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Taxing personal capital gains: removal of CGT discount

On behalf of myself and Dr Youngdeok Lim (UNSW) and John Minas (University of Tasmania) I attach two papers which reflect our considered view that the CGT 50% discount should be abolished (Re:think Discussion Question 29: "To what extent is the rationale for the CGT discount, and the size of the discount, still appropriate").

The arguments for the abolition of the CGT discount, and for its replacement with an annual exempt amount, are contained in the first attachment ("Evans Lim Minas CGT submission Attachment 1"), which is a paper currently under review with a leading Australian tax journal. This paper argues, on grounds of equity, efficiency and simplicity – and, importantly, on the grounds of fiscal sustainability – that the time is now right for consideration of the appropriateness of the existing preferences for individuals in the capital gains tax (CGT) regime. In particular, it queries whether the 50% CGT discount should continue to be available to individual taxpayers, and makes proposals for a reform that might lead to "improved" outcomes for the tax system and for Australia as a whole. In partial compensation for the removal of the 50% CGT discount, the paper considers the possible introduction of a CGT-free threshold (usually referred to as an annual exempt amount). The paper supports its analysis by estimating potential first round (static) and (where possible) second round (dynamic) effects on tax revenue of such changes, concluding that the proposed changes would not only enhance the equity, efficiency and simplicity of the tax system going forward, but would also result in an overall revenue gain for the government.

The second attachment ("Evans Lim Minas CGT submission Attachment 2") is a draft working paper scheduled to be submitted to a leading international journal. This study uses aggregate time series taxpayer data from Taxation Statistics in Australia for the years 1988-89 to 2012-13, together with a regression analysis based upon a series of variables, to establish taxpayer responsiveness to the effective cut in the CGT rate in 1999-2000. The initial results of the study indicate that capital gain realisations are relatively unresponsive to changes in the tax rate, suggesting that assertions at the time of the introduction of the CGT discount that the policy change could enhance tax revenue collections may have been inaccurate and overstated. Indeed, there may have been a substantial revenue loss to the fisc rather than any form of revenue gain.

On the basis of the research underpinning these two papers we are of the firm view that the CGT discount should be removed. We will be happy to answer any further questions that may arise.

Chris Evans, John Minas and Youngdeok Lim