The Report Committee for Kaileen McHugh
Certifies that this is the approved version of the following Report:

So You Want to Sell Your Backyard: An Analysis of Small-Scale Detached Condominium Developments in Austin, TX

APPROVED BY
SUPERVISING COMMITTEE:

Jacob Wegmann, Supervisor

Elizabeth Mueller

So You Want to Sell Your Backyard: An Analysis of Small-Scale Detached Condominium Developments in Austin, TX

by

Kaileen McHugh

Report

Presented to the Faculty of the Graduate School of

The University of Texas at Austin

in Partial Fulfillment

of the Requirements

for the Degree of

Master of Science in Community and Regional Planning

The University of Texas at Austin

December 2022

Acknowledgements

I would like to thank Dr. Jacob Wegmann, my primary reader, for his guidance in this process and positive support throughout graduate school. I would also like to thank my secondary reader, Dr. Elizabeth Mueller, for keeping me informed and curious about affordable housing issues in Austin. Many thanks to Josh Conrad for supporting me in the data aspect of the research, providing feedback, and sharing an interest in the topic. To all other CRP faculty and cohort peers: I am thankful we were able to persevere, work together, and continue our education during a global pandemic. Finally, I am especially grateful to my partner for always being there for me and supporting me on my educational endeavors.

Abstract

So You Want to Sell Your Backyard: An Analysis of Small-Scale Detached Condominium Developments in Austin, TX

Kaileen McHugh, M.S.C.R.P.

The University of Texas at Austin, 2022

Supervisor: Jacob Wegmann

This report explores small-scale detached condominium regimes in Central Texas. Small-scale refers to 2-unit properties, presented as single family homes with accessory dwelling units (ADUs). These units are commonly sold separately, circumventing the typical lot subdivision process. This is possible by utilizing the City of Austin's ADU regulations and the State of Texas condominium regulations. This report finds that this process has been largely pursued by for-profit developers, and that the resulting housing units are not affordable for the typical resident.

The report examines this process as a method for homeowners to pursue. Homeowners vulnerable to increased housing costs (those with low-, moderate-, and fixed-incomes) could build an ADU to sell (or sell an ownership interest in their land, to allow another entity to build and sell an ADU in their backyard) as a way to generate additional money and prevent displacement. A financial analysis finds that as the developer changes from "for-profit developer" to "non-profit developer" to "original homeowner as the developer" that the profits for the original homeowner increase; however, the regulatory and financial barriers also increase impacting the feasibility of the project.

Table of Contents

List of Tables 8

List of Figures 9

Chapter 1: Introduction 10

- Research Questions 11
- Report Outline 12
- Methodology 12
- Definitions 15

Chapter 2: Background Information 16

- Housing Market Conditions and Affordability in Austin 16
- Accessory Dwelling Units (ADUs) in Austin 21
- From Accessory Dwelling Units (ADUs) to Condominiums 27

Chapter 3: The Detached Condominium Landscape in Austin 29

- Condominium Regulations 29
- Types of Condominiums 30
- Data Analysis: All Detached Condominiums 32
- Data Analysis: Small-Scale Detached Condominiums 39

Chapter 4: Financial Analysis 52

- Scenario 1: For-Profit Developer as the Developer 55
- Scenario 2: Non-Profit Developer as the Developer 56
- Scenario 3: Original Homeowner as the Developer 58

Chapter 5: Conclusion 60

- Findings and Discussion 60
- Further Research 62

Final Reccomendations....62
Appendix: Financial Models....64
Scenario 1: For-Profit Developer....64
Scenario 2: Non-Profit Developer....64
Scenario 3: Original Homeowner as the Developer....66
Bibliography....68
Vita....70

List of Tables

Table 1: Median Home Prices and Median Family Income, Austin MSA (2011-2021) 18

Table 2: Detached Condominium Units by Zoning Type 33

Table 3: Condominium Units (Part of 2-Unit Detached Condominium Properties) by Zoning Type 40

Table 4: Affordability Analysis of Condominium Units (Part of 2-Unit Detached Condominium Properties) 50

Table 5: Financial Model for Development of an ADU Using a For-Profit Developer 55

Table 6: Financial Model for Development of an ADU Using a Non-Profit Developer 57

Table 7: Financial Model for Development of an ADU Using Original Homeowner as the Developer 58

List of Figures

Figure 1: Median Home Price, Austin MSA (2011-2021) 16

Figure 2: Types of ADUs 21

Figure 3: Example of an Alley Flat in Austin (1)..26

Figure 4: Example of an Alley Flat in Austin (2)..26

Figure 5: Detached Condominium Units and City of Austin Zoning Boundaries 35

Figure 6: Number of Detached Condominium Units by Percent Ownership in Common Areas within SF-6 Zoning...37

Figure 7: Detached Condominium Units by SF-6, PUD, and RR Zones 38

Figure 8: Detached Condominium Units by SF-3 Zoning 41

Figure 9: 2001 Willow Street, circa 2011 43

Figure 10: 2001 Willow Street, circa 2018 44

Figure 11: 2001 Willow Street, circa 2022 44

Figure 12: 2214 Garden Street, circa 2011..46

Figure 13: 2214 Garden Street, circa 2019..46

Figure 14: 2214 Garden Street, circa 2022..47

Figure 15: Condominium Units (Part of 2-Unit Detached Condominium Properties) by Year Built...48

Figure 16: Condominium Units (Part of 2-Unit Detached Condominium Properties) by TCAD Estimated Market Value...49

Chapter 1: Introduction

This report explores a housing model in Central Texas: building accessory dwelling units (ADUs) to sell without following the traditional lot subdivision process typically required at the municipal level. This topic remains largely unexplored in current literature, despite its impacts and potential in Austin.

In 2015, the City of Austin updated its ADU ordinance, which expanded the number of single-family properties that could build ADUs. Its intention was to help increase the housing stock and provide more affordable housing options to Austinites. With these updates many homeowners have been able to build ADUs on their properties to rent out, house family member or friends, or sell. However, it appears that building ADUs to sell has been largely pursued by developers. The ordinance change, along with state condominium regulations, has allowed developers to purchase single family homes, build ADUs on the properties (or demolish the original home and build two new units on the property still presenting as a single family home and ADU), and establish condominium regimes that allows the units to be sold to separate buyers[1].

This report does not attempt to determine which types of entities have been most vigorously pursuing the model of selling ADUs (a near impossible task), but rather examines how this model came to be and estimates the number of these units that currently exist. The report also explores this model as an affordable housing solution.

[1] It is important to note that local regulations make it difficult to split single family properties into multiple lots to sell separately, because they are typically too small to do so. The model of building ADUs to sell makes the development of two units possible on these lots, without technically separating the lot. The lot enters a condominium association (usually a nonprofit labeled as an LLC) that each unit owner has a stake in.

Building ADUs to rent has been investigated extensively as a solution for homeowners vulnerable to displacement. By utilizing their property and building a second unit, homeowners are able to generate additional income to put towards increased housing costs such as property taxes. Alternatively, homeowners could utilize the additional unit to house family members or friends. While this model has received extensive praise, it has not been scalable or known to have large impacts on the current housing landscape.

Homeowners producing ADUs to sell has not been researched as extensively but is thought to have similar challenges as producing ADUs to rent, including financial barriers and project management challenges. An alternative model would be for a developer to "purchase the backyard" of a homeowner. This partnership model would help streamline the process and reduce barriers to development, while still allowing the homeowner to generate money from their property. The homeowner would receive a large sum of money upfront (compared to smaller amounts at a time if they were to rent an ADU out). For some, especially vulnerable homeowners in gentrifying neighborhoods, this model has the potential to help them stay in place.

Research Questions

1) How many small-scale (2-unit) detached condominium properties exist in Travis County? i.e. how many properties exist where a single family home and ADU have been sold separately?
2) How would the costs in this model change based on who develops the ADU (a for-profit developer versus a non-profit developer versus the original

homeowner as the developer)? How would the profits change in each scenario for the homeowner who is "selling their backyard"?

3) How does this model fit into the affordable housing and anti-displacement discussions at the local level?

Report Outline

The report begins by exploring housing market conditions and affordability in Austin in Chapter 2. From here, an affordable housing strategy is introduced: homeowners producing ADUs to rent out for additional income. A brief literature review of this strategy is conducted and the discussion then segues into producing ADUs to sell (a type of condominium regime). Chapter 3 focuses on the condominium regime landscape in Austin: it outlines the legality of this model, describes what type of condominium an ADU would be considered, and provides estimates of how many of these units exist in Travis County through a detailed data analysis. Chapter 4 provides three financial scenarios that are adjusted depending on the type of developer: a for-profit developer, a non-profit developer, and a homeowner as the developer. The last chapter includes main findings, further research ideas, and final recommendations to increase the accessibility of this model beyond for-profit developers.

Methodology

This report utilizes several methodologies. First, a brief data analysis and literature review (Chapter 2) are conducted to examine the current housing conditions and affordability of the Austin MSA. This included reviewing data from the Austin Board of

Realtor's Central Texas Housing Market Reports, Redfin's Housing Market Data, Texas A&M University's Real Estate Research Center's Housing Reports, and the U.S. Census Bureau's American Community Survey data. Additional housing reports produced by the City, local non-profits, local universities, and private companies were reviewed (see bibliography).

Second, an in-depth analysis of Travis County Appraisal District (TCAD) data (Chapter 3) is conducted to examine the detached condominium landscape in Travis County, and to estimate the number of single family homes with ADUs that have been turned into condominium regimes. Data on detached condominiums was retrieved from TCAD. These specific units were found by filtering for those with a land state code of "A4" indicating it is a condominium, and "single family" indicating it is a detached unit (as opposed to "stacked", "hi-rise", or "townhouse"). All of these detached condominium units were then analyzed by their property value, the year they were built, the unit area (in square feet), exemptions, and the percent of interest that the unit owner has in the common areas of the property. All of this information is provided within the TCAD dataset.

Each unit address was then matched with its respective zoning type. Zoning data was retrieved from the City of Austin's open data portal "Zoning by Address" dataset. Zoning was utilized to help determine which units were part of large-scale detached condominium communities, mid-sized detached condominium properties, and small-scale detached condominium properties. Additionally, TCAD data and zoning data were uploaded to ArcGIS to produce visuals on where these units are located within Travis County.

To more accurately count the number of small-scale (or 2-unit) detached condominium properties, the percent of interest that each unit owner has in the common areas of the property was further analyzed. Those with 50% ownership were pulled and matched by address. Those with differing ownership structures (i.e. 60% and 40%, 45% and 55%, etc.) were pulled and individually matched by the ownership percents and addresses. Units could not be matched by address or parcel I.D. alone, as there were frequent inconsistences in the data (i.e. addresses were entered incorrectly, or sorting by parcel I.D. commonly indicated 1, 3, or 4 units per parcel, when there was actually 2). These 2-unit detached condominium properties were then analyzed similarly as all detached condominium units were before: by their property value, the year they were built, the unit area (in square feet), and exemptions.

Lastly, a basic financial model (Chapter 4) is created to examine the impacts of different types of developers (for-profit, non-profit, original homeowner) on costs and profits. Each input for the model is based on local market conditions, obtained from internet searches and interviews with local developers. See the appendix for specific sources.

The first step is the find the total cost of building the unit. This includes adding together construction costs, soft costs (design/architect fees, surveying fees, permitting fees, and the cost of establishing the condominium regime), and carrying costs (in this case just the cost of interest on the loan). I then estimate the sales price and subtract closing costs from this (which includes real estate commissions, broker fees, legal fees, title fees, and insurance for the seller). I then calculate the total expected profit (for both the developer and homeowner) by subtracting the total unit cost from the new sales price. From here, I calculate the portion of this profit that that developer would take, a percent of the return on the equity capital that the developer puts into the deal. This is a usually a fee reflected in total cost of building the unit, but in this scenario it is pulled below to show the portions of the profit that both the developer and homeowner are receiving. The developer's fee is then subtracted from total expected profit to see what the homeowner would be expected to get for "selling their backyard".

Definitions

The following words and/or phrases are used frequently in this report. The terms may be used differently or the meaning may change in different contexts. The list below helps clarify the words and/or phrases in terms of their meaning in this report.

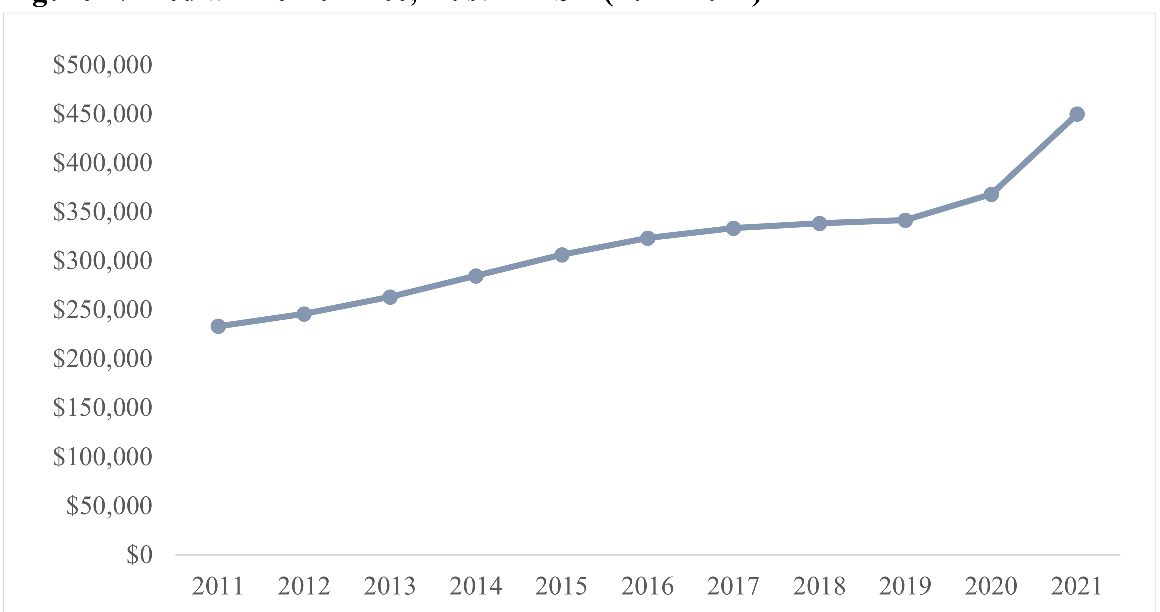
- Accessory dwelling unit (ADU): a detached secondary unit on a single family property. Also known as granny flats, alley flats, and carriage houses among other names. May be called ADUs or secondary units interchangeably in this report.
- Condominium: a form of real property ownership. Does not imply any particular building type. The units are individually owned, while the land is owned by a condominium association (typically a nonprofit) that each individual has a stake in. May also be called a condominium regime.
- Detached condominium: a condo whose individual units stand alone and are not attached to any other units including by walls, floors, ceilings, garages, or breezeways.
- Small-scale: refers to 2-unit condominium sites; commonly used within the phrase "small-scale detached condominium".

Chapter 2: Background Information

Housing Market Conditions and Affordability in Austin

Over the past several years, housing costs have significantly increased in the Austin Metropolitan Statistical Area (MSA). In September of 2022, the median home price for the area was $470,000. (Austin Board of Realtors, 2022). At the same time, median asking rents reached $2,395, nearly $400 greater than the national median (Redfin, 2022). In the past year and a half, median home prices jumped nearly 16% (Austin Board of Realtors, 2022), while median asking rents surged by 31% (Redfin, 2022). Additionally, when tracking median home prices in the past decade we see an increase from $233,527[2] in 2011 to $450,000 in 2021 (Texas A&M University, 2022). This is shown in Figure 1 below.

Figure 1: Median Home Price, Austin MSA (2011-2021)



Note: Data are retrieved from the Texas Real Estate Research Center at Texas A&M University (https://www.recenter.tamu.edu/data/housing-activity/#!/activity/MSA/Austin-Round_Rock). All prices have been adjusted for inflation, in 2021 dollars.

[2] Adjusted for inflation, in 2021 dollars

Most alarmingly, median family incomes in the Austin MSA have not been keeping up with soaring housing costs. In the past decade, median family incomes have only increased 22%, compared to the 93% increase in home prices (U.S. Census Bureau, 2021). When analyzing housing prices in relation to income through a ratio known as the median multiplier, we can see that housing affordability has been decreasing in the MSA. Prior to 2014 this number was 3.0 or less, indicating an "affordable" housing market. Between 2015 and 2019, the number rose to between 3.1 and 4.0, indicating a "moderately unaffordable" housing market. Finally in 2021, the number rises to 4.1, indicating a "seriously unaffordable" housing market[3]. Table 1 demonstrates these year by year changes.

[3]These ratings are determined by the Demographia International Housing Affordability Report: http://www.demographia.com/dhi.pdf

Table 1: Median Home Prices and Median Family Income, Austin MSA (2011-2021)

Year	Median home price[4]	Percent change in median home price from year prior	Median family income[5]	Percent change in median family income from year prior	Median multiplier
2011	$233,527	-	$89,522	-	2.6
2012	$245,894	5.0%	$88,621	-1.0%	2.8
2013	$263,191	6.6%	$90,637	2.3%	2.9
2014	$284,843	7.6%	$93,713	3.4%	3.0
2015	$306,473	7.1%	$96,225	2.7%	3.2
2016	$323,340	5.2%	$104,171	8.3%	3.1
2017	$333,342	3.0%	$103,890	-0.3%	3.2
2018	$338,469	1.5%	$105,000	1.1%	3.2
2019	$341,757	1.0%	$107,656	2.5%	3.2
2020	$368,195	7.2%	-	0.7%*	-
2021	$450,000	18.2%	$109,059	0.7%*	4.1

Note: Median home price data are retrieved from Texas Real Estate Research Center at Texas A&M University (https://www.recenter.tamu.edu/data/housing-activity/#!/activity/MSA/Austin-Round_Rock). Median family income data are retrieved from the U.S. Census Bureau, American Community Survey 1-year estimates. *Calculated as a percent change between 2019 and 2021, divided in half.

This large increase in home prices combined with a slower, steady increase in incomes has led to a widespread affordability crisis. Some households now cannot afford to buy homes when this may have been a possibility for them in the past. According to the Austin Housing Analysis project, the housing stock for low- and moderate-income households has changed dramatically. Currently, little to no single-family housing exists that would be affordable to low-income households (University of Texas at Austin, 2021). Additionally, there has been a decrease in single-family housing affordable to households making less than the median household income (University of Texas at Austin, 2021). The most recent Comprehensive Housing Market Analysis for the City of Austin specifically

[4] Adjusted for inflation, in 2021 dollars
[5] Adjusted for inflation, in 2021 dollars

outlines how between 2008 and 2018, the amount of for-sale housing that would be affordable for renters earning less than $75,000 decreased from 49% to 22% of the total homes listed and sold in those years (Root Policy Research, 2020). The same report shows that middle-income households experienced a drop in homeownership rates (Root Policy Research, 2020). In the U.S., homeownership is seen as a building block for future success and wealth accrual. Without affordable home purchase options, low- and moderate-income households may struggle to build wealth.

In addition to the market affecting households looking to purchase homes, it also affects current homeowners. When home prices increase rapidly, property taxes follow suit. For many homeowners, especially those who are low-income and/or on a fixed income, increases in housing costs can affect their ability to keep up with payments and stay in their homes.

One way to measure vulnerable homeowners in an area is to analyze cost-burdened households. Cost-burdened means that a household is spending more than 30% of its income on housing costs, leaving less income for other necessities such as food, transportation, childcare, and more. In the Austin MSA, 34.8% of homeowners are cost-burdened and 9.1% are severely cost-burdened, i.e., spending more than 50% of their income on housing costs (U.S. Census Bureau, 2020). Severe housing cost-burdens are more common for people of color in Austin. According to the Comprehensive Housing Market Analysis for the City of Austin, "non-Hispanic White households face severe cost burden 15% of the time; this compares to 25% of the time for African American households; 23% for Hispanic households; and 20% for Asian households" (Root Policy

Research, 2020). Because people of color experience higher cost-burdens, they may be more vulnerable to the detrimental effects of increasing housing costs.

While these conditions are a citywide phenomenon, they're particularly concentrated in an area known as the Eastern Crescent. After decades of segregation and racist policies and practices, intentionally resulting in lower property values for communities of color and working class households, the downtown-adjacent sections of the Eastern Crescent had become desirable for affluent households at the turn of the century.

As housing prices increase and a more affluent population moves in changing a neighborhood's character, a process known as gentrification, vulnerable households are displaced. According to Uprooted report, the process of gentrification has three elements: "1) the displacement of lower-income residents; 2) the physical transformation of the neighborhood-mostly through the upgrading of its housing stock and commercial spaces; and 3) the changing cultural character of the neighborhood" (The University of Texas at Austin, 2018).

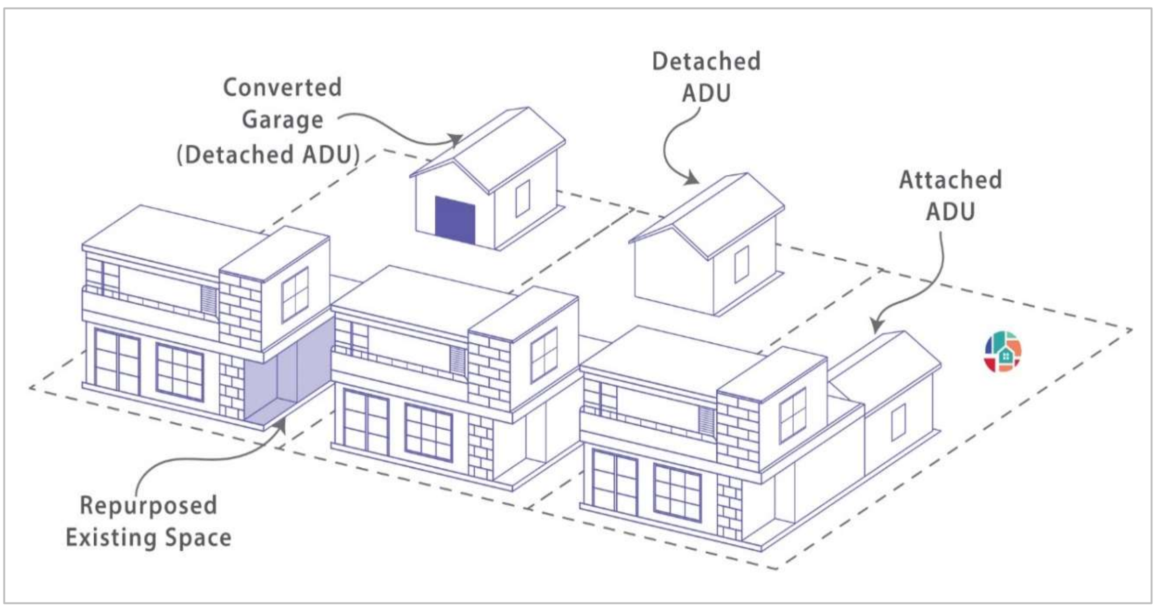
The Uprooted report highlights populations most vulnerable to displacement: people of color, people 25 and older without bachelor's degree, renters, people making at or below 80% MFI, and households with children in poverty (The University of Texas at Austin, 2018). Displaced households may lose their sense of community in this process. Additionally, they may be pushed into areas with lower housing costs, which may be further from the city center and needed services.

Many ideas have emerged across the nation and locally to try to mitigate the displacement of vulnerable households. This report focuses on strategies where homeowners are able to generate income from utilizing their property.

Accessory Dwelling Units (ADUs) in Austin

Accessory Dwelling Units (ADUs), also known as granny flats, alley flats, and carriage houses among other names, are secondary residential units built on a lot where a single family home or primary unit exists. According to the City of Austin, an accessory dwelling unit is "a separate dwelling unit on the same property as a single-family home that is smaller in size" (City of Austin, n.d.).

Figure 2: Types of ADUs



Note: Figure showcasing types of ADUs. The City of Austin ordinance and this report focuses on detached ADUs. Retrieved from https://detachedadu.com/events-about-adus/.

These units present many benefits. In terms of their uses, homeowners can produce ADUs on their properties to rent to others for additional income generation, or they can use them to house family members and guests. Additionally, they can sell these units separately by establishing a condominium regime on their property (details on how to establish a condominium regime are provided in Chapter 3). Because these units are smaller and share a lot with another structure, they are thought to be more affordable than other housing purchase options (University of Texas at Austin, 2021). Additionally, there is a wide array of literature outlining the broad benefits of this type of development including increasing density of neighborhoods, promoting walkability, and more (Ramsey-Musolf, 2018) (Cabrera & Najarian, 2013) (Johnson & Talen, 2010).

Despite ADUs' flexibility and benefits, their production across the country has long been stalled due to regulatory challenges. Zoning regulations such as parking requirements, minimum lot sizes, density limitations, and setback standards can prevent large areas of cities from producing second units on single family lots. For lots where development is possible, complicated and lengthy permitting requirements, site design requirements, and vocal neighborhood opposition groups can add to frustrations.

Many municipalities, including the City of Austin, have recognized these regulatory barriers and adjusted policies accordingly. The discussion of ADU development picked up in Austin in 2000, when the creation of Neighborhood Planning Areas allowed for neighborhood associations to decide whether to permit ADUs in their areas (University of Texas at Austin, 2021). With goals of increasing ADU production and creating more affordable housing opportunities citywide, the City updated its ADU ordinance in 2015 (University of Texas at Austin, 2021). The below excerpt highlights these adjustments:

> As per the new regulations, the new minimum lot size is reduced to 5,750 square feet for SF3 zoned lots. The maximum size of an ADU has been increased to 1,100 square feet or 0.15 FAR (Floor Area Ratio), whichever is smaller. The City reduced minimum distance from the main structure to 10 feet from 15 feet, while eliminating the requirement of the ADU entry being 10 feet behind the property line. While there is a one parking space requirement in addition to the parking of the main structure, parking requirements are eliminated for parcels within a 1/4 mile of activity corridors as identified by the Imagine Austin comprehensive plan. ADUs cannot be used for type 2 rentals (non-owner occupied single-family or duplex rental), and short-term rentals are limited to 30 days per year. The new ordinance also eliminated driveway requirements for ADUs. (Wegmann, 2016, p. 6)

The ordinance update has had mixed results. On one hand, ADU production has increased. In 2016, the amount of ADUs under construction had doubled from the year prior (Wegmann, 2016). When analyzing permit data for residential accessory use permits, the number of permits between 2017 and 2018 skyrocketed, from about 100 to over 1,500 (University of Texas at Austin, 2021). On the other hand, ADU production has not necessarily benefited those seeking more affordable options. It was suspected that developers would be the main drivers of ADU production, given their access to financing (Wegmann, 2016). More recently, the Austin Housing Analysis confirms that "Austin's ADU policy has led to a significant increase in high-value primary homes built as part of demolition and multi-unit redevelopments involving ADUs" (University of Texas at Austin, 2021).

So while ADU production increased in the past several years due to the removal of land use barriers at the city-level, it was not heavily pursued by existing homeowners looking to develop a second unit on their property, especially vulnerable homeowners that could benefit most from additional wealth building opportunities. There are many reasons for this. For one, in order for a homeowner to pursue this process they must act as a developer; they have to be familiar with or willing to learn the intense, complicated rules of financing, city zoning and building codes, construction, leasing, property management, and more (Chapple, Wegmann, Mashhood, & Coleman, 2017). For any homeowner this can be difficult and overwhelming, especially when added to other commitments such as work and family.

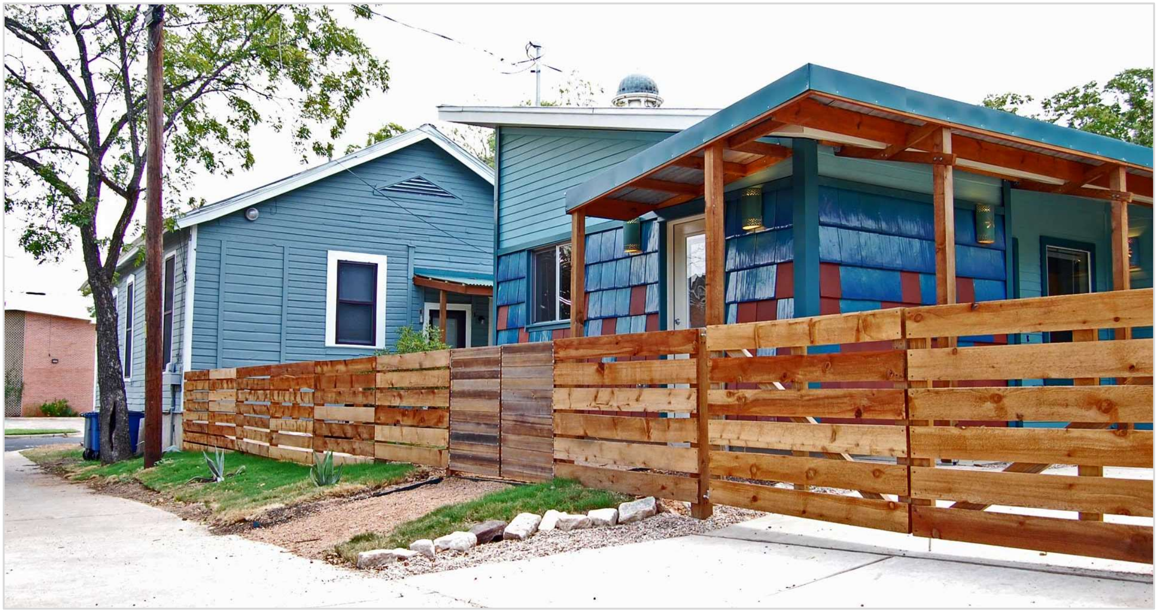
Another barrier for homeowners is financing the construction of an ADU. For low- and moderate-income seeking private financing, options are limited, especially when considering that financing usually needs to cover an entire property and not just the new structure. Two options are home equity lines of credit (HELOCs) and cash-out refinancing. An Urban Institute report compares these options:

> Home equity lines of credit, or HELOCs, leverage homeowners' existing equity. A homeowner must have at least 10 percent equity in their home, after which they can get a loan for an amount above that 10 percent threshold. However, HELOCs consider only the current value of a home, not the future value including the ADU, and thus may be too small to cover construction costs. Another downside of HELOCs is they are often variable-rate mortgages, and they require high credit scores to access. Cash-out refinances also allow borrowers to tap into the equity of their home—again, based on the current value, not the future value of the home with the ADU. Cash-out refinances require the homeowner to have at least 15 percent equity in the property. This is a higher threshold than HELOCs, but cash-out refinances have fixed, amortized interest rates, which is a benefit (The Urban Institute, 2020, pp. 15-16).

For homeowners to secure these options they need a low debt to income ratio, sufficient existing equity, and good credit scores, which many low- and moderate-income households struggle to achieve (Wegmann, 2016). Different funding mechanisms exist, including using cash savings, credit cards, borrowing from family or friends, construction loans or other risky loans, but many of these options are unrealistic or not ideal for many homeowners (The Urban Institute, 2020). Even if homeowners are able to secure initial financing, issues may arise with the project further increasing costs. In addition to this, once an ADU is constructed the value of the property may increase, which leads to increases in property taxes (Wegmann, 2016). As such, costs can increase quickly and unexpectedly.

What emerges is a need for technical assistance and flexible financing options. A local program, the Alley Flat Initiative, has attempted to remedy these needs. A collaboration between The University of Texas Center for Sustainable Development, Guadalupe Neighborhood Development Corporation, and Community Powered Workshop, the program began in 2005 as a way to bring sustainable, affordable "alley flats" (ADUs) into Austin neighborhoods. The partners worked with homeowners to build detached ADUs on the homeowner's properties for them to rent out for additional income or house family members and other guests. While the program has received national praise and has been used as a model for other cities, it has not been as successful in implementation: only 16 units have been produced since the project's conception (Jake Wegmann, personal communication, November 1, 2022). A detailed land analysis from 2008 estimated that thousands of city lots had the potential to develop alley flats (The University of Texas Center for Sustainable Development, 2008). Similarly to other innovative housing initiatives, scalability seems to be a disadvantage for the program.

Figure 3: Example of an Alley Flat in Austin (1)



Note: Unit produced by the Alley Flat Initiative. Featuring the Lydia design: a 584 square foot, 1-story unit with 1 bedroom and 1 bathroom. Perspective picture showing both the original unit and new unit. Retrieved from Community Powered Workshop (https://communitypoweredworkshop.org/the-alley-flat-initiative).

Figure 4: Example of an Alley Flat in Austin (2)

Note: Unit produced by the Alley Flat Initiative. Featuring the Canterbury design: an 830 square foot, 2-story unit with 1+ bedrooms and 2 bathrooms. Retrieved from Community Powered Workshop (https://communitypoweredworkshop.org/the-alley-flat-initiative).

From Accessory Dwelling Units (ADUs) to Condominiums

People develop ADUs for various reasons. They may be looking for a more affordable option for housing a family member or friend, or they may rent or sell the unit (or entire property) for additional income. In order to sell an ADU (or both the main structure and ADU separately from one another), the lot must be split (a long, expensive, and sometimes impossible task) or a condominium regime must be established on the property. Detailed steps for establishing a condominium regime on a single family lot are outlined in Chapter 3.

For homeowners looking to pursue this process of building and selling a second unit on their property, the path can be complicated and expensive, similar to building and renting a second unit on their property. The same regulatory, financial, and management challenges may exist. For others looking to pursue this process (particularly developers), the path can be a lot more streamlined, especially if it's something they've done before. Experienced developers are able to navigate regulatory and management challenges with more ease, and have better access to financing options. This may be why we've seen more ADUs built "…as part of demolition and multi-unit redevelopments…" (University of Texas at Austin, 2021). They can purchase a single family lot, demolish the original structure, and produce two high-value units that they can sell at a profit. This is commonly seen on properties on the east side of Austin, and other areas close to downtown such as Crestview or South Congress. Chapter 3 estimates how many of these units exist within Travis County, whether built by developers or the original homeowners.

Another model, one explored in this report, would be for developers (or other entities) to purchase "backyards" on single family lots where ADUs are permitted. The developer would purchase the right to build a second unit on the original owner's property, and manage the process including establishing the condominium regime, building the second unit, and selling the second unit. This approach would be more hands off for the original owner, but still allow them to utilize their property to generate money. Chapter 4 of this report explores the outcomes of different types of developers pursuing this model (a for-profit developer versus a non-profit developer versus the homeowner as the developer).

Chapter 3: The Detached Condominium Landscape in Austin

Condominium Regulations

The Texas Uniform Condominium Act (TUCA), within the Texas Property Code, outlines the legality and requirements of condominiums. Per this act, a condominium is:

> A form of real property with portions of the real property designated for separate ownership or occupancy, and the remainder of the real property designated for common ownership or occupancy solely by the owners of those portions. Real property is a condominium only if one or more of the common elements are directly owned in undivided interests by the unit owners. Real property is not a condominium if all of the common elements are owned by a legal entity separate from the unit owners, such as a corporation, even if the separate legal entity is owned by the unit owners (Texas Uniform Condominium Act, 1994, sec. 82.003).

TUCA outlines that municipalities are still able to regulate condominiums. The act "… does not affect or diminish the rights of municipalities and counties to approve plats of subdivisions and enforce building codes as may be authorized or required by law" (Texas Uniform Condominium Act, 1993). However, the act states earlier on that "A zoning, subdivision, building code, or other real property use law, ordinance, or regulation may not prohibit the condominium form of ownership or impose any requirement on a condominium that it would not impose on a physically identical development under a different form of ownership" (Texas Uniform Condominium Act, 1993). This means that city officials must regulate developments that look similar (i.e. single family homes) the same, regardless of ownership type (a single family home that is rented versus owned). This regulation is what allows condominium regimes to be possible in Austin.

In order to establish a condominium regime, one must first check that the property allows for condominium development. This includes checking local zoning laws and if any restrictive covenants exist on the property. After this, a “Declaration of Condominium” needs to be filed at the county level. This outlines what the physical layout of the property will look like, creates a non-profit corporation that acts as an owner’s association, and establishes the unit/land ownership types[6]. As of November 2022, Travis County real estate records display 7,193 Declarations of Condominiums (Travis County, 2022). Because the document can be complex and lengthy, it is typical (and recommended) for attorneys to draft these. Additionally, a surveyor or engineer is required to map out certain attachments to the declaration.

Types of Condominiums

Condominiums exist in many different built forms in Austin. They can look like large-scale multi-unit developments, single-family homes, or something in between. They can be residential, commercial, industrial, or mixed-use. They can be attached to one another or detached. The type of condominium discussed in this report has several names, with the most common ones being “detached condo”, “site condo”, or “horizontal condo”. According to Fannie Mae, definitions for detached condos are provided below:

> A condo unit that is completely detached from other condo units in the project. The unit may share no adjoining walls, ceilings, floors, or other attached architectural elements (such as breezeways or garages) with any neighboring unit. A detached condo unit may be in a project consisting solely of detached units or in a development containing a mixture of attached and detached units. Site condos in which the unit owner owns the detached condo unit and the land upon which the unit is built are a type of detached condo (Fannie Mae, 2022).

[6] TUCA provides detailed information on what needs to be included in a condominium declaration.

Properties with detached condominiums contain the physical unit, owned by an individual, and the land, owned by a non-profit association that each individual has a stake in. The land may have limited common elements for use specifically by an individual owner (typically patios, garages, etc.), and general common elements for use by all owners. As such, individual owners of the units do not own real estate (i.e. ownership is not extended to the land).

Detached condominiums have become popular in Austin because they do not require lot subdivision through the city's traditional regulatory process, a process that is not permitted under many zoning categories and where getting a variance or rezoning request can be extremely difficult. Instead, detached condominiums can be platted and planned through section 82.059 of TUCA (Burton, 2020). This is how owners of single family lots with ADUs are able to establish condominium regimes and sell the units separately (the lot does not need to be split and can circumvent minimum lot requirements). This is also why we've seen the expansion of "detached condominium communities". These are large-scale communities that look like traditional single-family home subdivisions (where the homeowner also owns their land), but are actually condominium regimes.

The first section of the following data analysis investigates the broad detached condominium landscape in Travis County. The next section of the data analysis examines the small-scale, or 2-unit, detached condominium properties in Travis County to begin to understand how many single-family lots with ADUs have been turned into condominium regimes.

Data Analysis: All Detached Condominiums

As of 2022, there are 13,264 detached condominiums in Travis County. When analyzing these units, the median property value is $572,581. This is comparable to the median home sales price of $550,000 for Travis County in 2022 (Austin Board of Realtors, 2022). This is expected, considering that these units present as detached single-family homes. In addition to this, the median area is 1,781 square feet and median year built for these units is 2016. As such, when analyzing all detached condominiums together they appear to be relatively new and affordable.

These units can be a part of large-scale detached condominium communities, mid-sized detached condominium properties, or small-scale detached condominium properties. To determine how many units fall within each property-type, they can be analyzed by zoning and by the percent that the unit owner has in the common areas of the property[7]. These methods are by no means perfect, and as such this section does not attempt to estimate the number of units in large-scale and mid-sized detached condominium developments. The section rather shows patterns seen in zoning and ownership shares in common areas for each type of development. In the next section on small-scale detached condominiums I report the results of a detailed analysis that provides these estimates.

Table 2 below shows the number of detached condominium units that fall within each zoning category. Most units fall within residential categories; however, some fall within commercial, office, or other categories. While there are some commercial and office

[7] Theoretically, the number of units on a property should be able to be analyzed by parcel ID or address, however a quick analysis proved too many inconsistencies in these methods.

units sprinkled in, most of these are actually residential. These could be inconsistencies between TCAD and City of Austin zoning classifications, or potentially cases where property owners were able to get zoning variances.

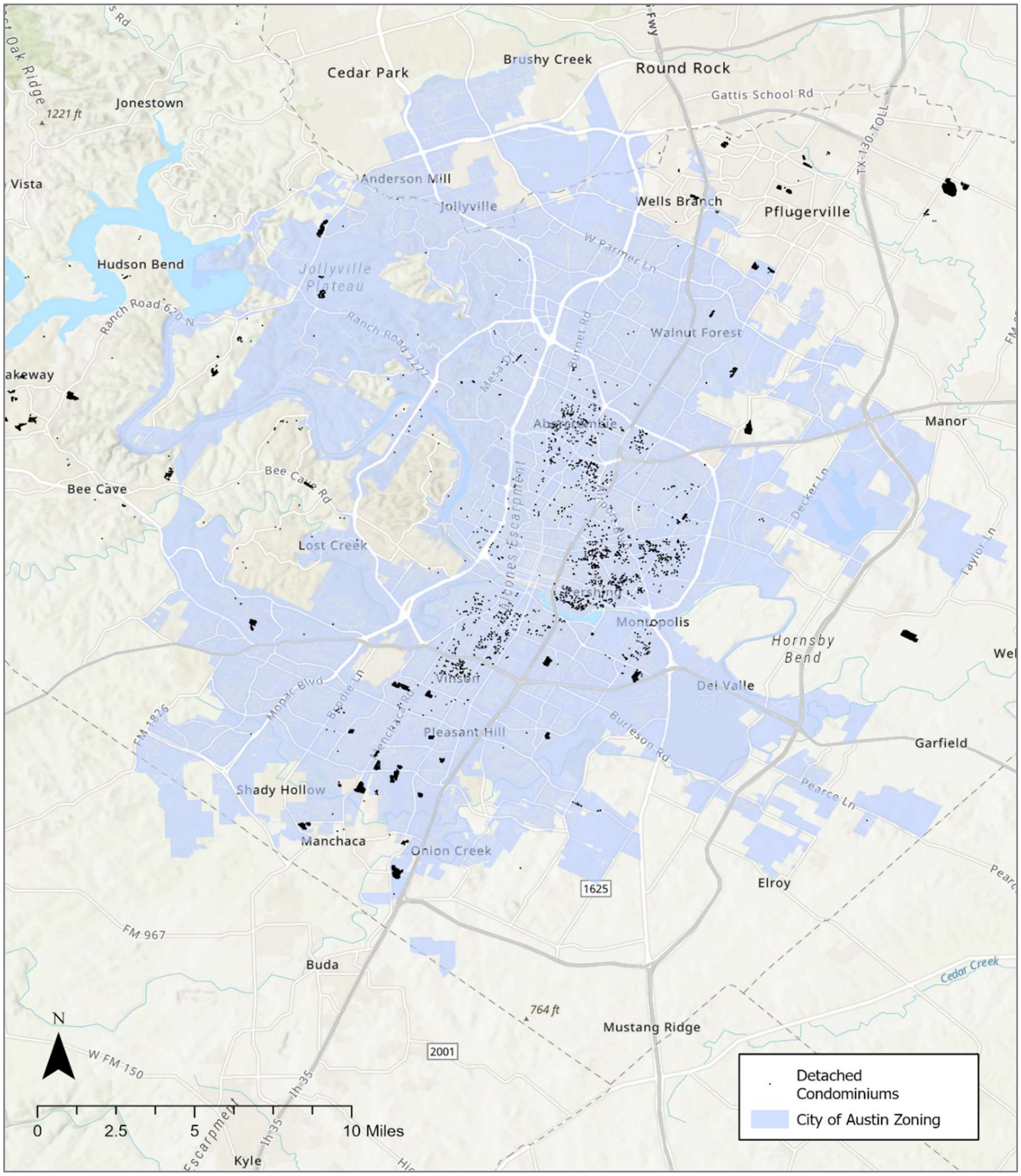
Table 2: Detached Condominium Units by Zoning Type

Base Zoning	Zoning Category	Number of Detached Condominium Units
SF-3	Family Residence	3271
SF-6	Townhouse and Condominium	2396
PUD	Planned Unit Development	1269
RR	Rural Residence	715
GR	Community Commercial	355
MF-2	Multi-Family Low Density	347
MF-3	Multi-Family Moderate Density	290
ERC	East Riverside Corridor	135
LO	Limited Office	106
MF-4	Multi-Family Moderate-High Density	59
LR	Neighborhood Commercial	54
CS	General Commercial Services	51
SF-5	Urban Family Residence	49
GO	General Office	34
TOD	Transit-Oriented Development	32
SF-4A	Single Family Small Lot	18
MF-1	Multi-Family Limited Density	10
SF-2	Single Family Standard Lot	6
P	Public (P)	2
N/A	No zoning identified	4065
Total		**13264**

Note: Condominium data are retrieved from the Travis County Appraisal District. Zoning data are retrieved from the City of Austin's open data portal (https://data.austintexas.gov/Locations-and-Maps/Zoning-by-Address/nbzi-qabm).

Many of the condominiums do not have identifiable zoning, denoted as N/A on Table 2. Of these condominiums with no zoning identified, the majority sit outside of the City of Austin limits and therefore outside of zoning boundaries, and 20 of these properties were unidentifiable. Figure 5 below shows where the condominiums are located in relation to the City of Austin's zoning boundaries.

Figure 5: Detached Condominium Units and City of Austin Zoning Boundaries



Note: Condominium data are retrieved from the Travis County Appraisal District. Zoning data are retrieved from the City of Austin's open data portal (https://data.austintexas.gov/Locations-and-Maps/Zoning-by-Address/nbzi-qabm).

The first property type analyzed, large-scale detached condominium communities, tend to look like traditional single-family home subdivisions (where the homeowner also owns their land), but they are actually condominium regimes. Research indicates that the SF-6 zoning category is ideal for the development of detached condominium communities given that these zones are in suburban areas with larger tracts of land available (Valenzuela, 2018). These large scale projects have seen a number of benefits, most notably they are known for:

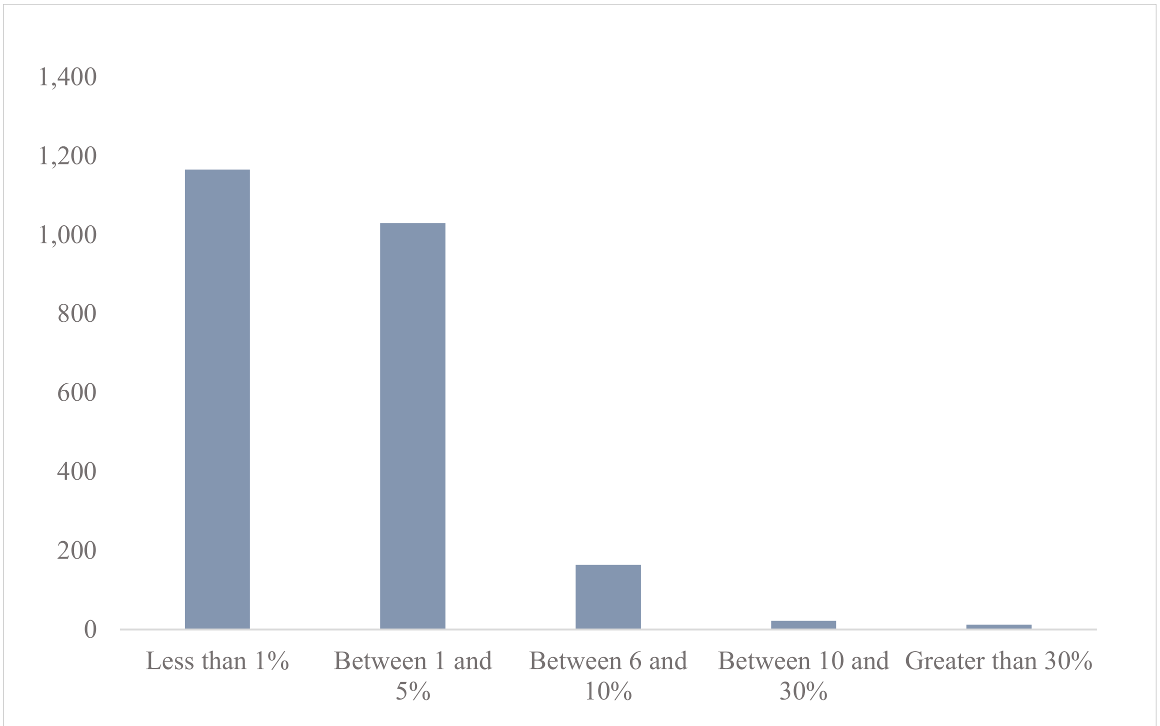
> (1) increasing density by allowing the developer to set the site condominium land area, (2) freeing the project from rectilinear lot lines, (3) greater flexibility to assign impervious cover to meet the market for building improvements (where impervious cover would otherwise be equally apportioned among platted lots), and (4) a more time and cost efficient local regulatory approval process (Burton, 2020, p. 3).

The data on these types of projects are limited, but a report from 2018 inventories this type of community in the South Austin area[8], determining that 20 communities exist with a total of 1,810 detached units (Valenzuela, 2018). It is likely these numbers have increased in the past couple of years.

Because the properties can contain up to hundreds of units, the percent that the unit owner has in the common areas of the property tends to be very small, usually less than 1%. For example, Figure 6 below shows the percent ownership in common areas for units that fall within SF-6 zoning (a total of 2,396 units).

[8] These types of communities exist elsewhere in Austin as well. The report mentioned only examines South Austin.

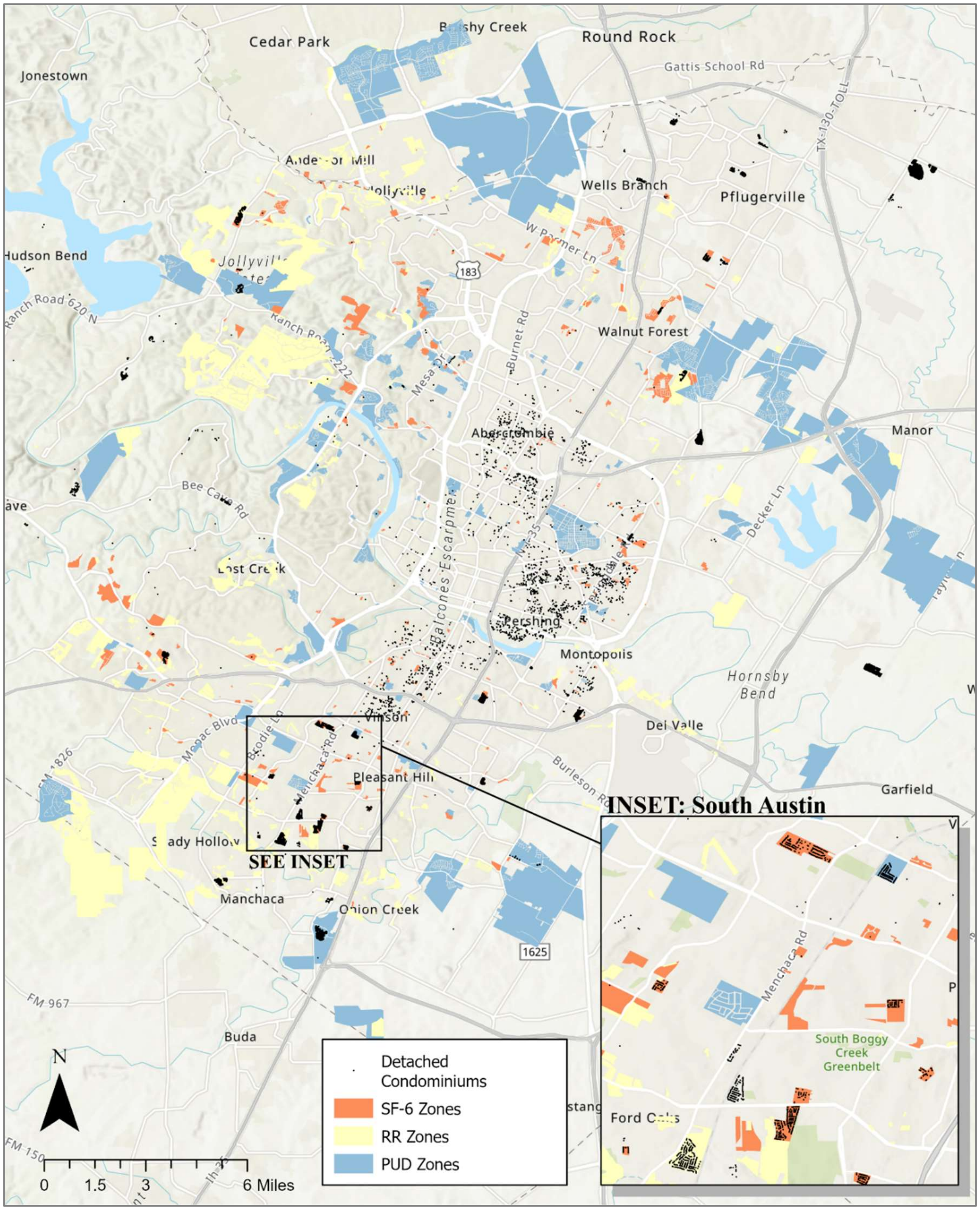
Figure 6: Number of Detached Condominium Units by Percent Ownership in Common Areas within SF-6 Zoning



Note: Condominium data are retrieved from the Travis County Appraisal District. Zoning data are retrieved from the City of Austin's open data portal (https://data.austintexas.gov/Locations-and-Maps/Zoning-by-Address/nbzi-qabm).

Upon further analysis, popular zoning categories for large-scale detached condominium communities (beyond SF-6) are PUD with 1,269 units and RR with 715 units. Similarly to SF-6, these zones sit further from downtown where larger tracts of land are available, making them ideal for this type of development. Figure 7 below displays SF-6, PUD, and RR zones. An inset is included for South Austin, highlighting detached condominium communities within these zones.

Figure 7: Detached Condominium Units by SF-6, PUD, and RR Zones



Note: Condominium data are retrieved from the Travis County Appraisal District. Zoning data are retrieved from the City of Austin's open data portal (https://data.austintexas.gov/Locations-and-Maps/Zoning-by-Address/nbzi-qabm).

Another type of property analyzed, mid-sized detached condominium properties, tends to be located in areas with MF (multi-family) zoning. These are seen scattered closer towards downtown in Figure 5. The number of units on these properties can vary, with the most common being 3 or 4. As such, ownership structures of common areas are typically split as 33% or 25% for each unit owner. It is unclear if research exists on these types of properties specifically; however, they could be further analyzed especially in relation to missing middle housing discussions.

The last assumed property type, small-scale detached condominium properties, tend to be zoned SF-3 (family residence), as seen scattered closer to downtown in Figure 5. This report classifies these properties as those with 2 units. This classification is created to help determine how many properties exist where a single family home and ADU were turned into a condominium regime. The ownership split for common areas can be 50% for unit 1 and 50% for unit 2, but these can also be uneven ownership splits (i.e. 30% for unit 1 and 70% for unit 2, or 65% for unit 1 and 35% for unit 2). More is presented on these types of properties in the next section.

Data Analysis: Small-Scale Detached Condominiums

An estimated 3,052 detached condominium units exist as part of 2-unit condominium properties in Travis County (i.e. there are an estimated 1,526 properties that were single family homes with ADUs turned into condominium regimes). This makes up around 23% of all detached condominium units.

Of these properties, 58% have an equal ownership structure, where the owners of both unit 1 and unit 2 maintain a 50% share of common areas. About 42% of units have a different split for ownership of common areas. In these units with majority-minority splits in ownership share, one unit owner will essentially have a controlling interest in the property. Some potential effects of this include different condominium fees between the units, and diminished value in the unit with a lesser share.

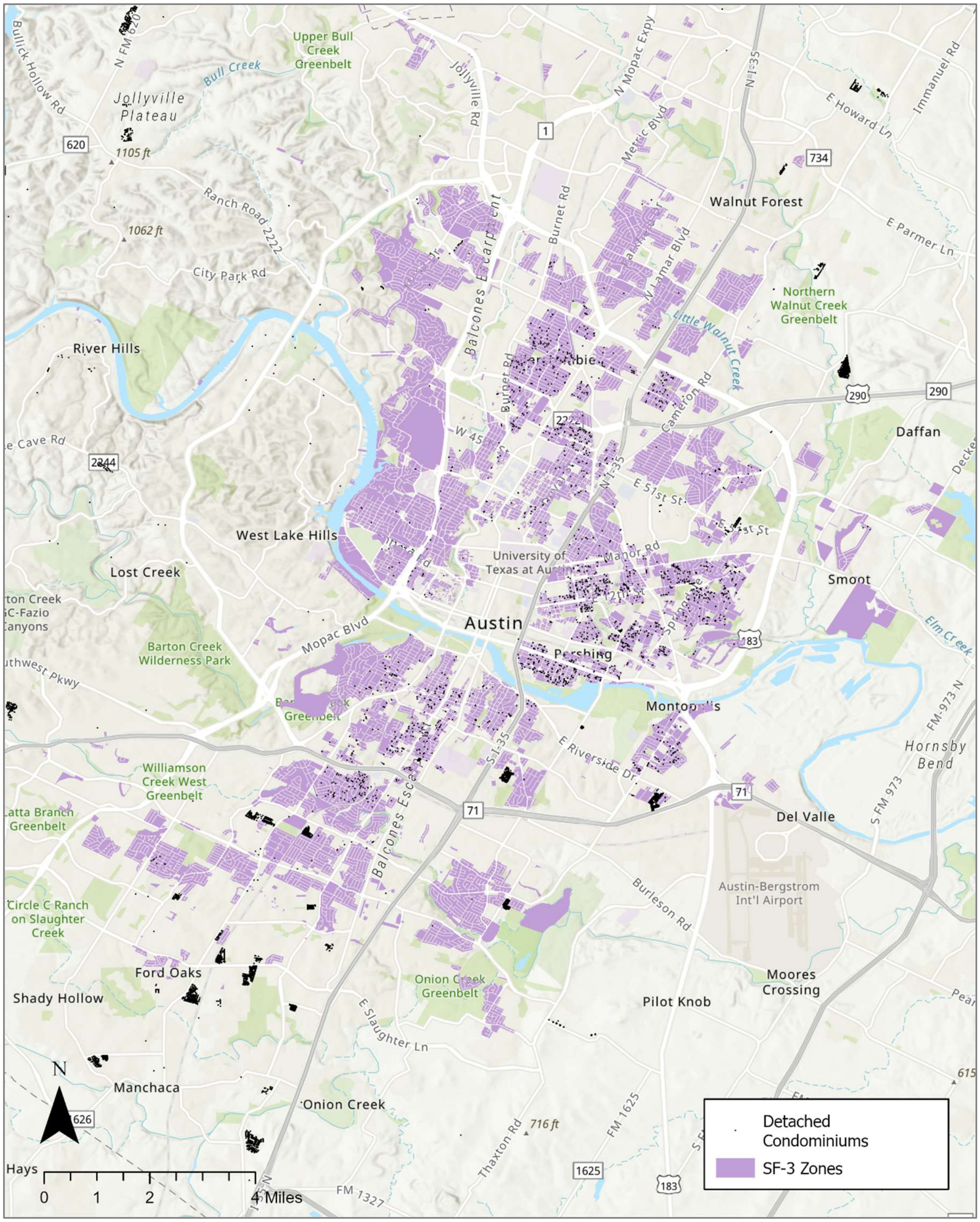
When analyzing small-scale detached condominium units by zoning, the majority (nearly 97%) fall under SF-3 (family residence) zoning. The breakdown by zoning is shown in Table 3. Additionally, Figure 8 shows the location of all detached condominium units within SF-3 zoning.

Table 3: Condominium Units (Part of 2-Unit Detached Condominium Properties) by Zoning Type

Base Zoning	Zoning Category	Number of Detached Condominium Units
SF-3	Family Residence	2812
MF-3	Multi-Family Moderate Density	17
CS	General Commercial Services	12
SF-6	Townhouse and Condominium	11
LR	Neighborhood Commercial	8
MF-4	Multi-Family Moderate-High Density	7
MF-2	Multi-Family Low Density	6
SF-2	Single Family Standard Lot	4
GR	Community Commercial	2
SF-4A	Single Family Small Lot	2
SF-5	Urban Family Residence	2
N/A	No zoning identified	16
Total		**2899***

Note: Condominium data are retrieved from the Travis County Appraisal District. Zoning data are retrieved from the City of Austin's open data portal (https://data.austintexas.gov/Locations-and-Maps/Zoning-by-Address/nbzi-qabm). 3,052 units were determined to be part of a small-scale condominium property, but only 2,899 of these units were able to be confirmed through an ownership in common areas analysis.

Figure 8: Detached Condominium Units by SF-3 Zoning



Note: Condominium data are retrieved from the Travis County Appraisal District. Zoning data are retrieved from the City of Austin's open data portal (https://data.austintexas.gov/Locations-and-Maps/Zoning-by-Address/nbzi-qabm).

The SF-3 zoning category does not explicitly allow for residential condominium use within the City of Austin's Guide to Zoning. However, many of these properties also fall within Neighborhood Planning Areas. In 2000, the city allowed for the Neighborhood Plan Contact Teams (NPCTs) in charge of these areas to decide whether to permit ADUs (University of Texas at Austin, 2021). Additionally, in 2015 the city updated its ordinances to allow for ADUs on smaller SF-3 lots, regardless of whether a neighborhood association had opted in to allowing ADUs; in addition, the minimum lot size was reduced to 5,750 square feet (University of Texas at Austin, 2021). So, a potential explanation for the large number of detached condominiums on SF-3 zoned lots is that the owners of these properties built an ADU behind an existing unit (or demolished the original unit and built two new units) and established a condominium regime so that both units could be sold separately.

Two specific examples of this scenario are provided below. Both examples are SF-3 zoned properties, located in East Austin on corner lots.

Example one is 2001 Willow Street. This property currently contains two units, each owned by a different individual who maintains 50% interest in the common areas. When analyzing the property's history, it is evident that it was part of a redevelopment scheme.[9] Figure 9 shows the property pre-development, where it contained a single 1,138 square foot unit set back far from Willow Street. In January of 2018, the property was listed for sale on Zillow for $420,000. It was bought within a month of being listed. Shortly after, the original structure was moved to outside the city limits. Images from 2018 (Figure 10)

[9] All property information is retrieved from the City of Austin's Property Profile tool (https://maps.austintexas.gov/GIS/PropertyProfile/), the City of Austin's permitting data (https://data.austintexas.gov/Building-and-Development/Issued-Construction-Permits/3syk-w9eu/data), and Travis County's Clerk Web Search (https://www.tccsearch.org/).

show the unit and other property structures (shed in the front, fence, etc.) as removed and/or demolished. In June of 2018, permits were filed and approved to construct a new single family home with an ADU on the property. A year later, the owners establish a condominium regime on the property, effectively splitting the new single family home and ADU into unit 1 and unit 2 respectively. The units are sold within a month. Per TCAD, the appraised value for unit 1 (1,728 square feet) is $966,045, and the appraised value for unit 2 (1,036 square feet) is $715,419. Figure 11 shows the two new units on the lot.

Figure 9: 2001 Willow Street, circa 2011

Note: Image shows the original 1,138 square foot unit on the property, set back far from Willow Street. The property also contains a fence and storage shed out front. Retrieved from Google Street View.

Figure 10: 2001 Willow Street, circa 2018

Note: Image shows the property now empty, after the original unit was removed and other structures demolished. Retrieved from Google Street View.

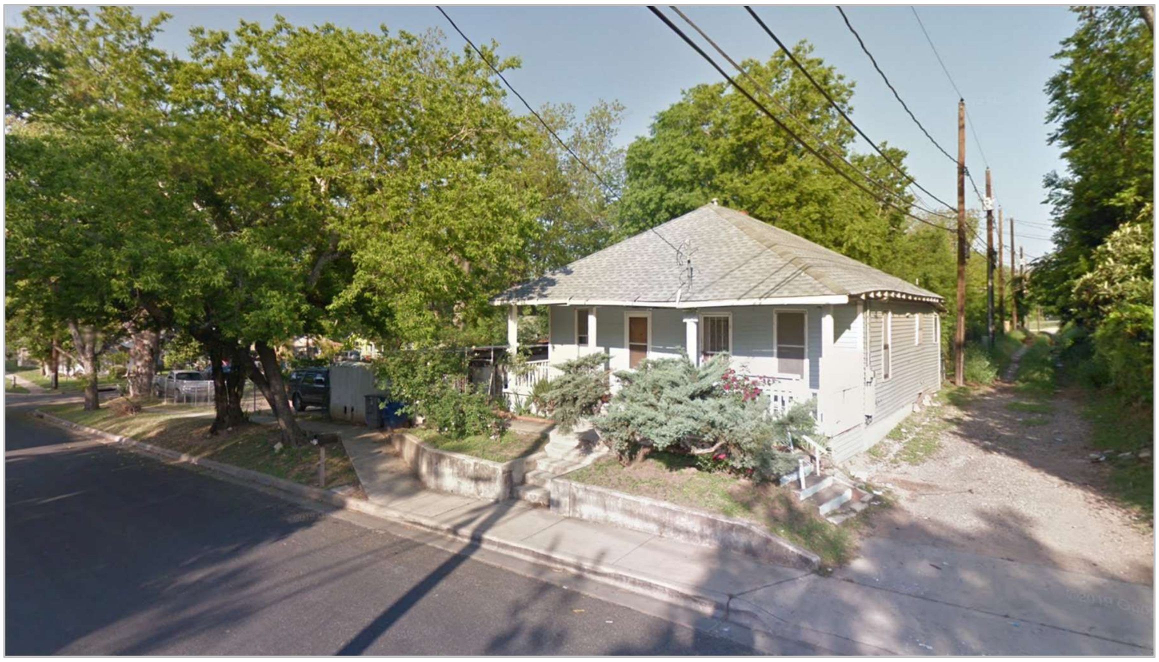
Figure 11: 2001 Willow Street, circa 2022

Note: Image shows the two new units on the lot: unit 2 (1,036 square feet) in the front and unit 1 (1,738 square feet) in the back. Retrieved from Google Street View.

Example two is 2214 Garden Street. This property also contains two units, each owned by a different individual. One unit owner maintains a 57.6% interest in the common areas and the other unit owner maintains a 42.4% interest in the common areas. When analyzing this property's history, it is evident that the original 952 square foot structure was maintained and an additional 3,396 square foot unit was added.[10] Figure 12 shows the lot pre-development. The original unit faces the "side street" (Mildred St), and has a large driveway/yard space along the main street (Garden St). In August of 2018, the property was listed for sale on Zillow for $395,000. Images from 2019 (Figure 13) show the unit being renovated. In the beginning of 2020, permits were filed and approved for a "secondary apartment" on the property. A year later, the owners establish a condominium regime property, turning the original unit into unit 1, and the new unit into unit 2. The new unit, unit 2, is sold in less than a month, while the original unit does not appear to be sold. Per TCAD, the appraised value for the new unit is $1,045,673, and the appraised value for the original unit is $598,877. Figure 15 shows the original unit in the foreground, and the new unit in the background.

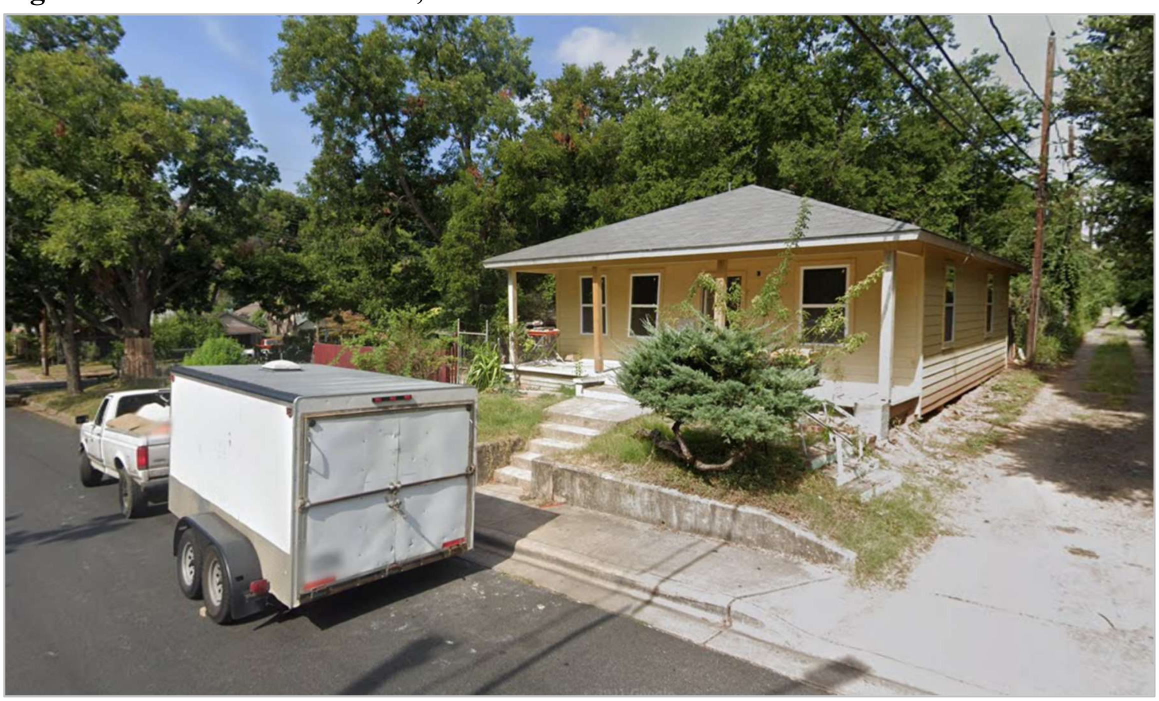
[10] All property information is retrieved from the City of Austin's Property Profile tool (https://maps.austintexas.gov/GIS/PropertyProfile/), the City of Austin's permitting data (https://data.austintexas.gov/Building-and-Development/Issued-Construction-Permits/3syk-w9eu/data), and Travis County's Clerk Web Search (https://www.tccsearch.org/).

Figure 12: 2214 Garden Street, circa 2011



Note: Image shows the original 952 square foot unit facing Mildred Street. The large side yard contains a driveway that faces Garden Street. Retrieved from Google Street View.

Figure 13: 2214 Garden Street, circa 2019



Note: Image shows the original unit being renovated in 2019. Image retrieved from Google Street View.

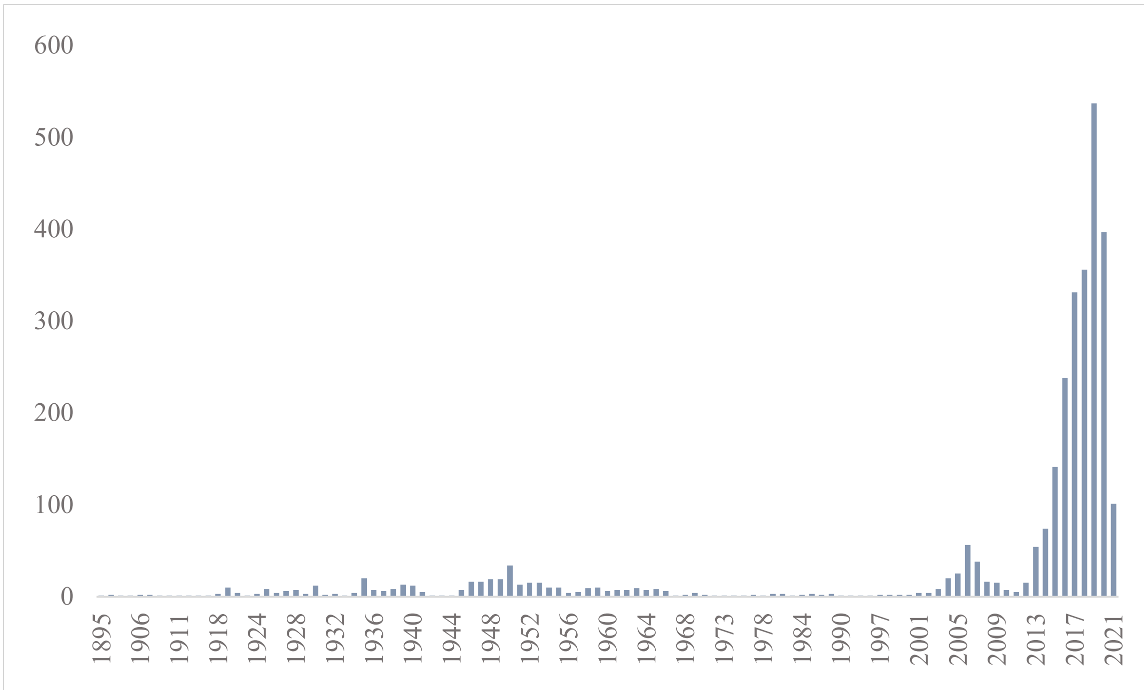
Figure 14: 2214 Garden Street, circa 2022

Note: Image shows the original unit (unit 1) renovated, and a new unit (unit 2) in the side yard facing Garden Street. Image retrieved from Google Street View.

It is difficult to determine how many properties are complete redevelopments (like example one) versus unit additions (like example two). One way to guess is to look at the year the units were built. Prior to 2000, 455 units were built. It could be assumed that these are original units still standing on the properties. This means about 31% of the small-scale detached condominium properties contain an original unit, and nearly 70% may be full redevelopments. However, when looking at units that experienced a complete remodel (such as unit 1 in example two), their year built field in TCAD is updated to the year of the remodel. For this reason, the estimates on original units still standing may be low. Additionally, this is not an accurate way to measure original homeowners that are still in place; developers or other outside entities may choose to keep the original home intact if it is in good condition and placed well on the property.

When further analyzing the year these units were built, it is evident there is a large increase in 2016 (see Figure 15). This is mostly likely the result of the City of Austin's ordinance changes the year prior. The median year built of these units is 2017.

Figure 15: Condominium Units (Part of 2-Unit Detached Condominium Properties) by Year Built

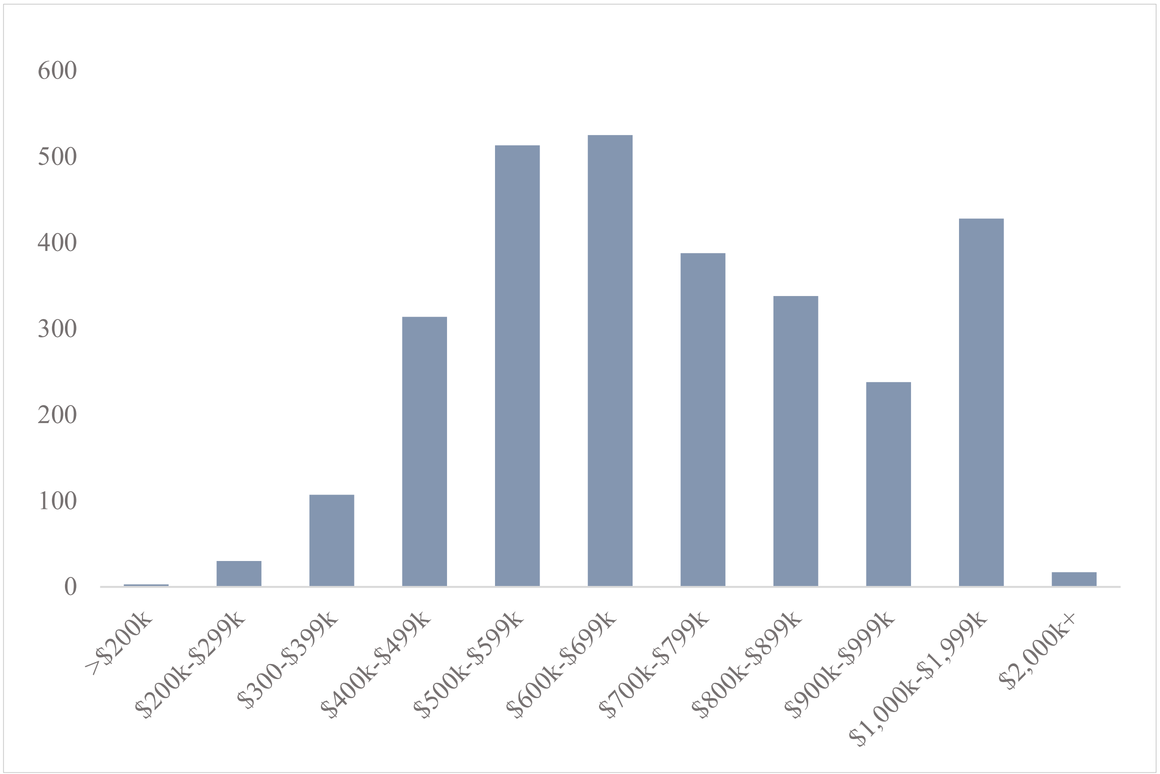


Note: Condominium data are retrieved from the Travis County Appraisal District.

The values of these units range from $163,805 to $2,957,515, with the median value at $692,246. This is nearly 21% greater than the median value of all detached condominium units, and 26% greater than the median home sales price for Travis County. Despite the increase in value, the units are not larger when comparing them to all detached condominium units: the median size for these units is 1,140 square feet while the median size for all detached condominium units is 1,781 square feet.

One explanation for the high value but small size of these units is that many of them are located in central Austin neighborhoods. These neighborhoods tend to be highly desirable, with high land prices, and the parcels tend to be smaller (sometimes with an already-existing home on the lot that the new unit has to be built behind), limiting unit size. As mentioned in Chapter 2, these units tend to be built as part of redevelopment schemes. Experienced developers are able to produce two high-quality units in these neighborhoods that can sell for high prices. All of these factors lead to these price differences when comparing these units to all detached condominium units. Figure 16 shows the range of property values for detached condominiums that are a part of the small-scale regimes.

Figure 16: Condominium Units (Part of 2-Unit Detached Condominium Properties) by TCAD Estimated Market Value



Note: Condominium data are retrieved from the Travis County Appraisal District.

When comparing the values of these units and median family incomes, it is evident they are largely unaffordable. With a median family income of $112,192[11] at the county level, it is suggested to not spend more than $336,576 on a home. The median value of these units is nearly double this suggested home price, indicating that these units may be out of reach for a typical family household. Only 48 units (or less than 2% of units) fall at prices affordable to those making less than the median family income. Around 12% of units fall at prices affordable to those making 1 to <1.5x the median family income. Around 30% of units fall at prices affordable to those making 1.5 to <2x the median family income. And 56% of units fall at prices only affordable to those making 2x the median family income. Table 4 highlights this analysis, focusing on the income needed for different property values. This affordability analysis furthers the argument that the City of Austin's affordability goals within their updated ADU ordinances are not achieved.

Table 4: Affordability Analysis of Condominium Units (Part of 2-Unit Detached Condominium Properties)

Unit Cost in Relation to MFI	Number of Units	As Percent of Total Units	Property Value (Low)	Property Value (High)	Income Needed (Low)	Income Needed (High)
<1	48	2%	$163,805	$324,457	$54,602	$108,152
1 to <1.5x	357	12%	$328,600	$490,521	$109,533	$163,507
1.5 to <2x	870	30%	$490,767	$654,330	$163,589	$218,110
2x+	1624	56%	$654,388	$2,957,515	$218,129	$985,838

Note: Condominium data are retrieved from the Travis County Appraisal District.

[11] U.S. Census Bureau, American Community Survey 2021 1-year estimates

Lastly, these units can be analyzed by tax exemptions to begin to paint a picture of *who* occupies these units. About 60%, or 1749 units receive a homestead exemption, indicating they are occupied by those who own the unit. The other 40% may be rented out by the unit owner, or the homeowner may be unaware of the homestead exemption. In addition to this, 77 units receive an "Over 65" exemption, 3 units receive a "Disabled Persons" exemption, and 18 units receive a "Disabled Veteran" exemption. These populations are more likely to be on fixed incomes, making them more vulnerable to increased housing costs and displacement. The ADU model can be a good solution for these individuals: perhaps they are the original owners of the lot and built a second unit to sell to be able to generate additional money and stay in place, or perhaps they bought the unit from a family member or friend to have a more affordable place to stay. It is also possible they just bought the unit off the market. Either way, the ADU model presents a potential solution for vulnerable populations looking to stay in place.

Chapter 4: Financial Analysis

The following scenarios evaluate three different types of developers that could pursue the model of building an ADU to sell: a (1) for-profit developer, a (2) non-profit developer, and a (3) homeowner as the developer. In each scenario, the original homeowner would stay in place, and the developer would build an ADU in the backyard to sell.

Scenario 1, the for-profit developer, is usually presented as a "we will buy your backyard" or "we build ADUs" scheme. A quick google search presents several developers pursuing this model in the Austin area. This approach would be "hands-off" for the original homeowner. The for-profit developer would tackle the entire project, i.e. financing, construction, establishing the condominium regime, and selling the new unit. The profit from the sale of the new unit would be used to compensate the homeowner for giving up partial use of their land (aka "selling off" their backyard), and to pay out the for-profit developer.

It is unclear if scenario 2, the non-profit developer, has been pursued locally[12]. Theoretically this process would be similar to the beforementioned scenario in that the non-profit developer would handle all aspects of the project, except at lower costs and with potential subsidies. Recently, the state of California approved the selling of ADUs through non-profits (Hart, 2021). With this, the sale of ADUs is now allowed statewide.

[12] Local non-profits have supported homeowners looking to build ADUs to rent or house family and friends. Additionally, the Guadalupe Neighborhood Development Corporation has built ADUs on properties it owns. But it remains unclear if local nonprofits have supported homeowners looking to build ADUs to sell.

Scenario 3, the homeowner as the developer, entails the original homeowner building and selling the ADU themselves. They would navigate the process including forming a condo regime, financing, hiring subcontractors as needed, filing permits, etc.

The goal of this analysis is to highlight the rough differences in costs, as well as the advantages and disadvantages of each type of developer. The financial model assumes certain conditions for ADU development that may not be realistic for every Austin property, but these conditions are used for simplicity's sake:

- The property meets all ADU minimum requirements, i.e. no rezonings or variances are necessary.
- The property has a non-challenging terrain, i.e. it is not sloped, and it contains no heritage trees[13].
- The ADU is built to maximum size of 1,100 square feet (the limit under current regulations).
- The ADU is able to share a water meter with the original home.
- The original home is in decent/nice condition with yard upkept, in a centrally located neighborhood.

It is important to note that any of these conditions not being met can affect the feasibility of the entire project. For example, a heritage tree could be in the center of the backyard, making development impossible. Or the water meter may not be able to be shared between both units, increasing costs by upwards of $30,000, causing the finances

[13] The City of Austin has a heritage tree ordinance, impacting a property owners' ability to remove certain trees. For removal, a variance is usually required and must meet specific approval criteria.

to not work out. Each property is different and many unforeseen factors can appear that impact the feasibility of a real project.

For this model we assume that a 1,100 square foot ADU is to be built. Construction costs are estimated at $225 per square foot, with a 5% discount for the non-profit and homeowner developers assuming they spend less on finishes, producing a more basic housing option. Labor and materials costs are the same otherwise. Soft costs are estimated to be 13% on top of construction, including architectural services, engineering, city permitting fees, property surveying, and establishing the condominium regime. To build the unit, it is typical for the developer to take out a loan. The loan interest rate is set at 8% for each scenario for simplicity and is included in the model as carrying cost (or holding costs). The for-profit and non-profit developers would typically obtain a construction loan, while a homeowner would obtain a home equity lines of credit (HELOCs) or utilize cash-out refinancing.

Depending on the type of developer, the developer fee changes: for-profit developers are expected to charge a fee of at least 20% which includes overhead and profit, while non-profit developers are expected to charge a fee of 15% for just overhead. If the original homeowner is the developer then there is no fee and they would pocket all the sales revenue from the sale of the new unit. The estimated sales price of the new unit in the for-profit developer scenario is $500,000, assuming the condominium regime is established in a centrally located neighborhood. This number is slightly less in the non-profit and homeowner as developer scenarios, assuming they spend less on finishes and produce a unit of slightly lower quality. The closing costs that cover real estate commissions, legal fees, title fees, and more is estimated to be 8% of the estimated sales price. These numbers are all estimates to illustrate the model, numbers for real projects may vary significantly. All sources for these estimates are provided in the appendix. A description of methods is included in Chapter 1.

Scenario 1: For-Profit Developer as the Developer

The total cost for a for-profit developer to build an ADU is estimated at $392,120. This includes $302,493 for construction and soft costs, and $89,627 in developer fees. These fees cover the developer's expenses including time and services, overhead costs like office space or additional staff, and additional profit for company owners. The estimated sales price of the unit is $500,000, and after closing costs of 8%, or $40,000, the sales price becomes $460,000. If we subtract total costs from this, the expected profit for a homeowner is $67,880. Table 5 shows these calculations. A full financial model is provided in the appendix.

Table 5: Financial Model for Development of an ADU Using a For-Profit Developer

Construction + Soft Costs	$302,493
Developer's Fee	$89,627
Total Cost	**$392,120**

Unit Sales Price	$500,000
Closing Costs	$40,000
Final Unit Sales Price	**$460,000**

Profit for Original Homeowner	**$67,880**

Note: Model number are estimates. Data are retrieved from interviews with developers and internet searches. A full financial model is provided in the appendix.

When analyzing this scenario, the developer's fee is on the lower end of what they would want to make.[14] Typically with a sales price of $500,000, they want to see a minimum of $100,000 for their time, energy, and money spent on a project like this one. Additionally, the sales price assumes the unit is in a centrally located, upkept neighborhood. With lower sales prices, the project becomes less worthwhile for developers. At the same time, the homeowner may not be satisfied with the outcomes. Their profit of $67,880 may seem significant, especially considering they did not have to produce the unit; however, this is a low amount when factoring in that they had to deal with at least six months of construction disruptions on their property, and giving up ownership of their backyard space forever. It's also important to consider that unexpected factors can increase costs of development. This could eat away at both the developer and the homeowner profits, making both parties unsatisfied with the deal.

Scenario 2: Non-Profit Developer as the Developer

The total cost for a non-profit developer to build an ADU is estimated at $349,150. This includes $287,849 for construction and soft costs, and $61,301 in developer fees. Construction costs are lower than scenario 1 because we are assuming they are spending less on finishes. These fees cover the developer's expenses including time and services, and overhead costs like office space or additional staff. There is no additional profit for company owners. This is why fees are able to be lower than scenario 1. The estimated sales price of the unit is $475,000, and after closing costs of 8%, or $38,000, the sales price

[14] Per personal communication with developers.

becomes $437,000. The sales price is lower than in scenario 1 because of the more-basic quality of finishes. If we subtract total costs from this, the expected profit for a homeowner is $87,850. Table 6 shows these calculations. A full financial model is provided in the appendix.

Table 6: Financial Model for Development of an ADU Using a Non-Profit Developer

Construction + Soft Costs	$287,849
Developer's Fee	$61,301
Total Cost	**$349,150**

Unit Sales Price	$475,000
Closing Costs	$38,000
Final Unit Sales Price	**$437,000**

Profit for Original Homeowner	**$87,850**

Note: Model number are estimates. Data are retrieved from interviews with developers and internet searches. A full financial model is provided in the appendix.

This model shows a more ideal outcome than scenario 1 for the original homeowner. Their profits earned from "selling their backyard" would better reflect how they value their backyard. The non-profit developer's fee reflects the maximum they would be able to charge in a multifamily development subsidized by Low Income Housing tax Credits; however, this model does not currently include subsidies. This non-profit developer's fee may be low considering that non-profit developers currently do not have knowledge of this process, i.e. there will be growing pains associated with learning this knowledge and applying it to real projects, most likely increasing project costs and requiring staff overtime. Because subsidies are not currently included in the model, non-profit developers may be able to charge above the 15% fee as needed. But if subsidies are included, project costs will be reduced and the idea of affordable housing solutions could be explored.

Scenario 3: Homeowner as the Developer

The total cost for a homeowner to build an ADU is estimated at $287,849. This only includes $287,849 for construction and soft costs, and no cost in developer fees. Construction costs are lower than scenario 1 because we are assuming they are spending less on finishes, similarly to scenario 2. And total costs are significantly lower than both scenario 1 and 2 because there is no developer fee: the homeowner is producing the unit themselves. The estimated sales price of the unit is $475,000, and after closing costs of 8%, or $38,000, the sales price becomes $437,000. The sales price is lower than in scenario 1 because of the more-basic quality of finishes, similarly to scenario 2. If we subtract total costs from this, the expected profit for a homeowner is $149,151. Table 7 shows these calculations. A full financial model is provided in the appendix.

Table 7: Financial Model for Development of an ADU Using Original Homeowner as the Developer

Construction + Soft Costs	$287,849
Developer's Fee	$0
Total Cost	**$287,849**

Unit Sales Price	$475,000
Closing Costs	$38,000
Final Unit Sales Price	**$437,000**

Profit for Original Homeowner	$149,151

Note: Model number are estimates. Data are retrieved from interviews with developers and internet searches. A full financial model is provided in the appendix.

The homeowner as the developer is the most ideal scenario in terms of maximizing the homeowner's profit. They would be able to avoid any developer's fee and seek the full profits from their unit sale. This scenario is also ideal because the homeowner does not have to follow through with selling the unit immediately if they do not wish to. They could potentially rent the ADU out, house family members or friends, use it as a short term rental, or use it themselves. Because a condominium regime has been established, they will still have the ability to sell it later if they choose.

A drawback to this scenario is that it is the most difficult scenario for an average homeowner to pursue. They must seek funding for the development of the ADU (challenges related to this are presented in Chapter 2). They must also build and sell the unit, a seemingly impossible task for anyone unfamiliar with real estate, and still challenging even for those with real estate experience. Having an unexperienced developer increases the project's risk of delay and increase in costs, which would eat into the expected profits. Having more experienced developers, such as for-profit or non-profit ones, helps reduce these risks.

Chapter 5: Conclusion

Findings and Discussion

As the demand to live in Austin and the population increases, the cost of housing follows suit. When these housing costs are increasing at much greater rates than income, housing becomes unaffordable for many. For homeowners, this could mean being displaced, especially for vulnerable homeowners in the Eastern Crescent. One potential solution that has been explored to help homeowners stay in place and capitalize on their existing assets is for them build an ADU on their property. This allows them to utilize their property to generate money from either leasing out or selling the ADU.

This report finds through a literature review that building ADUs to be used for rental income is an unsustainable model for low- and moderate-income homeowners. Many homeowners do not meet the requirements for financing and/or do not know how to navigate the process of building an ADU and act as a property manager. Many cities have proposed and implemented strategies or policies to mitigate these challenges; however, no city has produced a scalable model.

The model of building an ADU to sell has been mostly unexplored in current literature. It is unclear whether this model has been pursued in other states, but it does seem that California has allowed for non-profit developers to engage in this process (Hart, 2021). In Austin, the model appears to be more widely pursued by for-profit developers in redevelopment schemes rather than by non-profit developers or homeowners themselves. Usually when a for-profit developer is involved, it seems that the original home on the property is demolished to make room for two new units that can sell at much higher prices.

While new housing production is beneficial, this specific model contradicts the City of Austin's goal of increasing affordable housing development.

As of 2022, approximately 1,526 sites exist where single family lots were turned into condominium regimes (i.e. ADUs were added to the property and sold, or the original unit was demolished and two units were added and sold separately). This equates to 3,052 condominium units in total. Many of these units are in neighborhoods located close to downtown and zoned SF-3, such as the east side, immediately south of the river, and north of the University of Texas at Austin's campus. The vast majority of these units were built after 2016, seemingly after the City of Austin updated its ADU ordinances. The prices of these units remain high and unaffordable for many Austinites, with the median value at $692,246.

When exploring the financial models associated with this type of development, it is evident that a homeowner would make the most profit by building and selling an ADU themselves. But for many this can be a difficult and sometimes impossible task, given the amount of time and resources (especially financial) needed. Similarly to producing an ADU to rent out, many barriers are present for existing homeowners especially for low- and moderate-income homeowners. In the scenario where a homeowner "sells their backyard" to a for-profit developer, the process can be a lot more streamlined. The for-profit developer would handle the process of building and selling the ADU, but they would do so for a fee. After the fee is factored into costs, the homeowner may feel like they are not being compensated fairly for "selling their backyard". Another scenario explored would be for a non-profit developer to handle the process for the homeowner. They would be able to do so at a lower fee than a for-profit developer. Currently, it is unknown if any non-profit developers are pursuing this model, meaning they would have to grow their knowledge in this area, which can lead to unexpected costs that eat into profits. As such, each scenario has advantages and challenges that need to be considered when conducting real projects. It's also important to note that these scenarios are illustrated through near-perfect property conditions, meaning different factors can come into play that can drastically alter the cost and feasibility of the project.

Further Research

It is recommended that the literature on this subject of building ADUs to sell should be expanded. For one, more research should be conducted on models in other cities, specifically if other places allow for the sale of ADUs and the local impacts. Additionally, the specific impacts of this model in Austin could be further explored. For example, one could produce a case study on how a specific neighborhood has changed since the implementation of condominium regimes (some neighborhoods have been inundated with this model). Aspects such as affordability, impervious cover, infrastructure investments, and community sentiment (of long term residents) could all be explored. Lastly, the financial models could be built upon. One could analyze the effects of subsidies on the models, and/or analyze common financial challenges that arise to test project feasibility.

Final Recommendations

What is evident from this report is that for-profit developers are the main players in the model of creating ADUs to sell. Therefore the first recommendation is for the city to

produce educational materials that would encourage non-profit developers and homeowners to pursue this model and help streamline the process for them. This could include:

- A step-by-step guide for building ADUs to sell including the legality of the model, finding financing, estimating costs, hiring subcontractors, and the selling process;
- A draft legal document that can be filled out and used to file the Declaration of Condominium at the county level; and
- Low-cost, prefabricated ADU designs to reduce design costs.

A second recommendation is to **make funds available for ADU development in order to reduce financial barriers to non-profit developers and homeowners** looking to pursue this model. The California Housing Finance Agency has an ADU Grant Program that provides grants of up to $40,000 for homeowners seeking to build ADUs to put towards predevelopment and closing costs (California Housing Finance Agency, n.d.). Funds such as these would be instrumental in helping produce units on properties where development is otherwise impossible due to increased costs (i.e. the money originally going towards these costs in the project can go towards solving challenges that arise such as project delays or unforeseen issues). Alternatively, affordability requirements could be tied to these funds. This could potentially allow for the ADU to be sold at a more affordable price, while allowing the original homeowner to stay in place.

Appendix: Financial Models

Scenario 1: For-Profit Developer

This model roughly estimates the cost and profits for a for-profit developer to build and sell an ADU in a homeowner's backyard. Expected profits for the original homeowner are included as well. Descriptions and sources for each input is provided on page 67.

	Total
land	$0
demolition	$0
construction	$247,500
design/architect	$23,686
survey	$1,200
permitting	$2,700
declaration of condo	$5,000
carrying costs	$22,407
Total Cost	**$302,493**
Sales Price	**$460,000**
estimated sales price	$500,000
closing costs	$40,000
Expected Profit	$157,507
developer fee/cut	$89,627
homeowner cut	$67,880

Assumptions	
# of units	1
unit size (SF)	1100

Hard cost	
acquisition	$0
construction (SF)	$225

Soft Costs	
design/architect	10%
survey	$1,200
permitting	$2,700
declaration of condo	$5,000

Operational Costs	
carrying costs- interest rate	8%
closing costs	8%

Developer Fee	
overhead + profit	20%

Scenario 2: Non-Profit Developer

This model roughly estimates the cost and profits for a non-profit developer to build and sell an ADU in a homeowner's backyard. Expected profits for the original homeowner are included as well. Descriptions and sources for each input is provided on page 67.

	Total
land	$0
demolition	$0
construction	$235,125
design/architect	$22,501
survey	$1,200
permitting	$2,700
declaration of condo	$5,000
carrying costs	$21,322
Total Cost	**$287,849**
Sales Price	**$437,000**
estimated sales price	$475,000
closing costs	$38,000
Expected Profit	$149,151
developer fee/cut	$61,301
homeowner cut	$87,850

Assumptions	
# of units	1
unit size (SF)	1100
Hard cost	
acquisition	$0
construction (SF)	$214
Soft Costs	
design/architect	10%
survey	$1,200
permitting	$2,700
declaration of condo	$5,000
Operational Costs	
carrying costs- interest rate	8%
closing costs	8%
Developer Fee	
overhead	15%

Scenario 3: Original Homeowner as the Developer

This model roughly estimates the cost and profits for a homeowner to build and sell an ADU in their backyard. Descriptions and sources for each input is provided on page 67.

	Total
land	$0
demolition	$0
construction	$235,125
design/architect	$22,501
survey	$1,200
permitting	$2,700
declaration of condo	$5,000
carrying costs	$21,322
Total Cost	**$287,849**
Sales Price	**$437,000**
estimated sales price	$475,000
closing costs	$38,000
Expected Profit	$149,151
developer fee/cut	$0
homeowner cut	$149,151

Assumptions

# of units	1
unit size (SF)	1100

Hard cost

acquisition	$0
construction (SF)	$214

Soft Costs

design/architect	10%
survey	$1,200
permitting	$2,700
declaration of condo	$5,000

Operational Costs

carrying costs- interest rate	8%
closing costs	8%

Developer Fee

n/a	0%

Inputs for Financial Models

Land, Acquisition, and Demolition Costs: these costs are set to $0. The land is already owned and the ADU is to be placed in the backyard.

Unit Size: set to 1,100 square feet. This is the maximum unit size for an ADU per City of Austin regulations.

Construction Costs: set to $225 per square foot. Information retrieved from https://estimationqs.com/building-costs-per-square-foot-in-the-city-of-austin-tx-usa/ and https://seedpropertygroup.com/blog/housing-101-austin-home-building-cost and informed via interviews with developers.

Design/Architecture Fees: set to 9.57%. Information retrieved from https://architects.promatcher.com/cost/austin-tx-architects-costs-prices.aspx.

Surveying Costs: set to $1,200. Information retrieved from local surveying companies.

Permitting Fees: set to $2,700. Information retrieved and calculated from https://www.austintexas.gov/sites/default/files/files/Development_Services/Fees_Residential.pdf.

Declaration of Condominium Costs: set to $5,000. This includes hiring attorneys to draft the condominium regime documents (highly recommended) and file at the county level. Information retrieved via interviews with developers.

Carrying Costs: includes the loan interest rates, assumed to be 8%. Construction loan information retrieved via interviews with developers and HELOC loan information retrieved from https://www.usbank.com/home-loans/home-equity/home-equity-rate-and-payment-calculator.html.

Estimates Sales Price: assumed at $500,000. Information retrieved via interviews with developers.

Closing Costs: estimated at 8% of the estimated sales price for the seller. Information retrieved from https://www.simpleshowing.com/blog/how-much-are-closing-costs-for-sellers-in-texas.

Developer Fees: estimated as 20% for for-profit developers and 15% for non-profit developers. Information retrieved via interviews with developers.

Bibliography

Austin Board of Realtors. (2022). *Cental Texas Housing Market Report: September 2022.* Austin.

Burton, R. D. (2020). Texas Site Condominiums. *31st Annual Advanced Real Estate Drafting Course.* Dallas: State Bar of Texas.

Cabrera, J. F., & Najarian, J. C. (2013). Can New Urbanism Create Diverse Communities? *Journal of Planning Education and Research*, 427-441.

California Housing Finance Agency. (n.d.). *ADU Grant Program* . Retrieved from California Housing Finance Agency: https://www.calhfa.ca.gov/adu/

Chapple, K., Wegmann, J., Mashhood, F., & Coleman, R. (2017). *Jumpstarting the Market for Accessory Dwelling Units: Lessons Learned from Portland, Seattle, and Vancouver.* The Terner Center for Housing Innovation.

City of Austin. (n.d.). *Accessory Dwelling Units*. Retrieved from austintexas.gov: https://www.austintexas.gov/page/accessory-dwelling-units

City of Austin, Planning & Zoning Department. (2016, September). *Guide to Zoning.* Retrieved from https://www.austintexas.gov/sites/default/files/files/Planning/zoning_guide.pdf

Fannie Mae. (2022, October 5). *Selling Guide*. Retrieved from Fannie Mae: https://selling-guide.fanniemae.com/Selling-Guide/Origination-thru-Closing/Subpart-B4-Underwriting-Property/Chapter-B4-2-Project-Standards/Section-B4-2-1-General-Project-Standards/1082981071/B4-2-1-02-Waiver-of-Project-Review-08-07-2019.htm

Hart, M. (2021, December 15). *New law to allow ADUs to be sold separately from main residence*. Retrieved from firsttuesdayJournal: https://journal.firsttuesday.us/new-law-to-allow-adus-to-be-sold-separately-from-main-residence/81132/

HousingWorks Austin. (2022). *Austin City Council District-by-District Analysis 2021.* Austin.

Johnson, J. S., & Talen, E. (2010). Affordable housing in New Urbanist Communities:. *Housing Policy Debate*, 583–613.

Ramsey-Musolf, D. (2018). Accessory Dwelling Units as Low-Income Housing: California’s Faustian Bargain. *Urban Science*.

Redfin. (2022, October 13). *Rental Market Tracker: Rents Are Growing Half as Fast as They Were Six Months Ago*. Retrieved from Redfin: https://www.redfin.com/news/redfin-rental-report-september-2022/

Root Policy Research. (2020). *City of Austin Comprehensive Housing Market Analysis.* Denver: Root Policy Research.

Texas A&M University. (2022, September). *Housing Activity for Austin (Austin BoR)*. Retrieved from Texas Real Estate Research Center: https://www.recenter.tamu.edu/data/housing-activity/#!/activity/Local_Market_Area_(LMA)/Austin_(Austin_BoR)

The University of Texas at Austin. (2018). *Uprooted: Residential Displacement in Austin's Gentrifying Neighborhoods and What Can Be Done About It.* Austin.

The University of Texas Center for Sustainable Development. (2008). *Working Paper Series: The Alley Flat Initiative.* Austin.

The Urban Institute. (2020). *Designing Accessory Dwelling Unit Regulations.* Washington, DC.

Travis County. (2022). *Travis County*. Retrieved from County Clerk Web Search: https://www.tccsearch.org/

U.S. Census Bureau. (2020). *2016-2020 American Community Survey 5-year estimates for Austin MSA*. Retrieved from SocialExplorer.

U.S. Census Bureau. (2021). *2021 and 2011 American Community Survey 1-year estimates for Austin MSA*. Retrieved from SocialExplorer.

University of Texas at Austin. (2021). *Austin Housing Analysis*. Retrieved from https://storymaps.arcgis.com/collections/b1d4ecbe56d1427691045ca6b975db79

Valenzuela, J. (2018). *New Compact Communities: Detached Condominium Projects in Austin, Texas.* The University of Texas at Austin.

Wegmann, J. (2016). *Strategies to Help Homeowners Finance Accessory Dwelling Units in Austin.* Austin.

Vita

Kaileen McHugh grew up in Southwest Florida and graduated with a Bachelor of Science in Economics from The Florida State University. After undergrad she served in the AmeriCorps VISTA program in Indianapolis as an Economic Development Coordinator. She then enrolled in the Community and Regional Planning program in the fall of 2020. During her time in graduate school, Kaileen focused on topics related to economic development and affordable housing. Feel free to contact Kaileen in regard to this research.

Permanent email: kmchugh@utexas.edu

This report was typed by the author