Attachment D

INTRODUCING AN INTERNATIONALLY COMPETITIVE CAPITAL GAINS TAX SYSTEM

The Government will fundamentally reform the way in which capital gains are taxed. From 1 October 1999, individuals will pay no more than 24.25 per cent and superannuation funds no more than 10 per cent on nominal capital gains.

This removes impediments to efficient asset management, improves capital mobility and makes Australia's capital gains tax internationally competitive.

Other changes to capital gains tax dealing with small business reforms, scrip-for-scrip rollover relief and venture capital are set out in Attachments E, F, G and H respectively.

Key features

Reforms to capital gains tax taxation are as follows:

- Indexation of the cost base for calculating capital gains tax for all taxpayers is frozen at 30 September 1999.
- For assets acquired prior to implementation, and held for at least one year, individual taxpayers will have the choice of including in their assessable income either:
  - half the realised nominal gain; or
  - the whole of the difference between the disposal price and the frozen indexed cost base.
- For assets acquired prior to 1 October 1999, and held for at least one year, complying superannuation and related funds will have the choice of including in their assessable income either:
  - two-thirds of the nominal gain; or
  - the whole of the difference between the realised price of the asset and its frozen indexed cost base.
- For assets acquired on or after 1 October 1999, and held for at least one year, capital gains will be taxed at half or two-thirds of the difference between the disposal price and the original cost, for individuals and complying superannuation and related funds, respectively.
- Capital losses can be offset against capital gains so as provide maximum benefits to the taxpayer.
  - Nominal capital losses are to be offset against capital gains net of frozen indexation or the full nominal capital gain before it is reduced to determine the amount included in assessable income.
- Consistent with the existing law, revenue losses will be able to be offset after net capital gains have been determined.

- Averaging of capital gains will no longer be available.
- Assets eligible for depreciation allowances are no longer included in the capital gains tax regime — further details are provided at Attachment B.

Commencement dates

- Averaging of capital gains no longer applies to the disposal of assets after 11.45 am AEST on 21 September 1999.
- In the case of the disposal of assets eligible for depreciation allowances, all gains over the frozen indexed cost base will be taxed as ordinary income after 11.45 am AEST on 21 September 1999.
- Indexation is frozen at 30 September 1999. The other measures have effect from 1 October 1999.

Current arrangements

A capital gains tax liability arises where there is a real capital gain in the value of the asset between acquisition and disposal. The acquisition price and certain expenses (the cost base) are adjusted by the rate of inflation if the taxpayer owns the asset for at least one year. An averaging system applies to prevent an individual from being taxed on capital gains at a marginal rate higher than that applicable to their other income.

Assets acquired before 20 September 1985 are not subject to capital gains tax. The reforms to capital gains taxed announced by the Government will not disturb the taxation status of those assets.

Why change is needed

There is a need to enliven and invigorate asset management, to stimulate greater participation by individuals in investment, and to achieve a better allocation of the nation's capital resources. The existing capital gains tax arrangements discourage the realisation of assets and capital mobility. Economic efficiency is reduced as a result.

The measures will make the rate of capital gains tax in Australia for individuals competitive to those in other countries, particularly the United States.

Removing indexation and averaging from the capital gains tax regime:

- brings Australia into line with other countries;
- removes complexity from the taxation law;
- reduces compliance costs for taxpayers; and
- in the case of averaging, removes a concession that has led to unintended outcomes.

While companies will lose the benefit of indexation from 30 September 1999, they will receive the ongoing benefit of a lower company tax rate. In addition, shareholders who are either individuals or superannuation funds will benefit through the capital gains tax reforms.