ 7,472                        | \$ 2,562         |
| Traffic               | \$ 18,989                      |                 | \$ 18,989                       | \$ 5,264         |
| Wastewater            | \$ 10,365                      | \$ -            | \$ 10,365                       | \$ 3,815         |
| Water Meter           | \$ 5,047                       | \$ 5,047        | \$ 5,047                        | \$ 5,047         |
| School                | \$ 3,060                       | \$ 3,060        | \$ 4,896                        | \$ 4,896         |
| <b>Total</b>          | <b>\$ 55,274</b>               | <b>\$ 8,107</b> | <b>\$ 57,110</b>                | <b>\$ 25,131</b> |
| <b>Fees per Sq Ft</b> | <b>\$ 73.70</b>                | <b>\$ 10.81</b> | <b>\$ 47.59</b>                 | <b>\$ 20.94</b>  |

# ADU/SB9 Development in Petaluma

- Construction costs same across town; land costs higher on Westside, but rents and appreciation meaningfully higher
- Return on quality: higher rents, tenant quality, re-fi dynamics, asset marketability, lower O&M
- Existing house: minimal fees for upgrade & expansion
- Build ADUs first (similar size as SB9 but lower fees, easier to permit)
- Garages are profitable – not for parking...everyone wants storage
- Small units are profitable – as much as 2x variation per ft<sup>2</sup>
- ‘Buy, rehab, refi’ strategy challenging at current mortgage rates
- Striking balance: better to trade on comps than cash flow

# Midtown ADU project (Payran Street)



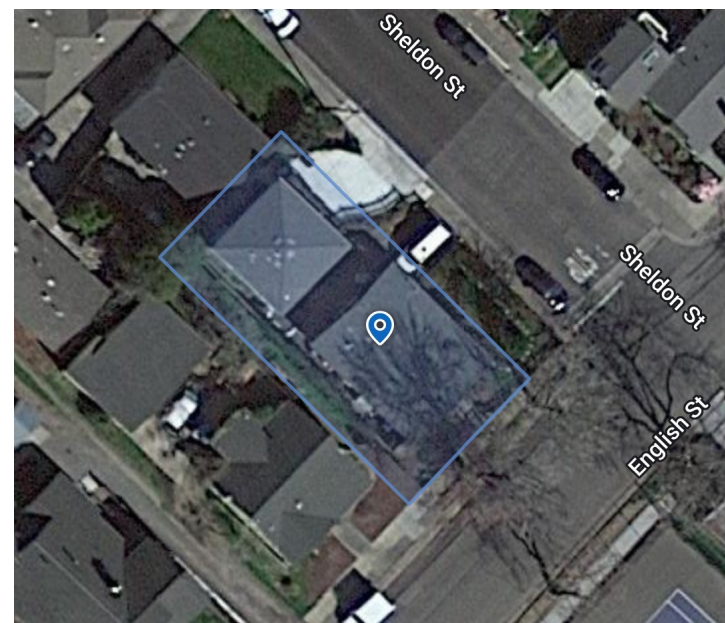
Purchased for \$705K in mid-2021  
Upgrade 1940s-era 2 bed/1 ba  
Add ~600 ft<sup>2</sup> ADU 1 bed/1ba  
Room for SB9 but not eligible (R3)  
Dwelling Group possibility  
Walk Score 89



# Westside ADU project (English Street/PHS)



Purchased for \$262K in 2013  
Upgrade 1940s-era 2/1 to 2/2  
Add 600 ft<sup>2</sup> ADU in 2018 (\$180K)  
Corner lot – separation benefits  
Walk Score 77



# Challenges & Limitations

- SB9 will need 5-10 years of 'clean up' to be as impactful as ADU is today: reduced impact fees, applicability in more zones, owner occupancy requirement, relaxing guaranteed min size (800 ft<sup>2</sup>)
  - Unlike many Bay Area cities, Petaluma is not currently seeking to restrict SB9 projects (thank you!!)
- ADU rules work well, but could be improved with greater height limits for true two-story structures (some reform in 2022), removing owner occupancy requirement for Junior ADUs (JADU), separate conveyance (affordability)

# Discussion

- What could accelerate use of ADU & SB9 pathways:
  - More developers!
  - Lower interest rates!
  - Incremental and tactical improvements for SB9
  - Align Dwelling Group code to SB9 concepts in GPU to allow use in extensive R3 neighborhoods in Midtown/Westside (rear yard setback issues)
  - City could adopt more favorable local rules for ADU (height limit, size)
  - Trends towards multi-modal transport supportive of smaller, denser housing
  - General Plan could expand density in R-zones, introduce by-right multifamily
  - Incentives to build ADUs into new tract home developments?
  - Apply political lessons of ADUs to GPU (people like gentle density, and we aren't limited to the state pre-emption laws)