How Will I Be Taxed When Selling My Vacation Home?

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September 19, 2023

Selling your vacation home can be a bit of a nerve-wracking experience when it comes to taxes. When you sell any property for more than what you paid for it, you can expect to deal with capital gains tax. However, selling a property that isn't your primary residence involves some extra considerations. While you can often sidestep capital gains tax on your primary house using the home sale tax exclusion, unfortunately, you don't get the same luxury when it comes to selling a vacation property.

Capital Gains Tax

Any profit made from the sale of a vacation home is subject to capital gains tax. To calculate your tax liability, you'll need to subtract the adjusted cost basis from the final selling price. Your adjusted cost basis is the original purchase price of the house, adjusted for expenses like closing costs, deductions, and significant renovations/improvements.

You can only include improvements that add to the value of your home, like replacing the roof or renovating the kitchen. Routine repairs meant to maintain the property's condition don't qualify. Including eligible expenses in your adjusted cost basis can help reduce the amount of tax you have to pay.

For instance, if you bought the house for $500,000 and spent $50,000 on a kitchen renovation, your adjusted cost basis is $550,000. Now, if you sell the home for $750,000, you'll have a $200,000 realized gain that can trigger either short-term or long-term capital gains tax.

> **Short-term Capital Gains:** If you've owned the house for a year or less, it's considered a short-term capital gain. Short-term gains will be taxed at your ordinary income tax rate, ranging from 10% to 37%. This rate depends on your annual ordinary income.
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> **Long-term Capital Gains:** If you've owned the house for over a year, it qualifies as a long-term capital gain. Long-term gains qualify for lower tax rates, ranging from 0% to 20%. This rate is based on your total taxable income in a given year.

If you happen to sell the house for less than your adjusted cost basis, you'll have a capital loss. While many investments allow you to deduct this loss from your taxable income for the year, this rule does not apply to vacation homes. Capital losses from a vacation home are not deductible.

State Tax

Any profit taxable at capital gain rates may also be subject to state income tax. When selling an out-of-state vacation home, you'll have to pay income tax in the state where the home is located. Some states have no income tax, while others charge north of 10%.

Some states and counties may impose real estate transfer taxes (i.e., deed transfer tax) when you sell a property. Whether you'll have to pay transfer fees and how much depends on where the property is being sold. The good news is that you can often include these fees in your adjusted cost basis when calculating your tax liability.

The Bottom Line

While selling a home can be stressful, the kind of property you're putting on the market can sway how much your tax burden will be. Vacation homes don't qualify for the home sale exclusion and will be subject to capital gains tax on any gains. Your exact tax rate will depend on how long you owned the home and your annual taxable income.