

Town of Los Gatos — Proposal to Accelerate Home Wildfire Mitigation

(for CEA SB-254 consideration)

Purpose

Recommend a two-part package the State can adopt, and localities can help implement, to lower up-front costs for homeowners, accelerate verified wildfire-mitigation work, and support insurance availability and affordability.

A. State Personal Income tax (PIT) Benefit for Verified Mitigation

Policy Design (two taxpayer options; election made at first claim): Provide homeowners a state Personal Income Tax (PIT) benefit for verified, permanently installed wildfire-mitigation work. The taxpayer elects one of the following at first claim:

- **Option A — 100% deduction (full expensing):** An above-the-line deduction equal to 100% of the verified, net project cost in the tax year the work is completed.
- **Option B — 100% refundable credit:** A refundable credit equal to 100% of the verified, net project cost, subject to per-home caps and annual appropriations, and assignable at the taxpayer's option to a financing administrator (e.g., to prepay principal on a PACE assessment at funding).

Eligible Measures (aligned standards): Use Safer-from-Wildfires and IBHS Wildfire Prepared Home checklists, limited to permanently installed improvements such as ember-resistant vents, eave/soffit/gutter hardening, ignition-resistant roofing, windows and doors, decks and fences, and non-combustible Zone 0 hardscape (for example, gravel or masonry within 0-5 feet).

Note: Ongoing vegetation maintenance and defensible-space services are not financed via PACE and, if incentivized, should be handled in a separate program.

Design Guardrails:

- **Net-of-aid only:** Benefit base is the homeowner's out-of-pocket cost after grants, rebates, insurance proceeds, or federal credits (if enacted).
- **No double-counting / one-benefit rule:** Taxpayers may claim either the 100% deduction or the 100% credit for the same project, not both. If a federal credit is received later, the State benefit is recaptured/adjusted to maintain net-of-aid.
- **Targeting & caps:** Apply per-home caps (e.g., \$10k-\$15k/yr), income phase-outs if desired, and eligibility mapping to CAL FIRE FHSZ with crosswalk to CPUC Tier 2/3 HFTD and local WUI overlays.
- **Verification & privacy:** Issue a Mitigation Certificate (photos + work details). Request CDI convene carriers to standardize a certificate data schema (IBHS/Firewise-compatible) recognized under approved filings. Certificates are homeowner-held; the Town/State does not transmit to insurers without owner consent.

B. PACE Wildfire-Mitigation Financing

Program-Design: Standardize and strengthen Residential PACE implementation for wildfire-hardening under existing SB 465 authority by adopting a uniform eligible-measures list aligned to Safer from

Wildfires, ensuring consistent availability in mapped hazard zones (CAL FIRE FHSZ with a crosswalk to CPUC Tier 2/3 HFTD and local WUI overlays), and delivering below-market, fixed rates through state credit enhancement or targeted rate buydowns. Repayment occurs via the property-tax bill as a separate, non-ad valorem line item and does not change the assessed value used for the 1 percent base property tax. Localities may also enable C-PACE for commercial properties at their discretion; this proposal does not prescribe local scope.

How to Achieve Below-Market Rates

- List Safer-from-Wildfires and IBHS measures as eligible; use pooled bonds and State credit enhancement or targeted interest-rate buydowns to reduce homeowner rates below prevailing unsecured-loan rates.
- Offer fixed terms matched to useful life (typically 10–20 years for most envelope measures, longer for roofs and hardscape). Absent buydowns or credit enhancement, administrators' base rates apply.

Optional State PIT Pathway for PACE-Financed Projects (annual election)

As an alternative to the upfront 100% deduction/credit above, allow PACE borrowers to elect an annual State benefit based on principal repaid:

- **Annual 100% deduction (principal-only):** Deduct 100% of PACE principal repaid each tax year (up to cap).
- **Annual 100% refundable credit (principal-only):** Credit 100% of PACE principal repaid each year (up to cap; credit may be refundable).
- Interest remains governed by existing mortgage-interest rules and is not part of this annual base.
- Anti-double-counting: The annual election is in lieu of the upfront 100% deduction/credit for the same project.

Consumer Protection and Mechanics:

- Align with the CFPB Residential PACE rule (Truth-in-Lending ability-to-repay and standardized disclosures) effective March 1, 2026.
- Some mortgage lenders require PACE payoff at sale or refinance; disclose escrow and DTI impacts up front.
- Tax treatment (existing law): Consistent with mortgage-interest rules, only the interest portion of a PACE assessment may be deductible if eligibility criteria are met; principal is not deductible. PACE assessments are not ad valorem property taxes.
- Verification uses the same homeowner-held Mitigation Certificate (shareable at the owner's election with insurers to pursue any available discounts).
- Statutory timing: Recommend extending or removing the January 1, 2029 sunset on wildfire-safety PACE authority to ensure program continuity.

Regulatory Alignment and Guardrails

The program supports CDI's mitigation-rating framework. The Town and State do not set rates or underwriting rules; discounts and eligibility remain actuarial and carrier-specific under CDI-approved filings. The Mitigation Certificate provides standardized proof; CDI would define the schema with carriers. Certificates are homeowner-held; the Town does not transmit to insurers without owner authorization. Primary eligibility mapping uses CAL FIRE FHSZ with a crosswalk to CPUC Tier 2/3 HFTD and local WUI overlays.

Economics and Break-Even (illustrative, not guarantees)

Assumptions: project cost \$12,500 (vents, eaves, Zone 0); PACE 5.5% APR, 15-year term (below-market via State buydown/credit enhancement); PIT bracket 9.3%.

- PACE annual assessment: $\approx \$1,226/\text{yr}$ ($\approx \$613$ per semiannual installment; $\approx \$102/\text{mo}$). Comparable unsecured loan 10%/5-yr $\approx \$266/\text{mo}$.
- Option A — 100% deduction (upfront, project cost): Year-1 State tax reduction equals the taxpayer's marginal PIT rate $\times$ net project cost. Example: at 9.3%, $\$12,500 \times 9.3\% = \$1,163$; at 12.3%, $\$1,538$; at 6.0%, $\$750$.
- Option B — 100% refundable credit (upfront, project cost): Year-1 State benefit equals 100% of net project cost up to the cap. Example: if the cap $\geq \$12,500$, the credit is $\$12,500$. If assigned to the PACE administrator at funding, the principal can be prepaid immediately, leaving only interest cost; otherwise the homeowner receives the refund and pays PACE over time.
- Annual principal election (PACE borrowers): Year-1 principal repaid $\approx \$552$ on this schedule; the annual 100% deduction would reduce taxable income by $\$552$ ($\approx \$51$ at 9.3%), or the 100% credit would be $\$552$. The annual amount grows each year as principal amortizes. This election is in lieu of the upfront benefit.
- PACE interest (existing law): Year-1 interest $\approx \$674$; at a 9.3% bracket this yields $\approx \$63$ of State tax reduction under mortgage-interest rules (if eligibility criteria are met).
- Insurance savings vary by carrier/verification. To offset the $\$1,226/\text{yr}$ assessment purely with premium savings, the required discount on total premium is approximately: $\$8,000 \rightarrow 15.3\%$; $\$10,000 \rightarrow 12.3\%$; $\$12,000 \rightarrow 10.2\%$; $\$14,000 \rightarrow 8.8\%$. If a carrier applies discounts only to the wildfire portion (e.g., FAIR Plan), adjust accordingly (e.g., 12.3% total $\approx 20.5\%$ on a 60% wildfire portion).
- Note: If the upfront 100% refundable credit is assigned to prepay PACE principal, the annual assessment is largely eliminated; remaining homeowner cost is mainly interest (declining over time), further offset by any insurance savings.

Alignment and Requested CEA Actions

- Include both tools, the PIT benefit and PACE below-market financing, in SB-254 recommendations to the Governor and Legislature.
- Provide model statutory language, a standardized eligible-measures list, and the Mitigation Certificate data schema (developed with CDI and carriers).
- Coordinate with CDI, CAL FIRE, Cal OES, CPUC, FTB, and CSCDA to ensure a single, simple homeowner pathway from financing to insurer documentation and potential discount.
- Recommend extending or removing the January 1, 2029 PACE wildfire-safety sunset.

- Provide model statutory language for both taxpayer options: (i) 100% above-the-line deduction on verified net project cost, (ii) 100% refundable credit on verified net project cost (with per-home caps, income targeting, assignability to reduce PACE principal, and anti-double-counting).

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