July 2024

Not So Gentle Density: An Early Assessment of the San Diego Bonus ADU Program

Jake Wegmann, Karen Chapple, Andrew Wofford, Li-Ping Lee, Annie Flom, Victoria Beckley, Holly Armstrong

Executive Summary

In 2020, the City of San Diego launched a first-of-its-kind program to spur the development of affordable missing middle housing. Known as the "Bonus ADU Program," it allows property owners and developers to build "bonus" accessory dwelling units (ADUs) in addition to the two ADU units currently allowed by state law.[1] Importantly, property owners can build a bonus unit and rent it at market rate only if they pair it with an income-restricted, affordable unit. These deed-restricted units must be capped at rents for 110% of area median income (AMI) over 15 years, or 80% of AMI over 10 years.

This report highlights the program's unexpected success in unlocking large-scale, affordable developments – several of which will create more than 100 units once completed. Our preliminary research indicates that the San Diego Bonus program is startling in its permissiveness, perhaps more so than any small lot redevelopment zoning reform anywhere in the United States. The program has expanded the concept of the ADU, typically envisioned as a single garage unit or "granny flat", into an entirely new type: multifamily apartment buildings (or "granny towers").[2] While the typical backyard ADU is developed by a homeowner living on the property to gain additional rental income, the typical Bonus ADU has an entirely different business model. Developers are buying existing single-family homes and duplexes on suitable lots and adding large numbers of units while operating them as rental housing.

Crucially, the program builds upon previous advancements in state law which have required by-right approval for ADUs and eliminated parking minimums within Transit Priority Areas (TPAs). By allowing unlimited Bonus ADUs on any site located in a TPA, without a parking requirement, San Diego officials have created one of the most effective missing middle housing reforms in the country. As of February 2024, nearly 1,300 units have been proposed under the program, 488 of which have entered into a recorded agreement with the city.[3]

Still, our research indicates notable barriers that the city should address. Certain development costs – particularly the high costs of required utility upgrades – can jeopardize the financial feasibility of smaller-scale Bonus ADU projects. These costs can be as high as $150,000 for projects producing 4-10 units, which likely prohibits existing low- and moderate-income homeowners from utilizing the Bonus ADU program. Meanwhile, the program has succeeded in producing significant new supply for moderate-income households, but it has not produced low-income units. So far, every developer who has utilized the bonus program has opted to restrict its affordable units to 110% of AMI, rather than 80% of AMI.

---

1 State law permits the construction of one attached JADU and one detached ADU on any eligible parcel. The law also permits a conversion of an existing structure, such as a garage, which would allow three ADUs under certain circumstances.

2 The term "granny tower" was first coined by opponents of the Bonus ADU program to describe the two- and three-story ADU developments permitted by the program. For more coverage of the program's opponents, see Ben Christopher's article in Cal Matters.

3 Internal data on Bonus ADU program, San Diego Housing Commission.

Key Recommendations

- *Implement an additional density incentive for projects that produce units affordable for low-income residents (at or below 80% AMI).*
- *Identify ways to lower utility upgrade costs, such as the original draft of [SB1210](SB1210) – proposed by Senator Skinner – which would cap utility costs at 1% of a new unit's building permit value.*[4]
    - *Consider capping utility upgrade costs at a lower rate for projects that target deeper affordability levels.*
- *Incentivize community development corporations (CDCs), community land trusts (CLTs) and other community-based organizations to utilize the Bonus ADU program by making pre-development funds available to qualified nonprofits.*
- *Explore other possible incentives to create more 3- and 4-bedroom units for large families.*
    - *Waive development impact fees for projects that produce large-family ADUs restricted at or below 80% AMI.*
    - *Increase the ratio of allowable bonus, market rate ADUs for large family, affordable units. For example, the program could allow 1.5 market rate ADUs for every 3-bedroom affordable unit, and 2 market rate ADUs for every 4-bedroom affordable unit.*

Our research was informed by preliminary approval data, pro forma analysis and interviews with city officials, advocates and developers. This policy brief begins with an overview of the program, followed by our key findings and recommendations moving forward. It is part of a more extensive study – to be published later in 2024 – examining the feasibility of expanding the San Diego Bonus ADU program statewide.

Introduction

In 2020, the City of San Diego launched a first-of-its-kind program to spur the development of affordable missing middle housing. The concept of missing middle housing refers primarily to small-scale multifamily housing (ADUs, duplexes or small apartment buildings), but it can also refer to housing that serves middle-income residents.[5] In the case of San Diego, city officials have created a program that successfully meets both definitions of the term – known as the "Bonus ADU Program," it not only adds additional small-scale housing, but it also requires that half of that housing be restricted to moderate- or low-income residents.[6]

The program allows property owners and developers to build "bonus" ADUs in addition to the two ADU units currently allowed by state law. Importantly, property owners can build a bonus unit and rent it at market-rate only if they pair it with an income-restricted, affordable unit. These deed-restricted units must be capped at rents for 110% of AMI over 15 years, or 80% of AMI over 10 years.

This report highlights the program's unexpected success in unlocking large-scale, affordable developments – several of which will create more than 100 units once completed. After an overview of the background of the program, we describe program outcomes in terms of numbers, affordability, and

4 As of May 2024, this bill has been amended and no longer includes the 1% cap; however, legislators should continue to evaluate possible caps for utility connection costs.

5 Parolek, Daniel, "What is Missing Middle Housing?", 2023.

6 Alameldin, Muhammad, "San Diego's Surprising Success in Spurring Missing Middle Housing: The Accessory Dwelling Unit Bonus Program," Terner Center, 2024.

size of units. The next two sections examine financial feasibility and location of the units. A conclusion provides recommendations for policymakers.

How the Bonus ADU Program Works:

- On any residential property in the city – including parcels zoned as mixed-use residential – property owners can build at least two bonus ADUs in addition to the two ADUs already permitted by state law.
- Bonus ADUs, like base ADUs, are permitted ministerially, or "by-right," meaning that there is no discretionary review process.
- Each market-rate bonus ADU must be paired with an affordable ADU, restricted to rent limits based on 110% or 80% of AMI. A unit restricted at 110% AMI must remain affordable for 15 years, while a unit restricted at 80% AMI must remain affordable for 10 years.
- Unlimited Bonus ADUs are permitted on properties located in a Transit Priority Area (TPA) – defined as any area within a half-mile of a major transit stop.
- Within TPAs and elsewhere, developers must conform to existing standards such as floor area ratio (FAR), lot coverage and height limits.
- Any Bonus ADU project that nets 10 or more new units must deed restrict one unit as affordable to residents at or below 50% AMI or pay an inclusionary housing fee.
- The San Diego Housing Commission (SDHC) completes income verification and ongoing monitoring for deed-restricted units, at a cost of $150 per unit.

Program Background and Expectations

The Bonus ADU Program is part of San Diego's ongoing efforts to harness statewide ADU reforms. Since 2017, staff in the Planning Department and Development Services Department had been observing ADU production and identifying possible barriers that led to higher costs, slower permitting and fewer units.

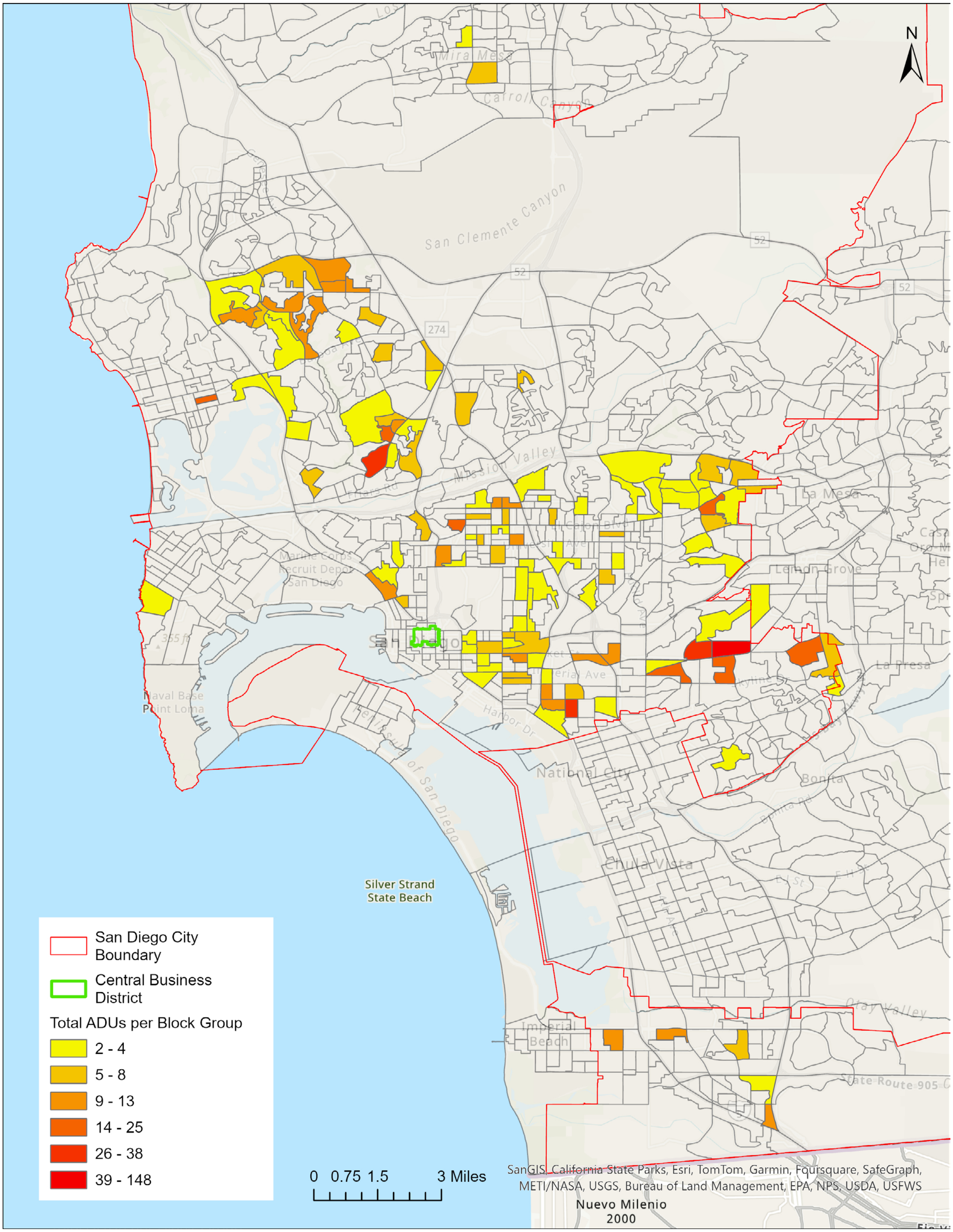
Before the creation of the Bonus Program, staff were continually updating the city's base ADU code to encourage more units. In 2017, they allowed ADUs on lots that had not yet reached maximum density. The original ADU code required that a single-family home on a lot zoned for a duplex be demolished and rebuilt as a duplex before any ADUs could be built. Planning staff had found that this requirement made ADU development infeasible on many lots citywide.[7]

Later, staff updated the regulations to allow for ADUs on any residential parcel, not just single-family and small-multifamily parcels as the original code required. This update meant that base ADU code applied to almost every residential parcel in the city, including large-multifamily parcels with larger lot sizes.

These earlier reforms laid important groundwork for the Bonus ADU Program to be effective. The program was put forward in response to Assembly Bill (AB) 671, which required cities to include a plan in their housing elements to "incentivize and promote the creation of accessory dwelling units that can be offered at affordable rent for very low, low-, or moderate-income households." With this goal in mind,

7 Gary Geiler, interview, 2023.

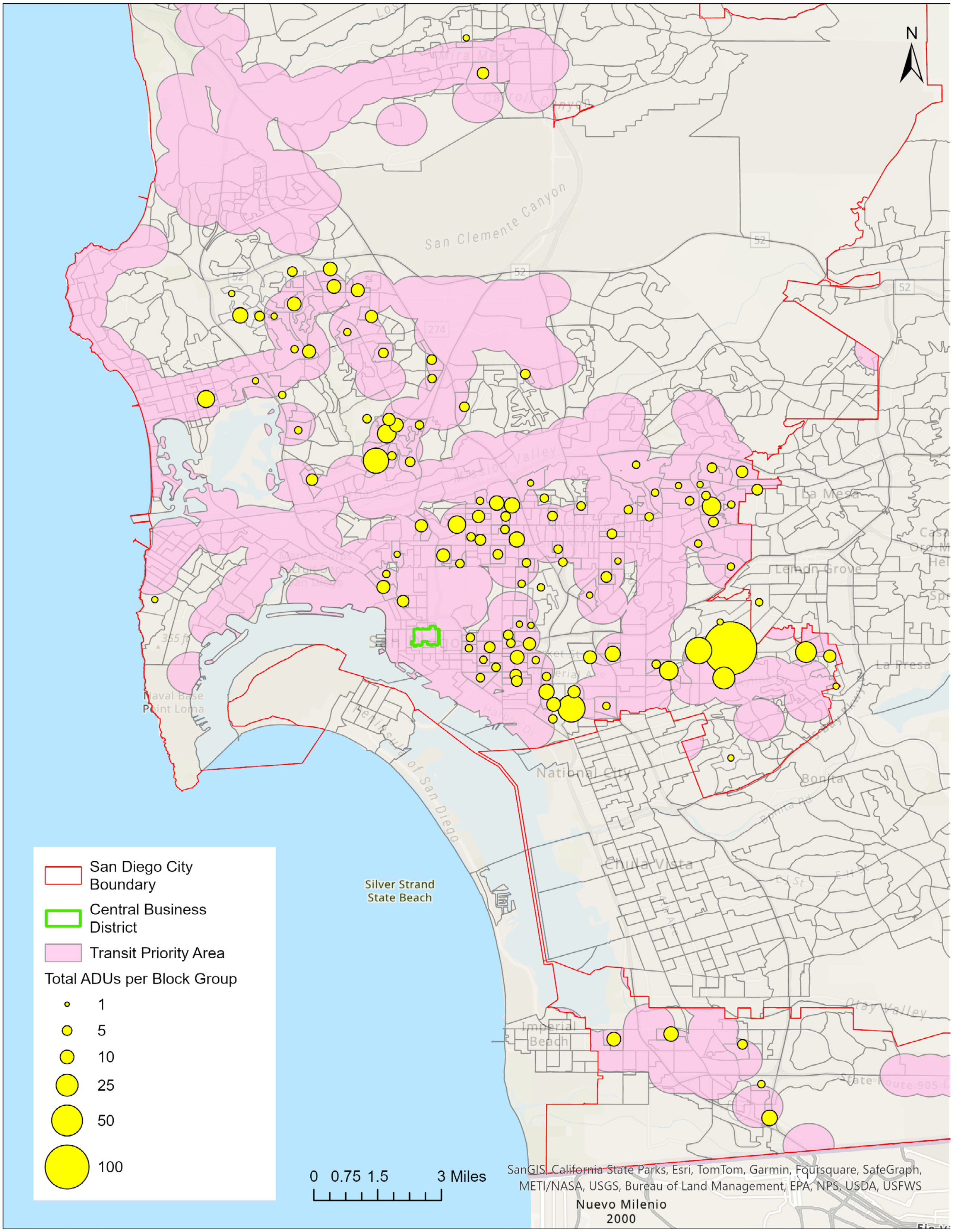
Fig. 1: San Diego Bonus ADU projects, by total units per block group.



Source: Internal data, San Diego Housing Commission.

Fig. 2: Transit Priority Areas (TPAs)* with Bonus ADU projects, by total units per block group.

**TPAs are defined as any area within 0.5 miles of a major transit stop.*



Source: Internal data, San Diego Housing Commission.

planning staff – led by Deputy Planning Director for Environmental Policy Kelly Stanco and then-Senior Planner Brian Schoenfisch – designed the program.[8]

In October 2020, the San Diego City Council voted unanimously to adopt a 'Housing Legislation Code Update,' which included the Bonus ADU program and the elimination of all parking requirements for ADUs citywide. Kelly Stanco presented the item to the Council and noted the enthusiasm for the program from the Department of Housing and Community Development. "[HCD] is particularly interested in and excited by our affordable ADU incentives. This is implementing a state law that requires us to incentivize the construction of [affordable] ADUs…this is our proposal and HCD fully supports it and is potentially looking to use it as a model for other jurisdictions."

The code update passed the council without community pushback or media coverage, which Councilmember Scott Sherman noted in his comments. "This isn't the sexy, make-the-news kind of story," he explained, before voting yes on the reforms. "But at the end of the day it's helping create more housing in San Diego and hopefully we can start bringing down the price of housing to the residents of San Diego by providing more of it and this is a great step in that direction."[9]

Although the passage of the program went largely unnoticed outside of city government officials and housing developers, it eventually gained attention for producing ADU projects of unprecedented scale. Gary Geiler – Assistant Director of San Diego's Development Services Department – noted that city planning staff and elected officials did not design the Bonus ADU program with the expectation that it would produce large-scale development. Instead, officials were clear that the program was designed to incentivize small-scale, infill development. The city hoped that the bonus program would create anywhere from 2-12 additional ADUs, depending on lot size.[10]

However, earlier reforms meant that large-scale ADU projects were now feasible under the parameters of the bonus program. Since the city had already permitted ADUs on large-multifamily parcels and eliminated all parking requirements, the unlimited unit counts within TPAs unlocked significant scale. Developers began utilizing the program on multifamily parcels larger than 10,000 square feet. Even with low FAR and lot coverage limits, these parcels are large enough to allow for very high unit counts.

Program Outcomes

Unexpected Unit Counts

The Bonus ADU program has led to several large-scale multifamily developments. There are a total of 33 projects under review as of February 2024 that we classified as large-scale, defined as projects adding 10 or more ADUs.

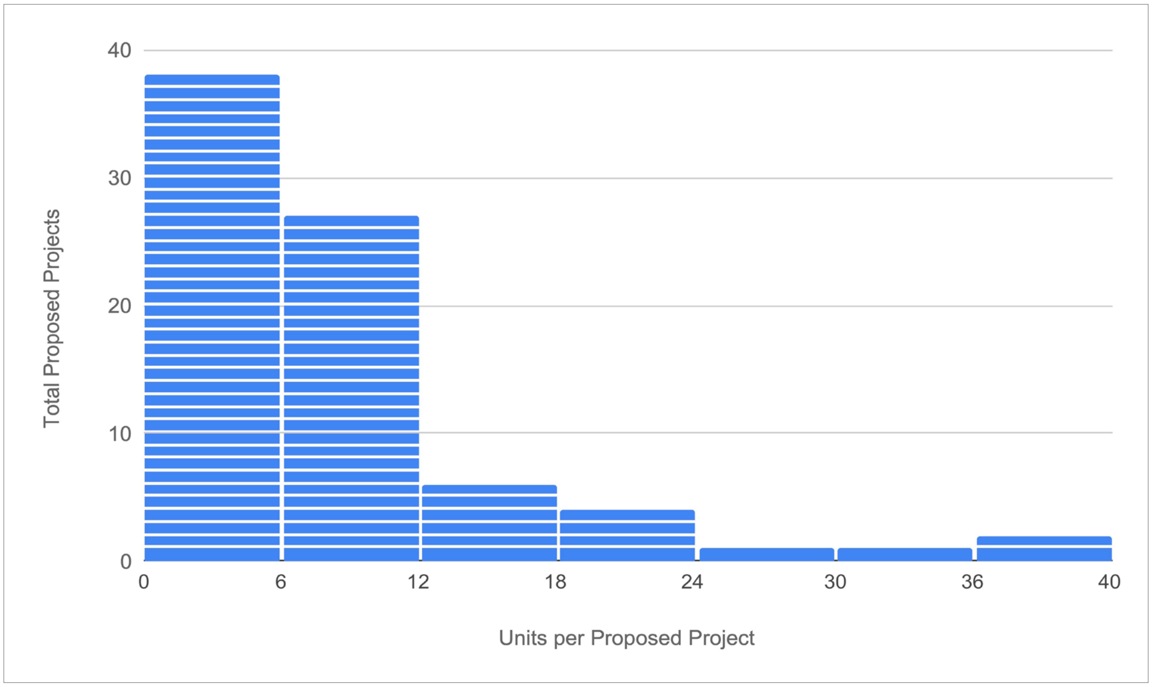
Among the projects in review is a proposal for 148 Bonus ADUs, located in the city's Encanto neighborhood. For now, this project is an outlier. The remaining large-scale proposals range from 10 to 38 units. However, local San Diego developers shared with our team details of large-scale projects they plan to submit to the city for review.

Christian Spicer – President and Founder of SDRE Homebuyers – is a developer based in San Diego who has utilized the Bonus ADU Program for a number of projects. He is currently in design-development

---

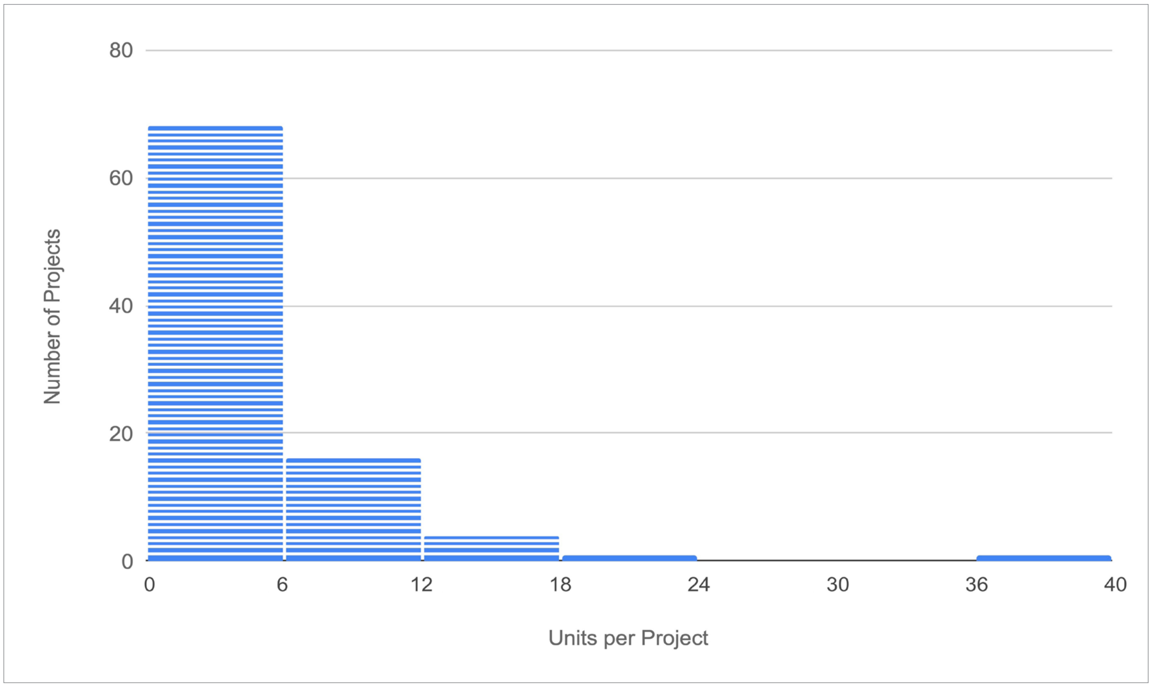
8 City of San Diego, Report of the Planning Commission, August 27, 2020.
9 City of San Diego, Minutes for the Regular Council Meeting, October 13, 2020.
10 Gary Geiler, interview, 2023.

Fig. 3: Total Proposed Projects by Units per Project



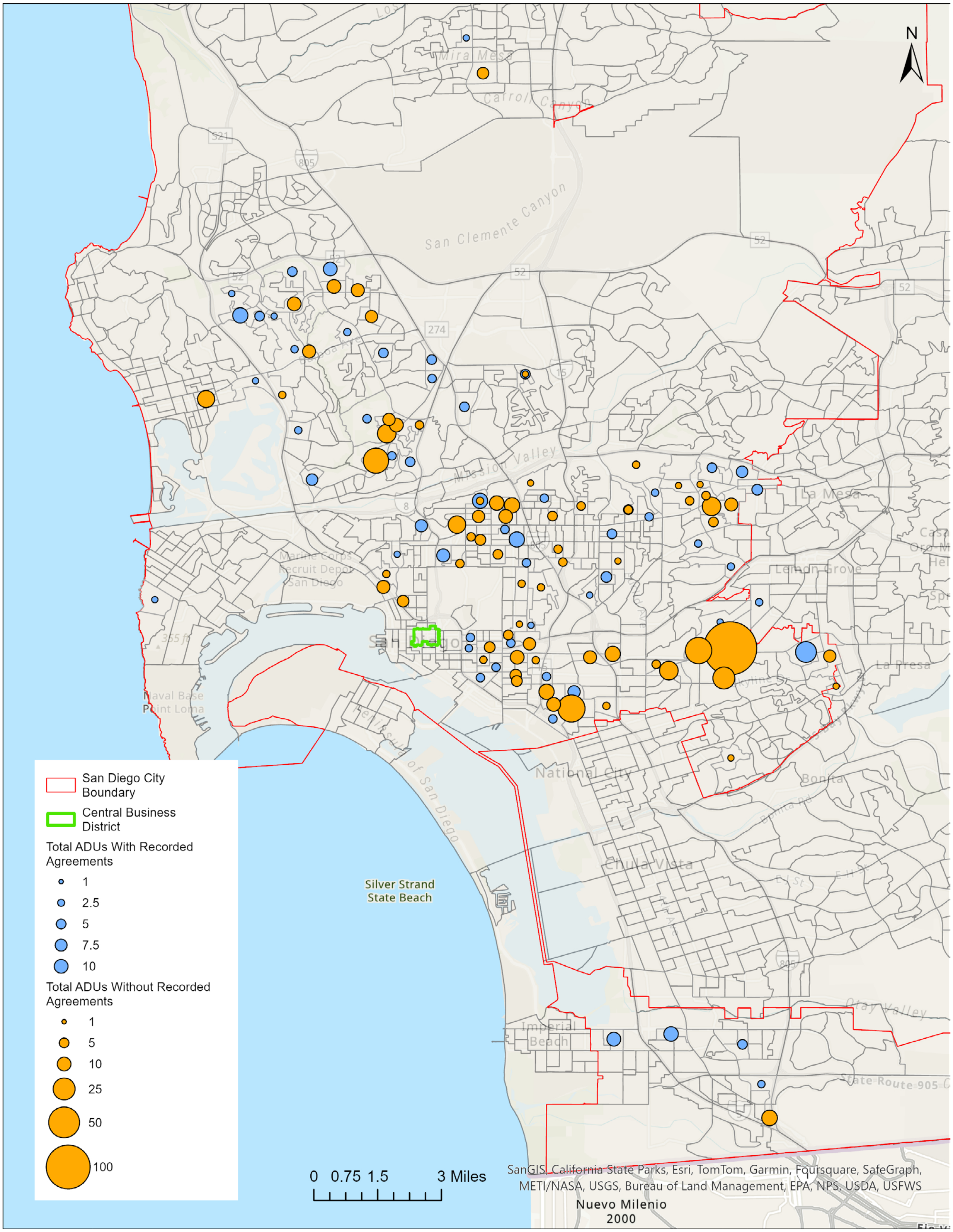
Source: Internal data, San Diego Housing Commission.
Note: This chart has removed one outlier, a 148-unit proposed project.

Fig. 4: Total Projects with Recorded Agreements by Units per Project



Source: Internal data, San Diego Housing Commission.

Fig. 5: Bonus ADU projects by total units per block group, proposed (without a recorded agreement) versus projects underway (with a recorded agreement).



Source: Internal data, San Diego Housing Commission.

for a 126-unit Bonus ADU project in the Pacific Beach neighborhood. He submitted the project to the city for grading and building permits in January 2024. Three additional projects in his pipeline propose over 100 units, the largest of which would produce 151 ADUs.[11] Spicer has a total of 2,200 units in his development pipeline, the vast majority of which will be permitted through the Bonus ADU program. Most of his projects are between 10 and 30 units, but at least nine projects will produce 40 units or more.[12]

Although Spicer's developments may be uniquely large, he is certainly not the only local developer using the program to produce high-unit projects. David Pearson – co-founder of the design shop PALO – has worked with developers to produce ADU projects with as many as 36 units.[13]

To be clear, the majority of Bonus ADU projects have produced smaller-scale development. Of the 181 projects currently under review, 148 will produce fewer than 10 units. It is also worth noting that only 90 of the projects under review have actually entered into a recorded agreement with the city. So far, the largest project to secure a recorded agreement with the city will produce 36 units.[14]

Going forward, city officials expect that most projects will continue to produce 2 to 12 units based on lot configurations and zoning. Gary Geiler predicted that about 10 total projects will produce 100 or more units in the coming years, noting that few lots are large enough to allow for 100-plus units under the parameters of the program.

For example, the city is currently reviewing a 100-plus unit project on a 125,000 square foot lot with an FAR of 0.45. That configuration allows the developer 56,000 square feet of floor area to work with. The lot is currently zoned for single-family (R-1-7) and has one single-family dwelling which will be demolished. As Geiler notes, most lots within Transit Priority Areas are much smaller. Lot size, existing FAR and height limits will likely constrain the total unit count.[15]

Affordability Challenges

Housing affordability is perhaps the most significant issue facing San Diego. Roughly half of the city's households are cost-burdened – spending more than 30% of their income on housing. Average rent prices in San Diego increased 46% from 2012 to 2019 and the city's median household rent is $2,200 as of 2022 – making it one of the most expensive rental markets in the country.[16] These housing costs take the biggest toll on low-income and very low-income households across the San Diego region. As of 2023, 141,544 low-income renter households in San Diego County do not have access to an affordable home.[17]

As part of required updates to the city's housing element, San Diego must plan for 108,000 new units of housing including over 32,000 for households making between 30-80% AMI and an additional 19,000 for households making between 80-120% AMI. The Bonus ADU program is a key part of the city's efforts to dramatically increase its supply of deed-restricted affordable housing.

---

11 Christian Spicer, interview, 2024.
12 Internal data, SDRE Homebuyers, 2024.
13 David Pearson, interview, 2023.
14 Internal data on Bonus ADU program, San Diego Housing Commission.
15 Gary Geiler, interview, 2023.
16 City of San Diego, General Plan Housing Element, 2021-2029.
17 CHPC, San Diego County Affordable Housing Needs Report, 2023.

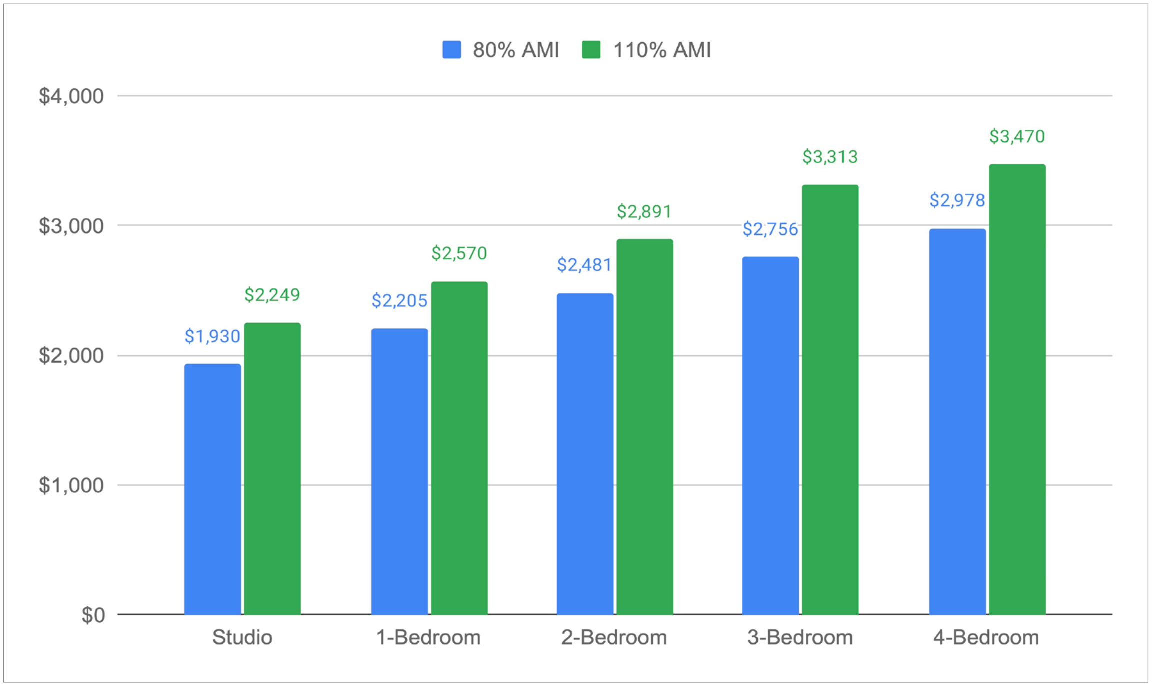
For every market-rate bonus ADU that a developer builds, it must create a deed-restricted affordable ADU. Developers have two choices for this affordability requirement: the affordable unit can be restricted for 15 years at a rent limit based on 110% of the county's Area Median Income (AMI) or for 10 years at a rent limit based on 80% of AMI. City staff designed this two-tiered system based on feedback they had received from developers.[18]

Of the 181 projects in review and the 92 projects with a recorded covenant, every single affordable ADU has been restricted to 110% AMI for 15 years. When given the choice, developers uniformly prefer a longer affordability covenant with higher allowable rents.[19]

In exchange, the city gets a bigger boost to its overall supply of rental housing and a significant boost to its supply of income-restricted affordable housing, albeit at moderate-income levels for a short time horizon. So far, city officials have indicated that they are more than happy to make this trade-off.

Fig. 6: San Diego rent limits by unit size and Area Median Income, 2023*

*Not including utility allowance deduction of $139



Source: San Diego Housing Commission Rent Limits, 2023.

Christian Spicer has found that 1-bedroom units are financially feasible for his projects. His 126-unit project will be largely 1-bedroom units. He plans to rent half of those units for $2,500, which will be reserved for residents making less than 110% of AMI. The other half will be rented at market-rate, between $3,000 and $3,200. This gap represents a significant savings for moderate-income residents.[20]

David Pearson – whose shop has produced several projects consisting entirely of studios – estimated that a market-rate Bonus ADU studio unit would rent between $1,700 and $2,500, depending on the neighborhood. As seen in Figure 6, affordable rent limits for studios are $1,930 at 80% AMI and $2,249

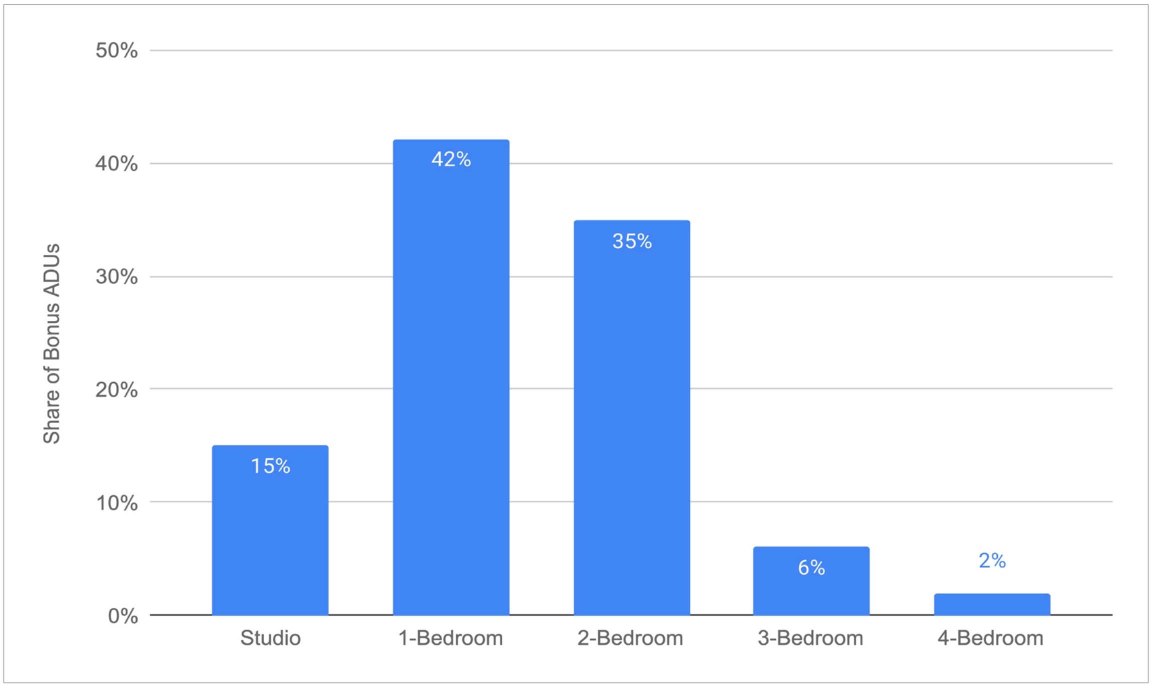
18 Gary Geiler, interview, 2023.
19 Internal data on Bonus ADU program, San Diego Housing Commission.
20 Christian Spicer, interview, 2024.

at 110% AMI respectively. In other words, the affordable units are comparable to market-rate prices in some neighborhoods of the city.[21]

Unit Size

So far, the city's preliminary data on unit size is incomplete. Of the nearly 1,300 proposed units, the city knows the bedroom size for about half. As seen in the following figure, 1- and 2-bedroom units represent the largest share of proposed Bonus ADUs. Several developers predicted that an increasing share of the units going forward will be studios and 1-bedrooms. Per state ADU law, any ADUs under 750 square feet are exempt from development impact fees, which incentivizes developers to build smaller units. These studios and 1-bedrooms will boost the supply of rental housing for students and young professionals, a large and growing demographic in San Diego. According to the city's housing element, 60% of San Diego households have only one or two persons – a share that is expected to grow as younger residents wait longer to purchase homes and start families.

Fig. 7: Unit sizes for proposed Bonus ADUs under review, by individual units



Source: Internal data, San Diego Housing Commission.
Note: 55% of projects did not specify unit size.

However, studios and 1-bedroom units will not provide rental housing for large families, which remains a significant need across the city. The housing element calls for the creation of a "Large Family Unit affordable housing incentive program encouraging 3-bedroom units in quality transit areas." As of now, the Planning Department has not yet specified or implemented that incentive program.[22]

The need for more large family units may be in tension with the incentive developers currently have to keep new ADUs under 750 square feet, which allows them to avoid development impact fees. City officials should explore additional incentives that can align these policy goals. For example, the city

21 David Pearson, interview, 2023.
22 City of San Diego, General Plan Housing Element, 2021-2029.

could waive development impact fees for projects that produce large-family ADUs (3 or 4 bedroom units) restricted at or below 80% AMI.

Additionally, city officials could consider increasing the ratio of allowable bonus, market rate ADUs for large family, affordable units. For example, the program could allow 1.5 market rate ADUs for every 3-bedroom affordable unit, and 2 market rate ADUs for every 4-bedroom affordable unit.

Financial Feasibility

Driving these outcomes are the development costs and revenue projections for Bonus ADU projects. Drawing on extensive conversations with developers along with pro formas that they shared, our research team built a composite case study representing the development costs of a typical Bonus ADU project within a TPA:

Case Study Characteristics[23]

Site size	6,000 square feet
Building size	Existing duplex: 1,500 sq. Feet 12 new ADUs: 350 sq. ft.
Total units	14 units
Unit mix	1 duplex: 2 separate 2 bed/1 bath units 12 ADUs: studios
Parking	5 spots (2 curb cut spots, 3 in alley)
FAR	1.0

Basic Development Costs

Hard costs	Materials labor	New construction ($400/sq.ft)	$1.68 million	$2 million
		Remodel ($70k/unit)	$140,000	
		Hard cost contingency (10%)	$183,000	
Soft costs	Fees, consultants, financing costs, tax and insurance	Pre-dev and utility consultants	$30,000	$603,000
		Architecture & engineering	$140,000	
		Utility connection upgrade	$90,000	
		City utility permit	$5,000	
		Development impact fees	$40,000	
		Insurance	$50,000	
		Taxes (15 months)	$12,000	
		Legal & accounting	$10,000	
		Construction loan interest	$209,442	
		Soft cost contingency (5%)	$16,850	
Acquisition	Initial value	Land	$792,000	$950,000
		Structure	$158,000	
			Total uses	**$3.55 million**

23 See Appendix I for detailed assumptions.

Sources of Funds

Total equity investment	$1,343,850	**$3.55 million**
Total amount financed	$2,212,442	
	Total sources:	**$3.55 million**

Rental Revenue

Unit type	Total units	Rent per unit per month	Rent per unit per annum	Total rent (PUPA)
Duplex	2	$3,000	$36,000	$72,000
Market-rate ADU	5	$2,500	$30,000	$150,000
Affordable ADU (110% AMI)	6	$2,110	$25,320	$151,920
Inclusionary ADU (50% AMI)	1	$1,067	$12,804	$12,804
			Annual revenue:	**$387,000**

Property Before Tax Cash Flow (PBTCF)

Potential gross income	$387,000
Vacancy rate (5%)	($19,350)
Effective gross income	$367,500
Operating expenses (30%)	($110,250)
Net operating income	$257,250
Capital reserve set-aside	$42,000
Property before tax cash flow	**$215,250**

10 Year Internal Rate of Return (IRR)	**15.9%**

The composite case study reveals that Bonus ADU developers are able to achieve significant densities on infill sites, while keeping their development costs relatively low. With unlimited units allowed and zero parking required, the FAR is the only significant constraint on development. As demonstrated above, even a low FAR permits 12 studio ADUs. The resulting rental revenue allows these projects to pencil, even with some notable costs.

Developers highlighted the cost of upgrading utility connections, in particular, as a serious pain point. Most bonus projects are adding 4-10 new units behind an existing single-family or duplex unit. The existing low-intensity use means that developers must upgrade the electrical and water utilities at a significant expense in order to add even a small number of additional units. The costs below are a more granular breakdown of utility costs included in the case study:

Table 1: Typical costs of upgrading utility connections for Bonus ADU projects

Utility-related expenditure	Cost
Electrical utility upgrade	$50,000
Water utility upgrade	$40,000
City permit for utility upgrades	$5,000
Utility consultant	$30,000
Civil engineers	$10,000
Total	**$135,000**

These costs are a serious barrier to infill, missing middle development. Developers also suggested that without reforms to lower the costs of utility upgrades, it will be financially difficult to restrict affordable ADUs at 80% AMI. In other words, capping these costs could allow the program to target deeper affordability levels. These findings indicate that as regulatory barriers to affordable development have receded in San Diego, the comparative importance of utility costs has increased significantly.

One legislative proposal under consideration in Sacramento, SB1210, offered a promising solution. The initial draft of the bill – authored by Senator Nancy Skinner – would have required that public utilities and municipal utility districts cap any upgrade fees at 1% of a new housing unit's building permit value.[24] The original draft also required that this 1% fee be charged over the course of a minimum of 10 years, smoothing the upfront costs for developers.[25] Applied to the case study pro forma above, Senator Skinner's bill would lower utility connection costs alone from $90,000 to $18,200 – not including other possible savings on consultants and fees. Since the remaining fees can be paid over 10 years, the proposed cap would effectively eliminate utility connection fees as an upfront development cost. The resulting savings in equity investment are shown in the table below:

Table 2: Total equity investment with and without cap on utility connection fees

	Total equity investment
Without 1% cap on utility connection fees	$1,343,850
With 1% cap on utility connection fees	$1,255,670
Total savings	**$88,180**

These savings in upfront equity investment can potentially allow developers to provide units at deeper levels of affordability. So far, no developer has produced a Bonus ADU restricted at 80% AMI over 10 years; instead, all affordable ADUs have been restricted at 110% AMI over 15 years.

When adjusted to reflect the savings from the 1% cap, the case study pro forma shows modest gains in IRR. The table below shows the effect of the cap on 10 Year IRR, for the existing rental mix (110% AMI) and a more affordable rental mix (80% AMI):

---

24 Building permit value refers to the total value of the construction costs–materials and labor–for which a building permit is issued. This figure is self-reported by developers when they apply for building permits. Developers may under-report this number; however, this model conservatively estimates that a developer is reporting the full value of the project's hard costs.

25 As of May 2024, this bill has been amended and no longer includes the 1% cap; instead, it requires that utility districts publish their fee schedules and service timelines. However, legislators should continue to evaluate and consider caps on utility connection costs.

Table 3: 10-Year IRR with & without cap on utility connection fees, by affordability level

	80% AMI	110% AMI
IRR without 1% cap	15.3%	15.9%
IRR with 1%	15.8%	16.5%

Developers opting for deeper affordability still achieve significant IRR. The rate for projects restricted to 80% AMI with a cap on utility fees is 15.8% – not far below the 15.9% IRR achieved under current conditions. The case study suggests that a cap on utility connection fees could be an opportunity to require deeper affordability levels from developers.
It is also worth noting that lowering these costs would particularly benefit smaller-scale projects, since these fees represent a larger share of those projects' development costs. However, even if the original draft of SB1210 or a similar bill were to become law, utility-related delays remain a significant issue that needs to be addressed as cities like San Diego push for streamlined, infill housing development.

The difficulty of upgrading utility connections has also affected the pool of construction labor available. Several developers highlighted a shortage of small-scale general contractors who have previous experience working with utility districts. Bonus ADU developers must choose between paying a large project management fee to a sophisticated general contractor with expertise in large-scale apartment buildings, or paying an affordable rate for a small-scale contractor who typically works on small ADU projects or renovations. The former option is costly, while the latter option often leads to delays with the utility districts.[26]

David Pearson described a "trial and error" process with general contractors who are learning the particularities of the Bonus ADU program. He believes that small-scale general contractors will slowly build an expertise with this new 9-12 unit type, including how to upgrade utility connections more efficiently. Until then, however, the complexity and costs associated with utility upgrades will make it very difficult for inexperienced, small-scale developers to utilize the Bonus ADU program.[27]

Location: Does the Bonus Program Fulfill AFFH Goals?

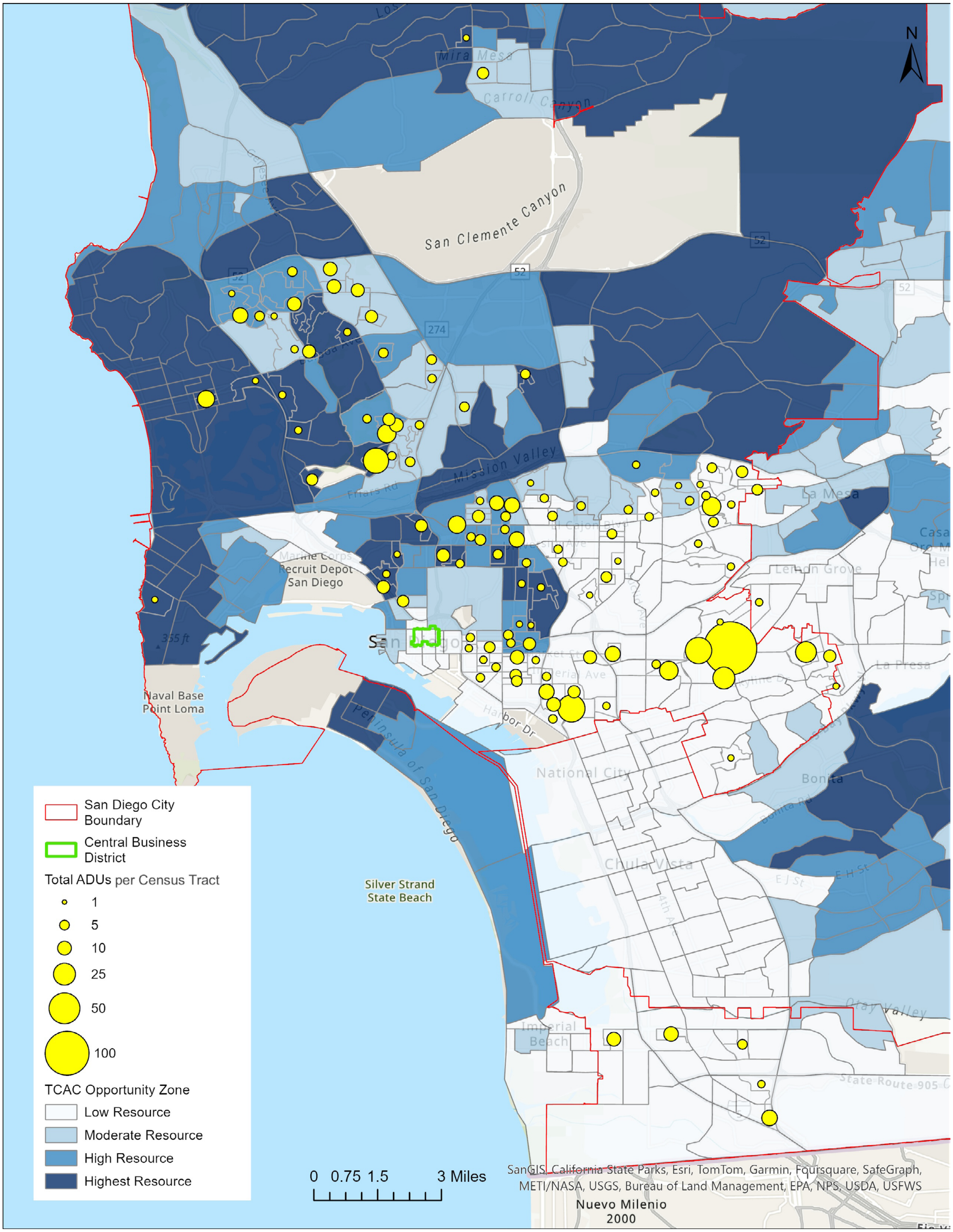
Under state law AB 686 – passed in 2018 – California cities are mandated to enact policies that Affirmatively Further Fair Housing (AFFH). A key indicator the state uses to measure progress towards AFFH goals are the TCAC Opportunity Maps. The TCAC Maps classify census tracts according to five categories based on socioeconomic status: High Segregation & Poverty; Low Resource; Moderate Resource, High Resource and Highest Resource.

Revisions to AFFH in 2021 required jurisdictions to enact policies in their housing elements that "increase affordable housing in high-resource neighborhoods that have often been exclusionary and bring additional resources to traditionally under-resourced neighborhoods." Has the Bonus ADU program helped San Diego achieve this goal?

The initial results are mixed. The program has been very successful in creating new housing in neighborhoods classified as "Moderate Resource" (middle income), which is a promising, early outcome. 40% of proposed Bonus ADUs are located in these areas, compared to only 25% of total ADUs citywide and 10% of total housing permits.

26 David Pearson, interview, 2023.
27 David Pearson, interview, 2023.

Fig. 8: Bonus ADU projects across TCAC Opportunity Areas, by total units per block group.



Source: Internal data, San Diego Housing Commission.

A very small share of proposed Bonus ADU projects are located in "Highest Resource" areas, as compared to the total ADUs and total housing permits across the city. These data are too limited and preliminary to draw firm conclusions about where the program is being utilized. However, if this result holds as the program continues, the city will have missed a significant opportunity to create income-restricted affordable units in its wealthiest and most exclusionary neighborhoods. These data also suggest that in lower resource areas of the city, nonprofit organizations like community development corporations (CDCs) and community land trusts (CLTs) have an opportunity to build Bonus ADUs, which could generate permanently-affordable housing at relatively low development costs.

Table 4: Share of projects by TCAC Opportunity Area, comparing all housing permits, total ADUs, and bonus ADUs

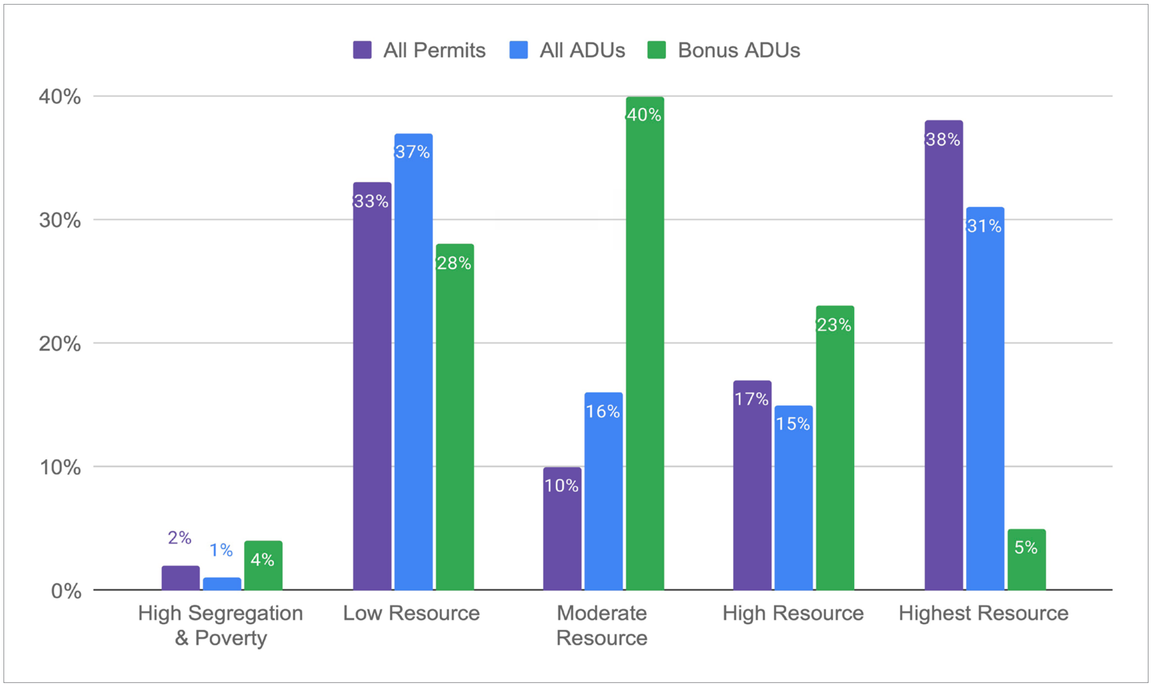
All San Diego Housing Permits (2018-2023)		
TCAC Category	**Project Count**	**% of Total Projects**
High Segregation & Poverty	163	2%
Low Resource	3520	33%
Moderate Resource	1009	10%
High Resource	1858	17%
Highest Resource	4090	38%
All ADUs (2018-2023)		
TCAC Category	**Project Count**	**% of Total Projects**
High Segregation & Poverty	73	1%
Low Resource	1934	37%
Moderate Resource	836	16%
High Resource	777	15%
Highest Resource	1661	31%
Bonus ADUs (2021-Present)		
TCAC Category	**Project Count**	**% of Total Projects**
High Segregation & Poverty	7	4%
Low Resource	51	28%
Moderate Resource	72	40%
High Resource	42	23%
Highest Resource	9	5%

Source: Internal data, San Diego Housing Commission; APR Data, HCD, 2018-2023.
Notes: "High Segregation & Poverty" is a designation for census tracts that are within "Low Resource" areas. This table counts projects proposed or permitted in "High Segregation & Poverty" census tracts separately from the "Low Resource" category.

An additional pattern the city should monitor is where large-scale Bonus ADU projects are being proposed by for-profit developers. Of the Bonus ADU projects currently in review, the largest would create 148 units. It is located in the city's Encanto neighborhood, a predominantly Black and Latino community categorized as a "Low Resource" area. Although income-restricted units may provide stability to renters in lower-income neighborhoods, the city may not want to see such a high concentration of units in areas that have historically absorbed more than their fair share of housing development.

On average, higher-unit count Bonus ADU projects are being proposed in “Low-Resource” areas more than any other TCAC zone. However, a regression analysis of project data found that there was no statistically significant relationship between a project’s unit-count and any particular TCAC zone.

Fig. 9: Share of projects by TCAC Opportunity Area, comparing all housing permits, total ADUs, and bonus ADUs



Source: Internal data, San Diego Housing Commission; APR Data, HCD, 2018 - 2023.
Notes:“High Segregation & Poverty” is a designation for census tracts that are within “Low Resource” areas. This chart counts projects proposed or permitted in “High Segregation & Poverty” census tracts separately from the “Low Resource” category.

When analyzing the location of Bonus ADU projects by the Median Family Income (MFI) of census tracts across San Diego, we find that the largest share of projects are located in census tracts in the lowest quintile of MFI.

As seen in Table 5 below, 57% of Bonus ADU projects are located in census tracts in the bottom two quintiles of MFI, compared to 45% of all ADUs and 37% of all housing projects citywide. Meanwhile, just 19% of Bonus ADU projects are located in census tracts in the top two quintiles of MFI, compared to 38% of all ADUs and 51% of all housing projects citywide.

Table 5: Share of projects by neighborhood median family income (MFI) quintile, comparing all housing permits, total ADUs, and bonus ADUs

All San Diego Housing Permits (2018-2023)		
MFI Quintile	**Project Count**	**% of Total Projects**
Q1 ($80,625)	1811	17%
Q2 ($110,568)	1570	15%
Q3 ($136,639)	1813	17%
Q4 ($171,917)	2763	26%
Q5 ($250,001)	2668	25%
All ADUs (2018-2023)		
MFI Quintile	**Project Count**	**% of Total Projects**
Q1 ($80,625)	1245	24%
Q2 ($110,568)	1088	21%
Q3 ($136,639)	942	17%
Q4 ($171,917)	1033	20%
Q5 ($250,001)	970	18%
Bonus ADUs (2021-Present)		
MFI Quintile	**Project Count**	**% of Total Projects**
Q1 ($80,625)	54	30%
Q2 ($110,568)	48	27%
Q3 ($136,639)	43	24%
Q4 ($171,917)	18	10%
Q5 ($250,001)	15	9%

Source: Internal data, San Diego Housing Commission; APR Data, HCD, 2018-2023; ACS Data 2018-2022.
Notes: Census tract MFI data was missing for 41 total housing permits, 13 regular ADUs and 3 Bonus ADUs.

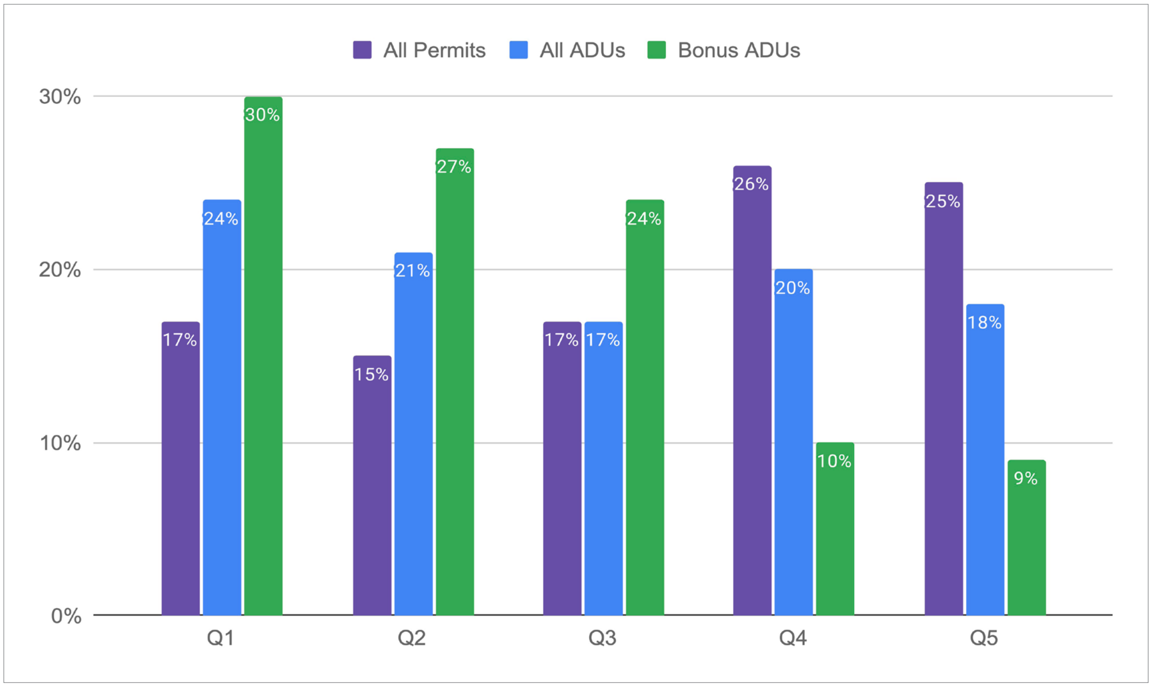
The MFI analysis confirms that the Bonus ADU program has succeeded in producing housing in moderate-income neighborhoods – nearly a quarter of Bonus ADU projects are located in census tracts in the middle quintile of MFI, compared to 17% of all ADUs and all housing projects respectively. Still, these findings indicate that Bonus ADU projects are much more likely to be proposed in lower-income census tracts and much less likely to be proposed in higher-income census tracts.[28]

Going forward, there are signs of demand for large-unit projects in higher-income areas of the city. If approved, Christian Spicer's 126-unit project will bring 63 income-restricted ADUs to the Pacific Beach neighborhood, located in a "Highest Resource" area of the city. If city officials hope to use the Bonus ADU program to pursue AFFH goals, city staff should identify ways to incentivize larger-unit projects in "Highest Resource" areas like Pacific Beach.

---

28 It is possible that the program's incentive to build in TPAs may contribute to this spatial distribution, as census tracts outside of TPAs in San Diego may skew wealthier and higher-income. Further spatial analysis is required to confirm whether the TPA incentive leads to more Bonus ADU projects being proposed in low-income neighborhoods.

Fig. 10: Share of projects by neighborhood median family income (MFI) quintile, comparing all housing permits, total ADUs, and bonus ADUs



Source: Internal data, San Diego Housing Commission; APR Data, HCD, 2018-2023; ACS Data 2018-2022.
Notes: Census tract MFI data was missing for 41 total housing permits, 13 regular ADUs and 3 Bonus ADUs. See appendix II for quintile designations.

One program the city should consider expanding is the recently created ADU Finance Program. The city could open the program up to Community Development Corporations (CDCs) and other local non-profit organizations trying to develop affordable housing in moderate- and high-resource areas. By providing soft loans and technical assistance, the city can encourage CDCs to build Bonus ADU projects that target deeper levels of affordability for longer periods of time throughout San Diego, including in historically exclusionary neighborhoods. Likewise, this subsidy could incentivize or require these organizations to create a minimum percentage of affordable, large family units.

Conclusion

San Diego has unlocked a very successful pathway to infill development. Thanks to years of iterative updates in Sacramento, state ADU law provides a reliable, by-right approval process that developers can trust. By attaching its missing middle housing initiative to well-established ADU laws, San Diego may have discovered a procedural "backdoor" to infill housing that usually requires politically-challenging rezonings.

Unintentionally, the city has also created a more streamlined pathway to large-scale multifamily development. The resulting type and business model are atypical for ADU development. Instead of a homeowner developing a backyard mother-in-law suite, San Diego's program sees more experienced developers purchasing single-family and duplex properties with large lots in order to add multifamily ADU buildings. It is not uncommon for these projects to include 10 or more units and several will produce over 100 units if approved.

While these surprisingly large projects will add much-needed supply to the city's rental housing stock, they are not necessarily the kind of "gentle density" promoted by advocates of missing middle housing. As developers continue to utilize the program, larger-scale projects may begin to concentrate in low-resource neighborhoods which have absorbed more than their fair share of previous housing development.

Notably, the program has not been effective in producing housing affordable for low- or very low-income residents. No developer has opted to produce affordable ADUs at or below 80% AMI; instead, every single affordable bonus ADU has been deed-restricted for residents at or below 110% AMI. Early data also suggest that developers are producing very few large family units, opting largely for studios and 1-bedroom units.

To ensure that the Bonus ADU program can further the city's AFFH goals and create housing affordable to low-income residents and large families, city officials should consider the following recommendations.

Policy Recommendations:

- Identify ways to create affordable housing for low-income residents (at or below 80% AMI) – not just moderate-income residents (at or below 110% AMI) – without jeopardizing the existing business model.
    - Implement an additional density incentive for projects that produce units affordable for low-income residents (at or below 80% AMI).
- Identify ways to lower utility upgrade costs, such as the original draft of SB1210 – proposed by Senator Skinner – which would cap utility costs at 1% of a new unit's building permit value.
    - Cap utility costs at a lower rate for projects restricted at or below 80% AMI.
- Incentivize community development corporations (CDCs), community land trusts and other community-based organizations to utilize the Bonus ADU program, encouraging local economic development.
    - Expand the ADU Finance Pilot Program to make more pre-development funds or loan assistance available to CDCs and nonprofits that apply to utilize the Bonus ADU program.
    - Incentivize CDCs and other local nonprofits to produce large family units using the Bonus ADU program.
- Explore other, possible incentives to create more 3- and 4-bedroom units for large families.
    - Waive development impact fees for projects that produce large-family ADUs restricted at or below 80% AMI.
    - Increase the ratio of allowable bonus, market rate ADUs for large family, affordable units. For example, the program could allow 1.5 market rate ADUs for every 3-bedroom affordable unit, and 2 market rate ADUs for every 4-bedroom affordable unit.
- Continue to monitor where large-scale Bonus ADU projects are being proposed and identify incentives to encourage moderate- and large-scale projects in High Resource and Highest Resource neighborhoods of the city.

Acknowledgements:

The Center for Community Innovation would like to thank all of the developers, advocates and city officials who spoke with us about the program. We would like to thank Muhammad Almeldin, Jared Basler, David Pearson, Celeste Goyer, Denise Pinkston, Gary Geiler, Dori Ganetsos and Paul McDougall for their additional feedback and commentary on this report. This research was funded by the California Department of Housing and Community Development; however, the authors are solely responsible for its content.

APPENDIX I: Composite Pro Forma Assumptions[1]

Operating Assumptions:

Vacancy factor	5%
Operating expenses as % of revenue	30%
Capital reserves (per unit per month)	$250

Permanent Loan Assumptions:

Loan to value (LTV)	64%
Interest rate	6.5%
Amortization period	25 years

Internal Rate of Return Assumptions:

Months of stabilized operations in year of construction	4
Annual OpEx and capital replacement costs growth factor	4%
Annual rent growth factor	3%
Implicit entry cap rate (exit cap rate assumed to be the same)	7.4%

APPENDIX II: MFI Quintiles for San Diego County Census Tracts 2018-2022

MFI Quintile	
Q1 (20th percentile)	$80,625
Q2 (40th percentile)	$110,568
Q3 (60th percentile)	$136,639
Q4 (80th percentile)	$171,917
Q5 (100th percentile)	$250,001

1 For access to the full, composite pro forma, please contact the research team by emailing awofford@berkeley.edu.