Capital gains

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The aim of the capital gains tax (CGT) provisions (Parts 3-1, 3-3 and 3-5 of the *Income Tax Assessment Act 1997*) is to tax, as income, gains made on the occurrence of a CGT event.

Examples of such events include when:

- a CGT asset is disposed of;
- a CGT asset is lost or destroyed;
- there is cancellation, surrender or redemption of shares;
- an agreement not to work in a particular industry for a set period of time is entered into;
- a trust is created over a CGT asset;
- a trustee of a unit trust makes a non-assessable distribution to a unitholder;
- a company makes a payment (not a dividend) to a shareholder;
- a lease is granted, renewed or extended;
- a deposit is forfeited because a sale or other transaction does not proceed; and
- a taxpayer stops being an Australian resident.

Each CGT event from which a capital gain or capital loss can arise is covered by a separate provision which specifies when the CGT event is considered to have occurred, the method of calculating any capital gain or capital loss and any exceptions (for example, when a capital gain or capital loss arising from the occurrence of the CGT event should be disregarded). This approach makes it easy for taxpayers to identify and determine whether or not their particular circumstances give rise to a capital gain or capital loss.

Determining capital gain or capital loss

For some CGT events that occur in relation to a CGT asset which is owned by the taxpayer, it is necessary to calculate the capital proceeds and the cost base or reduced cost base of the CGT asset to determine the capital gain or capital loss which arises.

'Capital proceeds' is the term used to describe the amount of money or the market value of any other property received by a taxpayer in respect of the happening of the CGT event.

'Cost base' is the term used to cover the total of amounts paid or the market value of other property given in respect of acquiring the asset together with certain costs and expenditures incurred in or when acquiring, holding and disposing of the asset. In many cases, deductible, recouped and other amounts cannot be included. Provisions can apply to reduce the cost base. In certain circumstances, amounts making up the cost base can be indexed to allow for inflation while the asset is held.

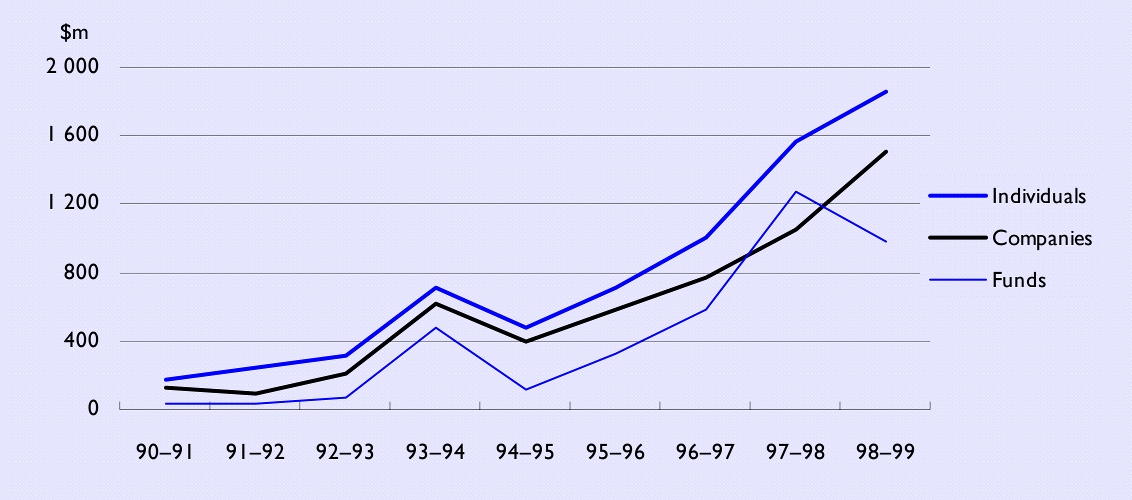
The 'reduced cost base' of a CGT asset is similar to the cost base, the main difference being that no indexation is included.

If the capital proceeds are more than the cost base, there is a capital gain. If the capital proceeds are less than the reduced cost base, there is a capital loss. If the capital proceeds are less than the cost base but more than the reduced cost base, there is neither a capital gain nor a capital loss.

With other CGT events, the cost base and reduced cost base of an asset are not relevant in calculating the capital gain (for example, the granting of a lease or the forfeiture of a deposit). Rather, the capital gain or capital loss is calculated simply by comparing the capital proceeds with incidental costs (legal expenses, for example) incurred in relation to the CGT event. For instance, when an agreement not to work in a particular industry for a set period of time is entered into, a capital gain will arise if the money received for giving the undertaking is more than the legal expenses incurred in entering into the agreement. A capital loss will arise if the money is less than the legal expenses.

Broadly, if the total amount of capital gains for an income year exceeds the total amount of capital losses for the income year (plus any capital losses that can be carried forward from previous income years), the taxpayer has a net capital gain which is included in assessable income. If the total amount of capital gains is less than the total amount of capital losses for the income year, the taxpayer has a net capital loss for the income year which cannot be deducted from assessable income. It can only be applied in reducing the amount of the net capital gain for a subsequent income year.

Figure 13.1: Tax payable on capital gains



In certain circumstances, the amount of tax payable on a net capital gain is calculated according to an averaging formula which takes the amount of tax payable on one-fifth of the gain and then multiplies that amount by five. This amount is then added to the tax that is payable on other income.

Tax payable on capital gains

In 1998–99, $4.4 billion in tax was payable by individuals, companies and funds, on net capital gains totalling $17.5 billion.

The amount of tax payable on net capital gains has increased considerably over the past decade. This increase can be attributed to many factors such as the increase in the value of real estate, the privatisation of government assets and the subsequent increase in shareholdings, and the share market boom over the last decade.

Disposal or sale of an asset is still the most common CGT event. Asset disposal may be related to a range of economic and social factors as well as to specific events. As a result, tax payable on capital gains is difficult to forecast.

Between 1994–95 and 1998–99, the number of individuals liable for tax on net capital gains has increased nearly three-fold from 270 531 to 766 390. The total value of their capital gains increased from $1.5 billion to $5.4 billion. There are many reasons for this. As interest rates declined, Australians looked beyond traditional savings accounts to make their money work more effectively. This, combined with several high profile floats on the stock exchange in recent years, has led to Australia's having one of the highest rates of per capita share ownership in the world. The result of this is increasing revenue through sales of shares.

Individuals and companies paid the largest proportion of tax on net capital gains, accounting for 43% and 35% respectively. Funds accounted for 23% of total tax paid.

The total value of gains was highest for funds, at $6.6 billion, down from $8.5 billion in the previous year. However, funds were liable for proportionately less tax due to the lower taxation rates applicable.

Table 13.1: Tax payable on capital gains

	Number[1]	Amount of gains	Tax on gains[2]	Average tax on gain
		$m	$m	$
Individuals	766 390	5 369	1 862	2 430
Companies	13 609	5 523	1 508	110 809
Funds	45 563	6 598	986	21 640
Total	**825 562**	**17 490**	**4 356**	**5 276**

1. Excludes non-taxable entities.

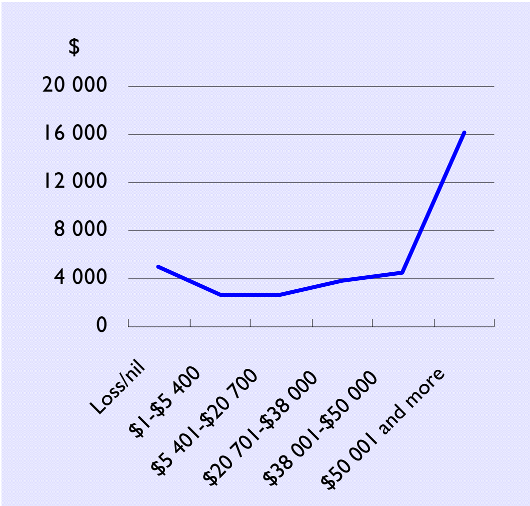
2. Tax payable on capital gains is estimated based on entity type and tax rates.

Table 13.2: Taxpayers with capital gains by grade of taxable income

Grade of taxable income	Individuals: With capital gains	Individuals: All taxpayers	Companies: With capital gains	Companies: All taxpayers	Funds: With capital gains	Funds: All taxpayers
	no.	no.	no.	no.	no.	no.
Less than $20 700	173 626	2 401 374	3 850	129 811	14 662	61 737
$20 700–$37 999	260 331	3 110 073	1 607	32 024	8 699	25 568
$38 000–$49 999	135 853	1 273 683	910	13 797	4 257	11 482
$50 000–$99 999	156 068	1 085 332	2 135	29 592	10 339	27 674
$100 000–$499 999	38 582	164 849	3 478	35 673	6 804	14 917
$500 000–$999 999	1 378	3 913	722	5 755	236	545
$1 000 000–$4 999 999	520	1 210	659	4 372	261	595
$5 000 000 & more	32	56	248	1 471	305	397
Total taxable	**766 390**	**8 040 490**	**13 609**	**252 495**	**45 563**	**142 915**
No tax payable	**160 178**	**1 754 077**	**7 031**	**337 129**	**10 227**	**32 757**

The proportion of taxpayers liable for tax on net capital gains increases as taxable income increases. For example, only 8% of taxable individuals in the $20 700–$37 999 taxable income range had a tax liability for net capital gains. This compares to 35% of people in the $500 000–$999 999 taxable income range. Overall, 71% of all tax paid on net capital gains by individuals was paid by those with a taxable income of more than $50 000.

Figure 13.2: Average net capital gains for individuals by grade of taxable income



In 1998–99, individuals who had a loss or no taxable income had higher average net capital gains than those who had a taxable income of $50 000 or less.

The average net capital gain for individuals was $6225. Males had an average capital gain of $7211 while females had a lower average of $5190.

Source of capital gains

Across all taxpayer groups in 1998–99, the highest proportion of capital gains was realised in respect of shares (47%), followed by trust distributions (24%) and real estate (14%). No statistics are available to indicate the source of gains attributable to trust distributions.

For individual taxpayers, $2.5 billion in net capital gains—nearly half of the total—was mainly from shares and $763 million was mainly from real estate. A total of $1.3 billion of net capital gains arose from trust distributions.

For companies, $2.7 billion—nearly half of the total of net capital gains—came from shares. Nearly $500 million of net capital gains arose from trust distributions, with a further $357 million from real estate.

For trusts, $4.3 billion—nearly two-thirds of the total of net capital gains—arose from shares. A further $31 million of net capital gains arose from real estate and $414 million from trust distributions.

Tax reform and capital gains

Fundamental changes have been made to the capital gains tax regime as part of the government's business tax reform plan. The existing tax regime discouraged the realisation of assets and capital mobility and resulted in reduced economic efficiency. The new reforms are intended to improve asset management, create greater participation by individuals in investment and to achieve a better allocation of the nation's capital resources. The reforms also make Australia's CGT internationally

Table 13.3: Individuals subject to tax on capital gains

Main source of capital gain	Individuals[1]	Amount of gain	Proportion of total gain
	no.	$m	%
Shares	335 547	2 544	47.4
Trust distributions	262 347	1 274	23.7
Real estate	37 457	763	14.2
Units in unit trusts	50 708	174	3.2
Goodwill on the sale of a business	5 995	105	2.0
Equipment and plant including trucks	7 070	36	0.7
Collectables	8 219	37	0.7
Personal-use assets	38 047	161	3.0
Instalment receipts	1 319	5	0.1
Other[2]	19 681	270	5.0
Total	**766 390**	**5 369**	**100.0**

1. Excludes non-taxable individuals.
2. Includes other assets not listed and not stated.

competitive. The reforms include the following changes.

In relation to CGT events that occur after 11.45 am by legal time in the Australian Capital Territory, 21 September 1999 (the start time), the following applies.

- If an asset has been owned for at least 12 months, a capital gain made by an individual or trust is discounted by one-half and a capital gain made by a complying superannuation entity is discounted by one-third. Capital gains must be reduced by capital losses before this CGT discount is applied.
- Indexation is abolished for assets acquired after the start time. For assets acquired before the start time and which are held for at least 12 months, indexation is frozen as at 30 September 1999. If a CGT event happens after the start time, individuals, complying superannuation entities and trusts can choose to calculate any capital gain on a frozen indexation basis or, alternatively, disregard indexation and take advantage of the CGT discount.
- Averaging of net capital gains is no longer available.
- Small business concessions and reliefs have been improved and extended to enable capital gains made by small business taxpayers to be reduced by one or more of four concessions:
  - the 15-year exemption
  - the 50% reduction
  - the retirement exemption
  - small business roll-over
- If an asset is plant at the time of the CGT event, any gain or loss on disposal is brought to account as assessable income or as an allowable deduction. The capital gain and loss provisions will not apply (and CGT concessions would not be available).

Table 13.4: Companies subject to tax on capital gains

Source of capital gain	Companies[1]	Amount of gain	Proportion of total gain
	no.	$m	%
Shares	6 244	2 685	48.6
Trust distributions	3 101	499	9.0
Real estate	1 131	357	6.5
Goodwill on the sale of a business	846	168	3.0
Plant and equipment	1 170	39	0.7
Collectables	42	5	0.1
Other[2]	1 075	1 768	32.0
Total	**13 609**	**5 523**	**100.0**

1. Excludes non-taxable companies.
2. Includes personal-use assets, units in unit trusts, other assets not listed, instalment receipts and sources not stated.

Table 13.5: Funds subject to tax on capital gains

Source of income	Funds[1]	Amount of gain	Proportion of total gain[2]
	no.	$m	%
Shares	27 705	4 327	65.6
Distributions from a trust	12 884	414	6.3
Real estate	661	31	0.5
Collectables	81	2	0.0
Equipment and plant including applicable trucks	45	1	0.0
Other[3]	4 187	1 823	27.6
Total	**45 563**	**6 598**	**100.0**

1. Excludes non-taxable funds.
2. A proportion of 0.0% indicates a proportion of less than 0.05%
3. Includes personal-use assets, units in unit trusts, other assets not listed, instalment receipts and sources not stated.

From 10 December 1999, the following applies.

- A new scrip for scrip roll-over may apply if certain interests in a company or trust are exchanged for comparable interests in an acquiring entity as part of a takeover or merger. Partial roll-over is available if the exchange involves other consideration such as cash.
- Venture capital investment in Australia is promoted by the exemption of capital gains earned through pooled development funds by Australian superannuation funds and by non-resident tax exempt pension funds.

Detailed tables

The following detailed tables on capital gains can be found on the CD-ROM attached to this publication.

Table 1: Capital gains subject to tax: income years 1990–91 to 1998–99

Table 2: Capital gains subject to tax: by entity and grade of taxable income

Table 3: Capital gains subject to tax: by business line and grade of taxable income