Understanding the CAPITAL GAINS TAX

As part of the 2017 Budget Proposal, Governor Inslee proposed a new 7.9% tax on capital gains income, similar to proposals in the Washington Legislature during the 2015 Session. While supporters of a capital gains income tax assert that it would apply only to assets that don't currently generate any tax revenue for Washington State, or would impact only the "1%," the reality is much different. Real estate and small businesses generate substantial tax revenues for Washington State and local government both during ownership and at sale.

Washington REALTORS® and the Washington Hospitality Association have analyzed how the proposed 7.9% state capital gains income tax would impact two common scenarios: (1) the sale of a small rental property; and (2) the sale of a restaurant business. This analysis shows that total taxes on the sale of real estate would be 45% of the gain, and for the sale of the restaurant business, taxes would be over 100% of the gain.

Our point? Real estate and small businesses already generate substantial tax revenues for Washington State and local governments during their ownership and sale. The tables to the right show the tax impacts on these two examples under Governor Inslee's 7.9% capital gains income tax proposal.

Real Estate Example: 4-plex Housing

Couple (filing jointly) buys a modest 4-plex housing unit in 2000 for $550,000 as investment property for anticipated retirement. Assume all units are same size and value. The couple live in one of the units as their primary residence and rents out the other three units to supplement income and mortgage payments. The rental units are placed into service on 1/1/2000. Upon retirement in 2017, the couple sells the 4-plex. Sale price is $1,500,000.

WA Capital Gains Tax (after exemption limit)	$60,114
WA State and Local REET at 1.78%	$26,700
Federal Capital Gains Tax and Recapture of Depreciation	$131,484
State and Local Property Taxes Paid During Ownership	$149,597
Total Taxes Paid During Ownership and at Sale	$367,895
Total Federal, State, and Local Taxes Paid as a % Gain	**45%**

Small Business Example: Sale of Restaurant Business

Family buys small commercial building and opens restaurant in 1990. Purchase price is $200,000. In 2000, family purchases second small commercial building in adjacent city and expands restaurant to second location. Purchase price for second building is $300,000. Both restaurants employ and have employed 10 persons. With the original owners nearing retirement, the family decides to sell the two restaurants:

	Original Restaurant/Building	Second Restaurant/Building
WA Capital Gains (after exemption limit)	$37,525	$29,805
State and Local REET, at 1.78%	$10,680	$10,680
Federal Capital Gains, Including Recaptured Depreciation	$123,750	$104,545
Total Taxes Paid on Sale	$171,955	$145,030
Historical Total Taxes Paid and Collected	Original Restaurant/Building	Second Restaurant/Building
State and Local Property Tax	$72,399	$81,598
State Personal Property Tax	$13,125	$10,625
WA B&O Tax	$118,576	$75,458
Unemployment Taxes (Assume 2%)	$79,200	$50,400
Worker's Comp (Rate $0.4134/hour)	$163,706	$104,177
Total Taxes Paid During Ownership and at Sale	$618,961	$467,288
Total Federal, State, and Local Taxes Paid as a % of Gains	118%	108%

Ironically, other forms of retirement income that have value similar to real estate or small business sales would be exempt from the proposed 7.9% capital gains income tax. For example, consider a person who is a PERS 1 retiree or holder of a company pension, who has average life expectancy, a retirement based on a final salary of $65,000, and an annual retirement benefit of $39,000. This person would receive total retirement income exceeding $500,000. This amount exceeds the taxable gains from many typical sales of real estate or small businesses—and yet would be exempt from the proposed capital gains income tax.

Washington REALTORS®
Promoting expertise in real estate

Washington Hospitality Association

Washington REALTOR® Support

...for Improving the Growth Management Act, Housing Supply, and Low-Income/Homeless Housing Programs

Lack of buildable land, low housing inventory, and skyrocketing prices continue to impact families in many parts of Washington State.

REALTORS® are supporting a number of different proposals to address these problems that will assist buyers and renters at all levels of income and need.

Senate Bill 5254:

- Improve the process in the Growth Management Act used to analyze the availability of land for housing in Buildable Lands Reports.
- Streamlines permitting and environmental review for multi-family or high-density housing developments.
- Ensure that housing market metrics such as affordability and inventory are reviewed in areas where housing issues like price & supply are most problematic.
- Reinforce that the GMA's population projections assigned to cities are not maximum growth levels, but minimums that cities may choose to exceed.
- Ensure that local GMA Comprehensive Plans can be adopted using the most up-to-date data on population projections from the Office of Financial Management.
- 10-year extension of the $40 document recording surcharge that funds local homelessness programs to 2027, to match proposed revisions to the state's homelessness prevention plan requirements.
- Allow local Real Estate Excise Tax (REET) revenue to be used for capital costs of homelessness housing until 2019, as a source of funding until cities have authority to seek an additional .1% sales tax for low-income housing and homelessness programs.
- Modify the existing property tax exemption for construction of new affordable housing units to apply to the preservation of existing housing units made available to low-income tenants.

Bill Being Drafted:

- Stimulate the market for condominium construction by reforming condominium construction liability laws based on University of Washington Runstad Center Report.