

# Smaller Homes Becoming a Bigger Deal

Economic and environmental sustainability play key roles in square-footage trend

By **Kathleen O'Brien**, president, O'Brien & Co.

**S**INCE 1950, HOMES' SQUARE-FOOTAGE has more than doubled in the United States, according to the National Association of Home Builders, while average household size has dropped. Whether this has meant an increase in true value is questionable.

Oversized homes and "McMansions" use significantly more energy to operate. For example, a 1,500-square-foot home with the same energy-efficiency and in the same climate as a 3,000-square-foot home would use half the energy to heat and two-thirds the energy to cool. With the energy-price volatility we are experiencing, this is no small thing for homeowners trying to pay their monthly mortgage and energy bills.

For builders and developers, larger homes also require more raw material than smaller homes. In addition to the environmental benefit of conserving natural resources, material efficiency in smaller homes can reduce construction costs significantly.

As mortgage brokers work with clients in today's constricted credit market, it's important to consider how economic and environmental sustainability can help turn deals for smaller homes into a larger piece of their puzzle.

To understand how home sizes have fluctuated, it's wise to learn the trends behind them.

First, the U.S. capital-gains-tax policy influenced house sizes by encouraging sellers to buy

up to a larger home. This policy changed in 1998, however, and sellers are no longer taxed for capital gains on the first \$250,000 for a primary residence — or \$500,000 if the sellers are a couple. Thus, the incentive to buy up is no longer a significant driver of house size.

Indirectly, the mortgage industry also has impacted new-home sizes by setting a ratio of house value to land value. Secondary-mortgage markets often specify that the lot should not be worth more than 30 percent of the total property value. Thus, homeowners have been encouraged to build large, expensive houses. In addition, appraisers often find it difficult to find small-home comps in established developments.

Zoning regulations, restrictive covenants and design standards also have blocked small housing developments. Some U.S. cities and neighborhoods have minimum home sizes in developments.

Finally, a combination of the "more is better" mentality, standardization among planners and builders, and consumer affluence have played large roles.

In recent months, however, the large-home trend has turned around. According to the U.S. Census Bureau, the average new-home size dropped from 2,629 square feet to 2,438 square feet between the second and third quarters of 2008. In part, this 7-percent drop is attributed to

the tremendous economic pressures facing builders and their customers in a difficult market.

In addition, municipalities are passing rules aimed at reducing new homes' environmental impact, which has aided smaller and green development. For example, Santa Barbara, Calif., requires that any new home larger than 4,000 square feet be built using green techniques certified by the Built Green Santa Barbara program.

Further, the energy-efficiency, healthier indoor air and durability of small green homes are key components that can add value to a property in multiple ways. Green-building-rating programs such as the U.S. Green Building Council's Leadership in Energy and Environmental Design for Homes provide incentive for builders to construct homes with sustainability in mind.

Obstacles to small-home construction or remodeling still remain, however. Overcoming them requires continued education, community activism for changing home-size policy, and developing innovative financing and appraisal approaches that recognize and reward the value that a small home represents.

In an era when foreclosures have reached an all-time high, the trend of smaller green homes and remodels can provide good long-term value — and most important, a potentially lessened financial burden. ■



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