



Build Homes, Build Revenue

A smarter alternative to an income tax

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Closing Washington's housing production gap by building 20,000 additional homes annually could generate roughly \$603 million in state revenue.

■ Executive Summary

One year after the largest tax increase in Washington State history, lawmakers are again considering major changes to the state's tax structure. With just under a month remaining in the legislative session and a multibillion dollar budget shortfall, the legislature is actively debating SB6346/HB2724, a new personal income tax, which includes an income tax on state-based small and medium-sized businesses.

This report evaluates whether expanding housing supply can address the need for additional state revenue more effectively than new income-based taxation.

This report finds that closing Washington's housing production gap by building 20,000 additional homes annually could generate roughly \$603 million in state revenue, or 23.6% of the projected first-year revenue from the proposed income tax. Similarly, a 13% growth in the overall construction industry could also produce revenue equivalent to one quarter of the income tax's projected first-year revenue.

These findings indicate that a modest slowdown in housing production and construction activity caused by the proposed income tax could quickly erode existing revenue streams enough to substantially offset the tax revenue generated from the industry. In contrast, encouraging homebuilding and supporting the construction sector presents a more effective approach to boosting state revenue and housing affordability.

■ Background

The Building Industry Association of Washington (BIAW) and the Washington Center for Housing Studies (WCHS) have anticipated the tax debate and its implications. Throughout the fall, we documented a growing budget imbalance driven by a downturn in residential construction, warned of Washington's Rainy-Day Fund ranking among the weakest nationally, highlighted worsening state economic forecasts, and commissioned a study from the National Association of Home Builders (NAHB) estimating the economic impacts of homebuilding in Washington.

Despite concerns, the legislature continues to emphasize tax-based solutions to the current fiscal instability. Consequently, this report serves as a continuation of our prior work, examining how policies that incentivize increased homebuilding can function both as a response to the housing affordability crisis and an alternative source of state revenue.

■ Income Tax Proposal

Washington's proposed "millionaires' tax" would impose a 9.9 percent personal income tax beginning in 2028 on Washington taxable income exceeding \$1 million. Despite being labeled as a "millionaire's tax," the proposal would primarily affect small business owners, often registered as pass-through entities, (LLCs, S corps, partnerships, and sole proprietorships), whose business income flows directly onto their personal tax returns. By contrast, large corporations, often registered as C corporations are taxed at the entity level, and shareholders are taxed only on distributed personal income such as wages or dividends. As a result, C corporations are generally insulated from direct exposure to a personal income tax on business earnings, while pass-through small business owners often cannot meaningfully separate business income from personal income for tax purposes.

Homebuilding often relies on one-time or cyclical income. A strong year, partial sale, refinancing, or catch-up payment can push a construction company past \$1M, creating significant personal tax liability.

The current proposal offers no ability to carry forward losses. Small business owners can't offset profitable years against prior bad ones, turning normal income swings into potentially crippling taxes.

The lack of loss-carry-forward will incentivize greater reliance on debt financing, as borrowing smooths taxable income. Incentives for unsound risk-taking in construction were already exposed during the 2008 housing collapse, after which Washington lost nearly 40 percent of its homebuilders and never fully rebuilt that capacity. Housing permits and completions still have not returned to their previous levels, and even at the market's peak in 2021, units permitted per capita remained below the highs of the mid-2000s permitted.

Similarly, it encourages a shift away from for-sale housing toward build-for-rent development, where income streams are more predictable. Additionally, increased tax burdens in low-margin industries like construction will have to be passed through to consumers in the form of higher home prices.

Methodological Approach, Assumptions, and Limitations

Construction activity is a major driver of state revenue, primarily through retail sales tax and the state real estate excise tax (REET).

Policies that promote homebuilding expand taxable activity by increasing employment, material purchases and property transactions. In contrast, personal income taxes discourage productive behavior.

This analysis quantifies how increased homebuilding can serve as an alternative source of state revenue.

First, it estimates how much additional state revenue would be generated if Washington closed its housing production gap and met its stated housing targets.

Next, it estimates the growth in homebuilding and the broader construction industry required to generate revenue equivalent to roughly 25% of the projected first-year revenue from the proposed income tax, a share comparable to the construction sector's contribution to other taxes, such as the state sales tax.

Official projections indicate approximately \$2.55 billion in revenue in fiscal year 2029, the first year of implementation, but do not provide a breakdown by industry or pass-through income, forcing us to use the 25% figure as an upper-bound assumption for sector-specific impacts.

This analysis focuses exclusively on two revenue streams that accrue directly to the state: the state sales tax and the state REET. It excludes local government revenues, permit and impact fees, job creation, and the indirect economic multipliers that result from household generation.

New housing also increases assessed property values and generates ongoing property tax revenue, but those effects are excluded here due to jurisdictional variation and data limitations.

To the extent construction changes, the resulting long-term revenue change would likely be larger than reflected in these figures. As a result, the estimates should be interpreted as a narrow picture of the fiscal benefits of increased homebuilding.

This report uses the \$2.55 billion revenue figure for FY 2029, as the income tax is fully levied starting January 1, 2028, with the first returns due in April 2029. FY 2029 is officially categorized as a "partial" revenue year, because it receives a single large payment rather than a full year of prepayments, which is projected to reduce compliance.

However, \$2.55 billion represents the estimated full-year equivalent revenue and provides a consistent baseline for comparison with later-year projections. Subsequent tax revenue projections are \$3.45 billion for FY 2030 and \$3.3 billion for FY 2031.

Part A: State Revenue from Closing the 20,000-Unit Housing Gap

Washington policymakers estimate the state needs approximately 50,000 new housing units annually to meet population growth and affordability needs. Statewide permit data is only available through October 2025, showing just under 30,000 units were permitted. Because permits slow during the winter months, and many permitted projects aren't completed, this analysis assumes a projected annual housing production shortfall of roughly 20,000 units.

We estimated state revenue from closing this gap by calculating the revenue associated with constructing an additional 20,000 homes. The estimate includes only two revenue streams that accrue directly to the state: the state REET and the state sales tax attributable to new residential construction. We calculated REET revenue by applying state excise tax rates to the estimated number of home sales generated by new construction. We calculated sales tax revenue by applying the state sales tax rate to the taxable portion of a home's construction-related expenditures.

The home construction revenue estimate is calculated as:

Revenue from new construction = (Average state REET per home × estimated home sales from new construction) + [(Median home price × percent taxed during construction) × state sales tax rate]

The analysis assumes a median home price of \$610,800, according to Redfin. State REET rates are taken from Washington Department of Revenue schedules and applied according to statutory price tiers. The state sales tax rate is 6.5 percent. Consistent with BIAW member feedback, at least 50 percent of the home sale price is used to reflect taxable construction-related expenditures such as labor and materials. Each newly constructed home is assumed to generate 1.5 home sales, reflecting typical housing market chain effects.

Part B: Construction Activity Growth Required to Match Income Tax Revenue

To benchmark the scale of potential revenue from housing-driven growth, the analysis also uses overall construction and home sale tax data. A recent study sponsored by the Association of General Contractors estimates that the construction industry (including suppliers and specialty contractors, as well as residential and commercial contractors) generated approximately \$3.8 billion in annual state sales tax revenue in 2024 (Schaufelberger, 2025). In addition, statewide REET collections totaled approximately \$1.2 billion in 2024, according to the Department of Revenue.

We used these figures to construct an approximate comparison metric that evaluates how much growth in construction activity would be required to directly generate revenue comparable to the proposed personal income tax.

The overall industry growth estimate is calculated as:

Income tax revenue equivalence ratio = Percentage of projected income tax revenue ÷ (construction-related state sales tax + state REET)

This ratio represents the percentage increase in construction-related economic activity and home sales required to produce an equivalent share of state revenue.

Results

Closing Washington's housing production gap by constructing an additional 20,000 homes annually would generate an estimated \$603,217,200 in state revenue directly via real estate excise taxes and state sales taxes. This accounts for 23.6% of the revenue projected from the proposed personal income tax in its first year of implementation. **Put simply, allowing the industry to meet Washington's stated housing production goal would generate nearly one-quarter of the proposed income tax's first-year revenue.**

At the industry level, total home sales and construction activity would need to grow about 13% to produce one quarter of the revenue projected from the proposed personal income tax. **In practical terms, a relatively modest expansion in construction activity and home sales (13%) would generate revenue comparable to 25% of the expected revenue from the first year of the proposed income tax.**

This growth is not unreasonable, as market incentives and disincentives can cause significant year-over-year fluctuations in construction. For example, the roughly 30,000 units permitted statewide through

October 2025 represent a 48% decline from the recent peak of nearly 57,000 units in 2021, according to Census Data. However, implementing the proposed income tax may impede a return to this growth, limiting economic activity and diminishing state revenue.

Importantly, these findings reflect only the construction industry and do not account for broader supply-side effects across the economy. The proposed income tax applies to a wide range of pass-through businesses beyond construction. While the construction industry is particularly susceptible, policies that discourage investment and expansion across sectors are similarly likely to reduce economic activity and associated tax collections.

Official revenue projections for the proposed income tax do not provide sector-specific detail, making it difficult to assess the total potential collections from the construction industry.

However, the analysis presented here indicates that within the construction sector, an income tax imposed without loss carryforward provisions could quickly suppress activity to a degree that materially offsets projected revenue gains. **Even a modest decline in housing production could reduce existing revenue streams enough to substantially erode the income tax revenue collected from construction.**

We have also developed an interactive housing revenue calculator that allows users to input different levels of housing production and observe the corresponding changes in projected tax revenue, providing a transparent way to test the sensitivity of these estimates.



Revenue Calculator

■ Policy Implications and Recommendations

Pursuing the income tax would be counterproductive to expanding housing supply, which is essential for improving housing affordability, supporting economic growth and generating substantial state revenue.

The Governor has already indicated that the current deficit will be addressed through a combination of budget adjustments and alternative tax measures, noting that an income tax would primarily finance future expenditures rather than resolve the existing deficit.

Eliminating the proposal would better align fiscal policy with the state's stated housing and economic objectives. At a minimum, any personal income tax proposal should allow for the carryforward of losses, enabling small business owners to offset profits in future years against prior losses.

In the end, the proposed income tax would hit small businesses, homebuilding, and local governments the hardest. It could also make state revenue less stable over time. Instead, encouraging more homebuilding and investment would grow revenue while also helping solve Washington's housing shortage.

If enacted, the policy would likely undermine its stated objectives of tax equity, economic fairness, and the sustainable funding of essential services. Instead, encouraging more homebuilding and investment would grow revenue while also providing more jobs and helping solve Washington's housing shortage.

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