TREASURY LAWS AMENDMENT (TAX REFORM NO. 3) BILL 2026: CGT ADJUSTMENTS (TRANCHE 2)

EXPOSURE DRAFT EXPLANATORY MEMORANDUM

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Glossary

This Explanatory Memorandum uses the following abbreviations and acronyms.

Abbreviation	***Definition***
AMIT	Attribution managed investment trust
ATO	Australian Taxation Office
Bill	Treasury Laws Amendment (Tax Reform No. 3) Bill 2026: CGT adjustments (tranche 2)
CGT	Capital Gains Tax
ITAA 1936	*Income Tax Assessment Act 1936*
ITAA 1997	*Income Tax Assessment Act 1997*
MIT	Managed investment trust
TAA 1953	*Tax Administration Act 1953*

Chapter 1: CGT adjustments (tranche 2)

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Outline of chapter

1.1 Schedule 1 to the Bill amends the income tax law to give effect to the second tranche of the Government's reforms to CGT, clarifying the operation of the amendments for more complex or specific arrangements and making additional technical and policy changes informed by ongoing stakeholder engagement.

1.2 References to legislation in this Explanatory Memorandum are to the ITAA 1997 unless stated otherwise.

Context of amendments

1.3 In the 2026-27 Budget, the Government announced reforms to negative gearing and CGT to help improve the fairness of the tax system, support home ownership and help fund new tax cuts for workers.

1.4 On 26 June 2026, the *Treasury Laws Amendment (Tax Reform No.1) Act 2026* and *Income Tax Rates Amendment (Tax Reform No. 1) Act 2026* received Royal Assent. These Acts made the following key CGT reforms, to apply from 1 July 2027:

- replaced the 50 per cent CGT discount for individuals, trusts and partnerships with cost base indexation to ensure only real gains are subject to taxation;
- introduced a 30 per cent minimum tax on capital gains, with an exemption for recipients of certain government payments, to ensure gains are subject to a tax rate closer to the tax rate individuals faced during their working life and commensurate with the tax rate paid by most workers; and
- applied the new arrangements prospectively to all capital gains accruing on and after 1 July 2027, including gains accruing on pre-CGT assets, while retaining access to the CGT discount to maintain support for new and affordable housing, and maintaining existing CGT concessions for small business.

1.5 The amendments made by those Acts were the first tranche of legislation to implement the core provisions of the Government's CGT reforms.

1.6 The Government has been consulting with stakeholders on a range of issues in relation to the reforms since the first tranche of CGT reforms passed Parliament. This has included consideration of various complex interactions between the first tranche of CGT reforms and existing tax laws.

1.7 This second tranche of CGT reforms builds on the prior legislation to ensure the reforms work as intended and apply appropriately.

Summary of new law

1.8 Schedule 1 to the Bill amends the income tax law to:

- extend the application of the CGT reforms to AMITs;
- clarify the operation of the CGT reforms relating to trusts (including MITs and AMITs), including:

   - allowing trusts that have no beneficiaries entitled to indexation to choose not to use indexation, and
   - ensuring trusts can apply the CGT discount for new residential dwellings and affordable housing;
- prevent taxpayers with deferred gains or losses in relation to a CGT asset from becoming liable to pay or being entitled to benefit from those losses where the CGT asset is subject to a CGT event that does not represent a substantial realisation of the asset;
- exempt capital gains arising for genuine testamentary trusts, deceased estates and special disability trusts from the 30 per cent minimum tax on capital gains;
- ensure that foreign residents and temporary residents receive CGT discount and indexation outcomes that are pro-rated to the number of days that they are Australian residents; and
- make other technical amendments to ensure the CGT reforms operate as intended.

Detailed explanation of new law

AMITs

1.9 The CGT reforms are intended to apply to capital gains, including the capital gains of trusts. The CGT reforms include a number of provisions to ensure that the reforms apply appropriately to trusts taxed under the general rules for trusts in Division 6 of the ITAA 1936 (including MITs).

1.10 However, the amendments did not address trusts that are AMITs, which are subject to a specific tax regime set out in Division 276. The amendments made by Schedule 1 to the Bill ensures that the new CGT regime applies appropriately to AMITs.

Overview of AMIT regime

1.11 A trust that is an eligible MIT may elect to be an AMIT under Division 276. MITs that elect to be an AMIT are:

- allowed to attribute amounts of income and tax offsets for tax purposes to members on a fair and reasonable basis according to their interests under Division 276 (in lieu of the present entitlement-based methods in Division 6 of the ITAA 1936 and Divisions 115-C and 207-B of the ITAA 1997);

- allowed to apply the underestimates and overestimates (unders and overs) regime to reconcile variations discovered by a trustee between amounts attributed to members (in an earlier income year) and amounts that should have been attributed without adverse tax consequences; and
- treated as fixed trusts with members having vested and indefeasible interest in a share of the income and capital of the AMIT throughout the income year.

1.12 The broad process in determining the capital gains of an AMIT and the attribution of the capital gains to members is as follows:

- the trustee applies the CGT provisions in Parts 3-1 and 3-3 to calculate capital gains and losses and determine eligibility for CGT discounts or CGT concessions in order to calculate net capital gains;
- Division 276 requires amounts to be determined by reference to their tax character. This means that capital gains are identified separately from other forms of income and evidenced in a particular document;
- the trustee works out the amount of the AMIT's capital gains that are attributable to each member (based on membership interest and worked out on a fair and reasonable basis in accordance with constituent documents). This is known as the 'determined member component';
- if a trustee has determined that too much or too little capital gain was attributed in a prior year, an under or over attribution is allocated to the determined member component in the income year that this is identified;
- a member is treated as having derived the capital gain in their own right (rather than as a member of a trust) and in the same circumstances as the AMIT. Individual members include this capital gain amount in their own tax calculations and can apply any provisions available to them (i.e. CGT concessions, discounts, carry forward losses); and
- where a member is attributed a component that has the character of a discount capital gain, the amount is to be treated as double the attributed amount. This ensures that the capital gain before the discount is attributed to the member and the member then applies any CGT provisions applying to their own individual circumstances.

Amendments to CGT provisions (Part 3-1 of the ITAA 1997)

1.13 Schedule 1 to the Bill amends Part 3-1 of the ITAA 1997 to ensure that the rules distinguishing between capital gains and losses arising before and after 1 July 2027 apply to gains and losses arising in AMITs. These amendments provide for AMITs to be deemed to sell and reacquire CGT assets it holds just before 1 July 2027 under Subdivision 112-E, consistent with other kinds of trusts.

1.14 This is achieved by:

- amending the drafting of subsection 112-165(1), which deals with the application of the rules for the deemed disposal and reacquisition of assets held before 1 July 2027 by trusts, to clarify its application to AMITs;
  [Schedule 1, item 20, paragraph 112-165(1)(d) of the ITAA 1997]
- amending subsection 112-165(2), which provides for the deemed sale and reacquisition of CGT assets held by trusts before 1 July 2027 so that the deeming applies for the purpose of the AMIT provisions in Division 276;
  [Schedule 1, item 21, subsection 112-165(2) of the ITAA 1997]
- amending subsection 112-170(3), which deals with gains and losses arising from deemed disposals of trust assets, so that the rules allowing for the deferral of those gains and losses until a realisation event occurs apply for the purposes of the AMIT provisions in Division 276;
  [Schedule 1, item 24, subsection 112-170(3) of the ITAA 1997]
- adding a new paragraph to subsection 102-6(5), which deals with when capital gains are deferred residential gains or deferred non-residential gains, so that this subsection applies to gains made by members of AMITs under Division 276 in the same way as gains made by members of other trusts; and
  [Schedule 1, item 4, paragraph 102-6(5)(c) of the ITAA 1997]
- making various other consequential amendments, including to notes, guidance material and categories of capital gains, to also refer to AMITs and their members and make related clarifications.
  [Schedule 1, items 1, 2, 3, 5, 6, 8, 22, 26, 27, 28, 32 and 37, section 102-6, subsection 110-36(1A), subsection 112-165(2), subsections 112-170(3), (4) and (6), subsection 112-180(3) and section 115-1 of the ITAA 1997]

1.15 Schedule 1 also clarifies the application of the 30 per cent minimum tax on capital gains to gains attributed by AMITs to members. Section 119-5 is amended to confirm that capital gains made during an income year because of section 276-80 (about attribution of gains of AMITs to members) are included in individuals' minimum tax capital gains for an income year.
[Schedule 1, items 58 and 60, subsections 119-5(2) and (3) of the ITAA 1997]

Amendments to AMIT provisions (Division 276 of the ITAA 1997)

Calculation of capital gains that includes indexation and attribution to members

1.16 An AMIT must determine the amounts of capital gains and losses using the new CGT method statement under section 102-5. In doing so, it must assume that the trustee is liable for tax in the same circumstances as an Australian member. When working out if an AMIT has a capital gain arising on or after 1 July 2027, the trustee applies indexation to the cost base (except for the third element) under subsection 110-36(1A) of the new rules.

1.17 Schedule 1 of the Bill amends section 276-85 which relates to working out the determined member component for a member – which is broadly the share of the income, capital and tax benefits of the AMIT attributable to the member. It provides that when working out a determined member component that includes a capital gain worked out using a cost base that includes indexation because it is a gain arising on or after 1 July 2027, then if the member would not have been entitled to use cost base indexation if they acquired and held the asset, an AMIT must work out the amount of the capital gain assuming:

- the cost base was adjusted to remove indexation; and
- no changes were made to how current capital losses, net capital losses from prior income years or quarantined amounts were applied to the capital gain.

[Schedule 1, item 62, subsections 276-85(4A) and (4B) of the ITAA 1997]

1.18 This means that a member will effectively receive a ‘grossed-up’ amount as they are treated as having made the capital gain in the same circumstances as the AMIT but without the gain being subject to indexation.

1.19 This is a similar approach to subsection 115-225(5) which applies to Division 6 trusts. This also reflects the approach under subsections 276-85(3) and (4) where an AMIT member has a determined member component consisting of a discount capital gain, the amount is adjusted to remove the discount by being treated as being double the attributed amount.

Example 1.1 Attribution of an indexed capital gain to an AMIT member

In an income year, an AMIT disposes of a CGT asset that was acquired after 1 July 2027 and chooses to apply the indexation method. The ‘non-residential capital gain’ (see subsection 102-6(1)) before indexation is $800,000. After indexing the asset's cost base, the capital gain is reduced by $200,000, resulting in a non-residential capital gain of $600,000. As there are no capital losses, the AMIT's net capital gain is $600,000.

A component with the character of an indexed non-residential capital gain of $600,000 is attributed to a resident member. The member is taken to have made a capital gain from a CGT event happening in relation to the relevant asset in their own right. Under subsections 276-85(4A) and (4B), the member's determined member component associated with the indexed non-residential capital gain is adjusted to remove the effect of the indexation benefit obtained by the AMIT. Accordingly, the member is treated as having made a non-residential capital gain of $800,000, being the amount of the gain before the AMIT applied indexation to the asset's cost base.

Treating the member as making a non-residential capital gain of $800,000 removes the effect of indexation that was applied by the AMIT. This allows the member to apply indexation if they are entitled to do so in their own right.

Other gross up provisions in Division 276

1.20 Division 276 contains other ‘gross-up’ provisions for discount capital gains. Schedule 1 to the Bill amends these provisions to also ‘gross-up’ capital gains calculated by an AMIT using indexation.

1.21 Section 276-105 ensures that tax is collected on amounts attributed by an AMIT to foreign resident members where those amounts are not dealt with through the MIT withholding provisions. The trustee of the AMIT is assessed on specified attributed amounts. Subsection (7) and (8) gross up discount capital gains so that the trustee is assessed on the entire gain. A similar rule relating to indexation is included. If a determined member component of a character relating to a capital gain is worked out using cost base indexation and the member would not have been entitled to cost base indexation if they held the asset, then cost base indexation is removed. This does not alter the application of the AMIT’s capital losses, previously unapplied net capital losses or quarantined amounts.
[Schedule 1, item 63, subsections 276-105(9) and (10) of the ITAA 1997]

Example 1.2 Division 276 gross up provisions for indexed capital gains

In an income year, an AMIT disposes of a CGT asset that was acquired after 1 July 2027 and applies the indexation method. The non-residential capital gain before indexation is $1,000,000. After indexing the asset's cost base, the non-residential capital gain is reduced by $250,000, resulting in an indexed non-residential capital gain of $750,000.

The AMIT determines a trust component with the character of an indexed non-residential capital gain of $750,000. A foreign resident member is entitled to 20 percent of the attributions of the AMIT. Accordingly, $150,000 of the indexed non-residential capital gain is attributed to the foreign resident member. Under subsections 276-105(9) and (10), the capital gain is grossed up to $200,000, removing the cost base indexation. This ensures that the trustee is liable to pay income tax on the grossed-up amount as the AMIT is not a withholding MIT.

1.22 Section 276-415 provides that a trustee of an AMIT is taxed on shortfall amounts between the determined trust component and determined member components. If the shortfall relates to a discount capital gain, the shortfall is doubled before calculating the trustee's tax liability. This ensures the entire capital gain amount is subject to tax by the trustee. A similar rule relating to indexation is included. If a determined member component of a character relating to a capital gain exceeds what the component would otherwise be because cost base indexation is removed under subsection 276-85(4B), then the determined trust component is increased by the excess. ***[Schedule 1, item 65, subsections 276-415(5) and (6) of the ITAA 1997]***

1.23 If a trust ceases to be an AMIT and discovers an under or over from an income year when it was an AMIT, the under or over will have taxation consequences for the trust in the discovery year. Section 276-810 is amended to provide that in working out whether a trust has an under or over in a discovery year of a character relating to a capital gain from an earlier year, if a determined member component exceeds what the component would otherwise be because cost base indexation is removed under subsection 276-85(4B), then the determined trust component for the earlier income year is increased by the excess. ***[Schedule 1, item 66, subsection 276-810(3) of the ITAA 1997]***

Unders and overs with discount capital gain

1.24 Section 276-305 adjusts the AMIT's trust component of a particular character for an income year to take into account any unders and overs of that character that the AMIT has in the income year. Unders and overs are broadly amounts of a particular character recognised by an AMIT in the current income year arising from an understatement or overstatement when calculating amounts of that character attributable to members in past income years.

1.25 Section 276-345(1) sets out how to work out the amount of an AMIT's under or over of a particular character for an income year (the base year) to be included in a later income year (the discovery year).

1.26 A new subsection is included in section 276-345 to confirm that the discovery year amount and the base year running balance amount are to be worked out in accordance with the law that applied for the purposes of assessments for the base year. This ensures that the CGT reforms do not affect the calculation of the tax position for income years ending before 1 July 2027. ***[Schedule 1, item 64, subsection 276-345(6) of the ITAA 1997]***

1.27 From 1 July 2027 onwards, the capital gains of an AMIT can only be discount capital gains in limited circumstances (such as where the gains relate to new residential dwellings or affordable housing).

1.28 This new subsection clarifies that the unders and overs regime for AMITs continues to operate for trust components including discount capital gains after 30 June 2027. Specifically, an AMIT may have an under or over for a discount capital gain for a base year prior to 1 July 2027 that may be discovered after 30 June 2027. This will be the case even if that capital gain would not have been a discount capital gain if made on or after 1 July 2027.

Amendments relating to trusts (including MITs and AMITs)

Trustee can choose not to use indexation if no beneficiaries entitled

1.29 Schedule 1 of the Bill includes a new section that provides that the trustee of a trust (including an AMIT) can choose not to apply cost base indexation in determining its capital gain from a CGT event if, immediately prior to the CGT event, all of its beneficiaries satisfy one of two conditions.

1.30 A beneficiary of a trust (the first trust) will satisfy the first condition if the beneficiary would not have been entitled to apply cost base indexation had they made the gain in the same circumstances as the trust.
[Schedule 1, item 10, subsection 110-36A(1) and paragraph (2)(a) of the ITAA 1997]

1.31 A beneficiary of the first trust will satisfy the second condition if the beneficiary:

- is the trustee of another trust (the **other trust**); and
- would itself be eligible to choose to not apply indexation under this provision on the assumption that the other trust made the capital gain from the asset, having acquired and held the asset in the same circumstances as the first trust.

[Schedule 1, item 10, subsection 110-36A(1), paragraph 110-36A(2)(b) and subsection 110-36A(3) of the ITAA 1997]

1.32 In other words, this means the trustee can choose to not apply indexation to the cost base of the CGT asset of the trust only where each of its direct beneficiaries or members either:

- is not entitled to apply indexation; or
- is a trustee of another trust that would itself be eligible to choose not to apply indexation (because all of that trust’s beneficiaries are either not

entitled to apply indexation or are trusts who can choose not to apply indexation because of another application of this rule).

1.33 The first case covers the situation where the trust's direct beneficiaries or members are entities that are not entitled to indexation which include:

- companies;
- if the CGT asset is not taxable Australian property—non-residents;
- if the CGT asset is taxable Australian property—non-residents for the whole of the ownership period; and
- complying superannuation funds.

1.34 The second case covers the situation where an interest in a CGT asset is held through a chain of trusts. It allows each trustee in the chain to choose not to apply indexation if each of its beneficiaries or members either fall within the first case or is the trustee of another trust that has itself chosen not to apply indexation under a previous application of the provision.

1.35 The trustee's choice to not to apply cost base indexation applies in working out the following capital gains:

- the trust's capital gain from the CGT event;
- for a trust other than an AMIT, each capital gain that a beneficiary is treated as having made under Division 102 and section 115-215; and
- for AMITs, each capital gain that a member is treated as having made under section 276-80.

[Schedule 1, item 10, subsection 110-36A(4) of the ITAA 1997]

1.36 This choice is available only in a narrow set of circumstances (set out above) only to reduce an unnecessary compliance burden for trustees. It means that trustees do not have to undertake calculations required to use indexation when determining the trusts' capital gains if none of its beneficiaries will be entitled to benefit from indexation.

1.37 If the trust has made the choice under new section 110-36A and makes a capital gain relating to a new residential dwelling or affordable housing, the trustee can only apply the CGT discount in relation to the gain, and is excluded from applying indexation.

1.38 If the trustee has chosen not to apply indexation, the normal cost base rules in Division 110 apply to the calculation of the capital gains.

1.39 The choice not to apply indexation for a gain is made by the trustee. Consistent with other choices for the purposes of CGT, it need not be made in a particular form and simply needs to be reflected in the way the trustee lodges its tax return.

1.40 Consequential amendments are made to section 110-36, including guide material, to reflect this choice for trustees.
[Schedule 1, items 7 to 9, subsections 110-36(1A) and (2) of the ITAA 1997]

Example 1.3 Trustee choice not to apply cost base indexation where no beneficiaries are entitled

ABC Trust disposes of a CGT asset in the 2028-29 income year which it had acquired in 2027. The trustee would ordinarily apply cost base indexation in working out the capital gain.

Immediately before the CGT event, all beneficiaries of the trust are individuals that had been non-residents for the whole period from 1 July 2027. If those beneficiaries had made the capital gain directly in the same circumstances, none of them would have been entitled to apply cost base indexation.

The trustee chooses under section 110-36A not to apply cost base indexation when calculating the trust's capital gain. The gain is therefore worked out using the ordinary cost base rules rather than an indexed cost base.

Trusts can apply the CGT discount for new residential dwellings and affordable housing

1.41 Schedule 1 to the Bill makes amendments to ensure that both Division 6 trusts and Division 276 AMITs can choose to apply the 50 per cent CGT discount for capital gains made at the trust level where the gain arises from a CGT event happening to a CGT asset which is a new residential dwelling under section 115-102 or affordable housing under 115-125 on or after 1 July 2027.

1.42 Amendments are also made to ensure that the CGT discount for new residential dwellings and affordable housing can apply to AMITs and members of AMITs.

New residential dwellings

1.43 Schedule 1 amends the rules providing a CGT discount for individuals and trusts for capital gains relating to new residential dwellings to separate the rules for individuals and trusts.

1.44 The existing section 115-102, which provides the CGT discount for capital gains from new residential dwellings, previously only applied to gains made by individuals, including through a trust. This has not changed. However, section 115-102 is amended to apply appropriately to gains made by individuals that are a member of an AMIT in light of the wider changes made to the treatment of AMITs.
[Schedule 1, items 41 to 46, section 115-102 of the ITAA 1997]

1.45 The amendments to section 115-102 ensure that the CGT discount can apply to an individual on or after 1 July 2027 where they:

- dispose of the new residential dwelling directly; or
- are attributed a trust capital gain relating to the new residential dwelling from a trust under section 115-215 or from an AMIT under section 276-80.

1.46 A new section is included in relation to new residential dwellings and gains made by trusts. This new provision applies to trustees where on or after 1 July 2027 they:

- dispose of the new residential dwelling directly; or
- are attributed a trust capital gain relating to a new residential dwelling under section 115-215 or from an AMIT under section 276-80.

[Schedule 1, item 47, section 115-103 of the ITAA 1997]

1.47 This new section ensures that the CGT discount is applied at the trust level and the discount capital gain flows through to beneficiaries or members where relevant.

1.48 Paragraph 115-100(a), which sets out the discount percentage for new residential dwellings, is amended to refer to both sections 115-102 and 115-103.
[Schedule 1, item 39, paragraph 115-100(a) of the ITAA 1997]

Example 1.4 Division 276 where AMIT invests in a new residential dwelling

In an income year, an AMIT disposes of a new residential dwelling and makes a residential capital gain of $2 million. In calculating its determined trust components, under subsection 115-103(1), the trustee of the AMIT chooses to apply the CGT discount to the residential capital gain (rather than indexation) resulting in a discount capital gain of $1 million. As there are no capital losses, the AMIT's net capital gain is $1 million.

The AMIT attributes the discount capital gain to its member, an AMIT (AMIT B). Under subsections 276-85(3) and (4), the member's determined member component associated with the discount capital gain is adjusted to remove the effect of the discount applied at the AMIT level. Accordingly, AMIT B grosses up the discount capital gain to $2 million as it is treated as having made the residential capital gain before the earlier AMIT applied the discount. The trustee of AMIT B chooses not to apply the 50% discount and applies indexation instead under subsection 115-103(3). After indexing the asset's cost base, the residential capital gain is reduced to $1.5 million. As there are no capital losses, AMIT B's net capital gain is $1.5 million.

Subsequently, a component with the character of the indexed residential capital gain of $1.5 million is distributed to a resident member. Under subsection 276-85(4A) and (4B), the member's determined member component associated with the indexed residential capital gain is adjusted to remove the effect of the indexation benefit applied at the AMIT level. The member is treated as having made a residential capital gain of $2 million, being the amount of the gain before AMIT B applied indexation to the asset's cost base. This allows the member to apply the discount or indexation if they are entitled to do so in their own right.

Affordable housing

1.49 Schedule 1 also amends the existing provisions relating to the CGT discount for investors in affordable housing so that they also apply at both the individual and the trust level.

1.50 Section 115-125, which provide the existing discount for affordable housing, previously only applied to gains made by individuals, including through a trust. This has not changed. However, section 115-125 is amended to apply appropriately to gains made by individuals that are a member of an AMIT in light of the wider changes made to the treatment of AMITs. ***[Schedule 1, items 48 to 51, section 115-125 of the ITAA 1997]***

1.51 A new section is included in relation to affordable housing and gains made by trusts. This new provision applies to trustees where on or after 1 July 2027:

- a CGT event happens to their ownership interest in a dwelling that is used to provide affordable housing; or
- they are attributed a trust capital gain relating to a dwelling used to provide affordable housing under section 115-215 or from an AMIT under section 276-80.

[Schedule 1, item 52, section 115-126 of the ITAA 1997]

1.52 This allows trusts and AMITs continuing access to a 50 per cent CGT discount for investments in affordable housing from 1 July 2027. The additional CGT discount of up to 10 per cent for investments in affordable housing by individuals does not apply for trusts or AMITs (although it is available for individuals in relation to capital gains they receive through a trust).

1.53 Paragraph 115-100(e), which sets out the discount percentage for affordable housing, is amended to refer to both sections 115-125 and 115- 126. ***[Schedule 1, item 40, paragraph 115-100(e) of the ITAA 1997]***

Consequential amendments

1.54 Consequential amendments are made to the following provisions to refer to the new residential housing and affordable property provisions that apply to gains made by a trust:

- paragraph 112-165(1)(f) provides that the deeming provision for trusts does not apply to new residential dwellings or affordable housing; ***[Schedule 1, item 20, paragraph 112-165(1)(f) of the ITAA 1997]***
- subsection 114-30(2) ensures that cost base indexation is not to be used for new residential dwellings or affordable housing if there has been a choice for the CGT discount to apply instead; ***[Schedule 1, item 36, subsection 114-30(2) of the ITAA 1997]***
- subsection 115-225(4) sets out the situations which modifies the calculation determining the attributable capital gains of a trust and requires it to be calculated by removing cost base indexation; and ***[Schedule 1, items 54 to 57, subsection 115-225(4) of the ITAA 1997]***
- paragraphs 119-5(2)(b) and (c) provide that the minimum tax on capital gains does not apply in relation to new residential dwellings or affordable housing unless the relevant entity chooses indexation and the minimum tax over applying the CGT discount. ***[Schedule 1, item 59, paragraphs 119-5(2)(b) and (c) of the ITAA 1997]***

1.55 A consequential amendment is also made to paragraph 115-215(4)(a) to change the rules for determining when capital gains an individual received via a trust are discount capital gains. Previously, these rules were amended to address circumstances involving affordable housing investment in which a capital gain could not be a discount capital gain for a trust, but in which an individual was intended to be eligible for the CGT discount for affordable housing investments. As a result of the changes discussed above, these circumstances can no longer arise. Given this, the change made to address this situation has been removed. ***[Schedule 1, item 53, paragraph 115-215(4)(a) of the ITAA 1997]***

Amendments to TAA 1953 – fund payments

1.56 Amendments are made to sections 12-405 and 12A-110 in Schedule 1 to the TAA 1953. These amendments ensure that the method statement to determine the amount of a 'fund payment' is adjusted to remove indexation from the cost base in calculating certain capital gains.

1.57 Sections 12-405 and 12A-110 in Schedule 1 of the TAA 1953 set out the meaning of fund payment for MITs and AMITs. A fund payment is broadly the portion of a MIT or AMIT distribution that represents Australian taxable income and gains that is subject to the MIT withholding tax regime for foreign investors.

1.58 The amount of the fund payment is worked out using a method statement set out in sections 12-405 (for MITs) and 12A-110 (for AMITs) in Schedule 1 of the TAA 1953. In relation to capital gains, the trustee must:

- exclude amounts which are capital gains or losses that are not taxable Australian property; and
- in determining the net income of the trust, it must assume that any capital gains from taxable Australian property which have been or would be discounted by the trustee are double the actual amount (this removes any CGT discount).

1.59 Schedule 1 to the Bill includes a new step 2(c) to the method statement for MITs in subsection 12- 405(2). This new step requires trust capital gain from taxable Australian property to be adjusted for the following new special rule relating to indexation:

- the new special rule relating to indexation applies if capital gain of the trust has been worked out using cost base indexation; and
- the special rule adjusts step 2 of the method statement so that trust capital gain is worked out under the method statement in subsection 102-5(1) of the ITAA 1997 assuming the cost base was adjusted to remove the effect of indexation. This special rule has no impact on application of capital losses, previously unapplied net capital losses or quarantined amounts under the ITAA 1997 method statement.

[Schedule 1, items 73 and 74, subsections 12-405(2), (6) and (7) of the TAA 1953]

1.60 The trust calculates the fund payment at the trust level. The reversal of indexation included in capital gains from taxable Australian property is done for the entire amount. It is only fund payments by withholding MITs that are subject to withholding tax.

1.61 Similar amendments are made to section 12A-110 which relates to the fund payment method statement for AMITs. Specifically:

- step 2 of the method statement in section 12A-110(5) is amended to provide that any capital gain of the trust is to be adjusted for the new special rule relating to indexation;
- new subsection 12A-110(11) provides that the new special rule relating to indexation applies to capital gains from taxable Australian property of a trust that has been worked out using cost base indexation; and
- new subsection 12A-110(12) sets out the new special rule that a trust capital gain is worked out under the method statement in subsection 102-5(1) of the ITAA 1997 assuming the cost base was adjusted to

remove the effect of indexation. This special rule has no impact on application of the trust's capital losses, previously unapplied net capital losses or quarantined amounts under the ITAA 1997 method statement.

[Schedule 1, items 75 and 76, subsections 12A-110(5), (11) and (12) of the TAA 1953]

Application of deferred gains to certain CGT events and exemptions

Precluding some CGT events from triggering a taxing point for deferred gains

1.62 Under subsections 112-160(3), 112-170(3) and 112-180(3), a taxpayer with an initial notional gain or loss in relation to the CGT asset will make a deferred gain or loss in the income year in which a realisation event occurs in relation to the CGT asset. Section 977-5 defines a realisation event for a CGT asset as a CGT event other than CGT event E4, E10 or G1.

1.63 The intent is that a deferred gain should only arise when there is a substantive realisation of the CGT asset in which a capital gain based on the value of the asset is taxed. To be relevant, a CGT event must be able to occur after 30 June 2027 to a CGT asset in existence before 1 July 2027. There are some realisation events that do not satisfy these requirements, either because they cannot occur after 1 July 2027 in relation to a CGT asset that was in existence before 1 July 2027 or because they are not a substantive realisation of the CGT asset to which they relate.

1.64 Schedule 1 of the Bill prevents certain CGT events from triggering the liability to pay tax on the deferred gain. This is achieved by including a new definition of 'deferral realisation event' for a CGT asset to be a realisation event for the CGT asset other than the following CGT events:

- events that do not involve a substantive realisation of all or part of an underlying CGT asset:
  - C3 (which occurs for a trustee when an option issued by the trustee ends without being exercised);
  - F3 (which occurs for a lessor, who pays a lessee to vary the terms of a lease);
  - F5 (which occurs when a lessor receives a payment to vary a lease);
  - H2 (which occurs if there is an event relating to a taxpayer's CGT asset that does not have other CGT consequences);

  - K2 (which occurs if a bankrupt pays an amount in relation to a debt that was taken into account working out certain prior year capital losses);
  - K5 (which occurs where an entity related to a taxpayer makes certain kinds of capita losses from collectables);
  - K9 (which occurs when a general partner in certain kinds of venture capital partnership arrangements become entitled to the payment of certain entitlements);
  - K10 (which occurs where a taxpayer makes certain kinds of foreign exchange gains);
  - K11 ((which occurs where a taxpayer makes certain kinds of foreign exchange losses); and
  - K12 (which occurs where a taxpayer that is a foreign hybrid makes certain kinds of capital losses;
- L1 to L8 (which occur in relation to various events connected to tax consolidated groups): are excluded as they fix calculation issues that arise in the context of the consolidation regime, and are similarly not substantive realisations of the underlying CGT asset; and
- events that involve the creation of a new asset so will never be relevant to a deferred gain relating to a pre-existing asset. While these CGT events likely cannot occur in relation to an asset with a deferred gain, they have been excluded for clarity.
  - D1 (which occurs where a taxpayer creates new rights);
  - D2 (which occurs when a taxpayer grants an option);
  - D3 (which occurs when a taxpayer grants a right to certain income from mining);
  - E9 (which occurs when a taxpayer creates a trust over future property);
  - F1 (which occurs where a taxpayer grants a lease);
  - H1 (which occurs when a deposit is forfeited to a taxpayer);
  - K1 (which occurs when a taxpayer receives a new emissions unit); and
  - K6 (which occurs when a taxpayer disposes of a pre-CGT asset).

[Schedule 1, items 12 and 72, subsections 112-152(1) and 995-1(1) of the ITAA 1997]

1.65 The term 'deferral realisation event' is then used in the following provisions in Subdivision 112-E (relates to deemed sale and acquisition on 1 July 2027) to ensure that deferred gains and losses relating to a CGT asset only arise when a later CGT event that is a deferral realisation event happens to the asset:

- subsection 112-155(1);
- subsection 112-165(1);
- paragraph 112-175(1)(b);
- paragraph 112-180(1)(d); and
- paragraph 112-185(1)(a).

[Schedule 1, items 14, 20, 30, 31 and 33, paragraphs 112-155(1)(b), 112-165(1)(b), 112-175(1)(b), 112-180(1)(d) and 112-185(1)(a) of the ITAA 1997]

Example 1.5 Excluded CGT event does not trigger recognition of a deferred gain or loss

Roxi owns an investment unit which she rents out. She acquired the unit on 1 September 2025.

In June 2027 Roxi decides that she wants to move into the unit. The tenants' lease on the unit does not end until 1 October 2027. After negotiating with her tenants, Roxi agrees to pay them $2,000 if they are prepared to end the lease on 31 July 2027. The tenants agree and the lease agreement is varied on 15 July 2027.

CGT event F3 happens on 15 July 2027 when the lease is varied. Roxi will make a $2000 capital loss from CGT event F3 happening.

Roxi does not need to recognise a deferred gain or loss as CGT event F3 is excluded from the definition of 'deferral realisation event' under subsection 112-152(1).

CGT exemptions and deferred gains

1.66 Schedule 1 to the Bill makes amendments to ensure certain exemptions provided under Subdivision 118-A, Subdivision 152-B and Division 855 work correctly for both deferred gains and losses and capital gains and losses made on the realisation event mentioned under Subdivision 112-E. Without such amendments, the exemption might not apply to the deferred gain or loss at the realisation event and the time at which the exemption criteria must be satisfied (at deemed sale or realisation event) may be uncertain.

1.67 A new definition of 'deferral exemption' is included to mean an exemption under any of the following provisions:

- sections 118-10, 118-12, 118-20, 118-24, 118-27, 118-30, 118-35, 118- 60, 118-65, 118-70 or 118-80;

- subdivision 152-B; or
- section 855-10.

[Schedule 1, items 12 and 72, subsections 112-152(2) and 995-1(1) of the ITAA 1997]

1.68 New subsections are included in sections 112-160 and 112-170 (about deferring a gain or loss from the deemed sale and acquisition on 1 July 2027) so that:

- the deemed sale and reacquisition are disregarded when applying the deferral exemption at the time of the realisation event. This means that, in applying a deferral exemption, the deferred gain and gain from the realisation event (or deferred loss and loss from the realisation event) are treated as a single gain or loss made from the realisation event;
- if the deferral exemption does apply after undertaking the process above, then:
  - if the deferral exemption would result in the gain or loss from the realisation event being disregarded, any capital gain or loss made from this deemed CGT event is also disregarded; and
  - if the deferral exemption would reduce the gain or loss by an amount, then if the amount of the reduction exceeds the amount of the gain or loss from the realisation event, then deferred gain or loss is reduced by the balance of the amount of the reduction (if this results in a reduction in a gain being applied to a deferred loss, the deferred loss is increased by that amount, and vice versa); and
- consequential changes are made to other provisions to reflect this change, including guide material.

[Schedule 1, items 19, 27 and 29, subsections 112-160(7), (8), (9) and (10), the note 3 to subsection 112-170(4) and subsections 112-170(7), (8), (9) and (10) of the ITAA 1997]

Example 1.6 Application of deferral exemption to a deferred gain and realisation gain

Banana Co was formed in 2003 and has conducted a banana processing business in North Queensland from that time.

Bonni has at all times been the director and sole shareholder of Banana Co and continues to hold those shares following the commencement of the CGT changes on 1 July 2027.

At that time Bonni will make an initial notional gain on the deemed sale and re-acquisition of her shares in Banana Co, that will be deferred until a later deferral realisation event happens.

On 10 April 2029 Bonni (an Australian resident) signs an agreement with Mango Co to sell her shares in Banana Co, and settlement occurs on 10 June 2029. As the sale of the shares is a deferral realisation event, Bonni will make two capital gains in the 2028-29 income year:

- a deferred gain (equal in amount to the initial notional gain); and
- a capital gain for the realisation event (CGT event A1);

Bonni is aged 56 and is retiring. For working out whether the conditions for the Subdivision 152-B exemption are satisfied, Bonni is treated as having made a single capital gain from the realisation event that happens on the sale of the shares.

The qualifying conditions for the exemption (including those relating to age, retirement, the active asset requirements and the maximum net asset value test) are applied to that CGT event at the time it occurs.

If Bonni satisfies those conditions, then the amount of the deferred gain is disregarded, even though at the time the initial notional gain was made Bonni was aged 54 and would not have met the conditions for the exemption.

1.69 Similar issues arise for roll-overs and similar types of concessions where a gain or loss is disregarded and the cost base of the asset or a replacement asset is modified. These include the relationship breakdown roll-over in Subdivision 126-A and the concession for transfer of the assets of a deceased estate to a beneficiary.

1.70 The intention of the Government is that CGT events for which the gain or loss is disregarded as a result of a roll-over or similar concession will not cause an individual to make a deferred gain or loss.

1.71 However, additional complexities arise for deferred gains and losses in the context of roll-overs and similar concessions, especially where the asset to which the deferred gain relates is transferred to another entity or replaced as a result of the roll-overs. These complexities have meant that the amendments to address this issue are not included in this tranche of legislation. Instead, these amendments are intended to progress in a future tranche of legislation.

CGT minimum tax exemption for testamentary trusts, deceased estates and special disability trusts

1.72 The Government announced in the 2026-27 Budget that it will implement a minimum 30 per cent tax on discretionary trusts. Following consultation, the

Government announced on 18 June 2026 that testamentary trusts will be excluded from this minimum tax on discretionary trusts (subject to integrity requirements for genuine testamentary purposes for discretionary testamentary trusts). Further public consultation on the implementation of the minimum tax on discretionary trusts was undertaken between 8 July 2026 and 31 July 2026.

1.73 Schedule 1 of the Bill makes amendments to the CGT minimum tax provisions to provide comparable exemptions for gains arising in testamentary trusts for beneficiaries of those trusts from the minimum tax on capital gains. Specifically, capital gains realised by a genuine testamentary trust, deceased estate or special disability trust will be exempt from the 30 per cent minimum tax on capital gains.

1.74 A testamentary trust is a trust established under a person's will. It can be used to protect assets of the deceased estate and can continue for many years. It is not a defined term in the income tax law, but paragraph 102AG(2)(a) of the ITAA 1936 identifies trusts that are testamentary trusts for the purposes of providing concessional treatment to trust income that minors receive from a testamentary trust.

1.75 A deceased estate is the property of a person who has died, administered by their legal personal representative. For tax law purposes, deceased estates are treated as a trust, with the legal personal representative as the trustee.

1.76 A special disability trust is a specific kind of trust that meets requirements set out in the *Social Security Act 1991* or the *Veterans Affairs Act 1986* (see subsection 995-1(1)). Broadly, a special disability trust must be established to provide for the accommodation and care needs of a single principal beneficiary with a severe disability and must comply with specific requirements around how is it governed and operated.

1.77 Schedule 1 of the Bill amends subsection 119-5(2) and inserts new provision to provide that the minimum tax capital gain of an individual does not include a gain that the individual makes if the individual makes the gain because they are a beneficiary of a trust that meets specific requirements.
[Schedule 1, items 59 and 61, paragraph 119-5(2)(d) and section 119-20 of the ITAA 1997]

1.78 A gain that arises for an individual as a beneficiary of a testamentary trust will qualify for this exemption if the gain arises in relation to assessable income of the trust that is covered by paragraph 102AG(2)(a) of the ITAA 1997 and is not covered by the integrity rules discussed below.
[Schedule 1, item 61, subsection 119-20(2) of the ITAA 1997]

1.79 Assessable income of a trust will be covered by paragraph 102AG(2)(a) if it ultimately arises from assets of the deceased estate that have been placed in a testamentary trust, including income derived from the profit of those assets. Any gains arising from assets that do not originate with the deceased estate from which the testamentary trust arose does not benefit from the exemption from the minimum tax. This is the result of the integrity rule in subsection

102AG(2AA) of the ITAA 1936, which limits the concessional treatment of the income of a testamentary trust to the income that arises from property that was transferred from the deceased estate and the profits from the investment of that income. This was introduced so that assets unrelated to the deceased estate could not be added to testamentary trusts to take advantage of the prior favourable tax treatment for the income of testamentary trusts. Picking up this rule in the context of the exemption for the minimum tax on capital gains similarly ensures that the benefit of the concession is similarly limited.

1.80 This exemption does not apply to any capital gain arising for a beneficiary of a testamentary trust arising outside the trust, including from the realisation by the beneficiary of assets received from the trust.

1.81 A gain that arises for an individual as a beneficiary of a deceased estate will qualify for this exemption if the gain arises in relation to assessable income of the trust that would be covered by paragraph 102AG(2)(a) of the ITAA 1997 were the deceased estate a testamentary trust that is not covered by the integrity rules discussed below. Similar to testamentary trusts, this limits the exemption to gains arising from the estate of the deceased person, excluding any assets later placed into the estate. Assets arising from the collection of debts or realisation or investment of assets of the deceased person are not assets later placed in the estate; they all ultimately derive from the deceased estate.
[Schedule 1, item 61, subsection 119-20(3) of the ITAA 1997]

1.82 This exemption has limited application. Most capital gains arising in relation to deceased estates are taxed in the hands of the deceased estate, which is not subject to the minimum tax, or disregarded for beneficiaries as a result of Division 128 of the ITAA 1997. However, this exemption ensures that the rare case in which a capital gain may arise for a beneficiary does not result in disadvantage and ensures consistent treatment.

1.83 Similar to the exemption for testamentary trusts, this exemption does not apply to any capital gain arising for a beneficiary of a testamentary trust arising outside the trust, including from the realisation by the beneficiary of assets received from the trust.

1.84 Finally, a gain that arises for an individual as a beneficiary of a special disability trust also qualifies for this exemption. These gains are not subject to the rule that applies to testamentary trusts requiring a link to the estate of a deceased person. Special disability trusts have no necessary link to deceased estates. Further, the rules governing the beneficiaries, governance and operation of those trusts prevent their use in contrived schemes to avoid the minimum tax of capital gains.
[Schedule 1, item 61, subsection 119-20(4) of the ITAA 1997]

1.85 Gains arising in testamentary trusts and deceased estates must satisfy two further integrity rules to qualify for the exemption,

1.86 The first integrity rule denies the benefit of the exemption for a capital gain if the gain arose as the result of a scheme undertaken for the purpose (or for purposes including the purpose) of having this exemption apply to a gain. The purpose does not need to be the sole or dominant purpose of the scheme, but must be more than an incidental purpose. This rule ensures that the exemption is only available to gains legitimately arising in testamentary trusts, excluding gain arising from contrived arrangements. This rule is consistent with existing integrity rules that apply to testamentary trusts in the context of the concessions for the income of minors.
[Schedule 1, item 61, subsections 119-20(5) and (7) of the ITAA 1997]

1.87 The second integrity rule denies the benefit of the exemption for a capital gain if the gain is derived from property that only became part of the property of a deceased estate as the result of a scheme undertaken for the purpose (or for purposes including the purpose) of ensuring that the property would become the property of a deceased estate and benefit from the exemption. The purpose does not need to be the sole or dominant purpose, but must be more than an incidental purpose. Similar to the first rule, this rule ensuring that the exemption from the minimum tax on capital gains for only available to gains arising legitimately arising in testamentary trusts, excluding gains from assets only held in such a trust as a result of contrived arrangements.
[Schedule 1, item 61, subsections 119-20(6) and (7) of the ITAA 1997]

1.88 This rule does not apply merely because activities are undertaken to increase the value of the estate a person leaves to their heirs, as these will not amount to a more than incidental purpose of ensuring the application of the exemption. Instead, the application of this rule is limited to contrived schemes driven by this tax outcome.

1.89 Neither of the integrity rules applies to special disability trusts. The rules governing the beneficiaries, governance and operation of those trusts already address the risk of contrived arrangements.
[Schedule 1, item 61, subsections 119-20(5) and (6) of the ITAA 1997]

CGT outcomes for foreign and temporary resident individuals

1.90 The first tranche of CGT reforms did not extend cost base indexation to foreign and temporary resident individuals. The Explanatory Memorandum for the first tranche noted that future amendments may be considered in relation to how entities that are resident for only part of the period they hold a CGT asset may access indexation.

1.91 Schedule 1 to the Bill ensures that foreign and temporary resident individuals have CGT discount and indexation outcomes that are pro-rated to the number of days that they are Australian residents (and also not temporary residents) during the relevant testing period, in line with the new policy settings for CGT.

1.92 This is achieved by amendments:

- extending the deemed sale and reacquisition provisions to mixed residency cases involving taxable Australian property assets;
- removing residency restrictions which would otherwise exclude foreign residents and temporary residents from accessing indexation; and
- providing an alternative indexation factor formula for mixed residency cases involving direct gains (apportioned indexation factor formula).

1.93 Further consideration is being given to determining appropriate outcomes for taxpayers who change their residency status (mixed residents) and who make capital gains indirectly through a trust.

Cost base indexation for mixed residents

1.94 The amendments remove residency restrictions which would otherwise exclude foreign residents and temporary residents from accessing cost base indexation for CGT events happening on or after 1 July 2027. This involves repealing section 114-25 of the ITAA 1997, which was introduced in the first tranche of CGT reforms. This ensures that subsection 110-36(1A) can apply to foreign or temporary residents, which provides that relevant elements of the cost base of a CGT asset should include indexation for CGT events on or after 1 July 2027 where the requirements of Division 114 are met. This includes foreign or temporary residents that hold new residential dwellings or affordable housing after 1 July 2027, where the chosen treatment is indexation (over the CGT discount).
[Schedule 1, items 6, 8, 35 and 56, section 114-25, note 1 to subsection 115-225(4), notes 1 and 2 and heading of subsection 110-36(1A) of the ITAA 1997]

1.95 The apportioned indexation factor formula apportions the otherwise applicable indexation factor for the period an individual was an Australian resident (but not a temporary resident) during a particular testing period (which is the part of the holding period for an asset that is after 1 July 2027). This formula ensures that cost base indexation is appropriately applied in mixed residency cases.
[Schedule 1, items 69, 68, 69, 70 and 71, subsections 960-275(1D) and (1E), subheadings for subsections 960-275(1), 960-275(1B), 960-275(2) and subsection 960-275(4) of the ITAA 1997]

1.96 The amendments include rules for working out whether an individual was an Australian resident (and not a temporary resident) during the relevant testing period. This includes providing for rules prescribing the effect of the residency status of one individual on a second individual. For example, such rules may apply in situations where there is a CGT roll-over or the death of an individual. The rules are modelled on existing provisions in the taxation laws.

[Schedule 1, items 11 and 34, subsection 112-5(6B) and sections 112-190, 112-195 and 112-200 of the ITAA 1997]

1.97 Where an individual was a foreign or temporary resident during the entire testing period, the apportioned indexation factor formula provides a result of one, and effectively no indexation is available. This is also explained in a legislative note.
[Schedule 1, item 69, note to subsection 960-275(1E) of the ITAA 1997]

1.98 Extending the deemed sale and reacquisition provisions to mixed residency cases involving taxable Australian property assets ensures that for such assets which are acquired before 1 July 2027 and continue to be held on and after 1 July 2027, there is a cost base on 1 July 2027, which is to be indexed, in calculating the post-1 July 2027 portion of any capital gain. The rules prescribing the effect of the residency status of one individual on a second individual described above, also apply for the deemed sale and reacquisition provisions.
[Schedule 1, items 13, 14, 15, 17, 20, 34 and 72, paragraphs 112-155(1)(c) and (d), 112-165(1)(c) to (e), subsection 995-1(1) (definition of membership testing period), sections 112-190, 112-195 and 112-200, notes to subsection 112-155(1) and headings for sections 112-155 and 112-160 of the ITAA 1997]

CGT discount for mixed residents

1.99 As a result of the amendments explained above, amendments made in the first tranche of CGT reforms and the existing law, foreign residents and temporary residents who would have had access to the pro-rata CGT discount prior to the reforms, will continue to have CGT discount outcomes that are pro-rated to the number of days that they are Australian residents (and also not temporary residents) during the relevant testing period, in line with the new policy settings for CGT.

1.100 Extending the deemed sale and reacquisition provisions to mixed residency cases involving taxable Australian property assets (other than new residential property and affordable housing) ensures that for such assets which are acquired before 1 July 2027 and continue to be held on and after 1 July 2027, there is a CGT event on 30 June 2027. This will result in any deferred notional capital gains that are discount capital gains (i.e. pre-1 July 2027 discount capital gains) having a discount testing period that ends on 30 June 2027. The discount testing period is mainly relevant for the application of sections 115-105, 115-110 and 115-115 of the ITAA 1997 (the key provisions providing a pro-rata CGT discount to mixed residents) and generally determines the period within which residency status is tested.
[Schedule 1, items 13, 14, 15, 17, 20, 34 and 72, paragraphs 112-155(1)(c) and (d), 112-165(1)(c) to (e), subsection 995-1(1) (definition of membership testing period), sections 112-190, 112-195 and 112-200, notes to subsection

112-155(1) and headings for sections 112-155 and 112-160 of the ITAA 1997]

1.101 The outcomes achieved by this are:

- Individuals that cease being an Australian resident (but not a temporary resident) and become a foreign or temporary resident before 1 July 2027 who would have had access to the pro-rata CGT discount prior to the reforms will be able to access the CGT discount for any deferred notional capital gains that are discount capital gains (i.e. pre-1 July 2027 discount capital gains), pro-rated to the number of days that they are Australian residents (and also not temporary residents) during the discount testing period.
- Individuals that cease being an Australian resident (but not a temporary resident) and become a foreign or temporary resident after 1 July 2027 who would have had access to the pro-rata CGT discount prior to the reforms will be able to access the full 50 per cent CGT discount for any deferred notional capital gains that are discount capital gains (i.e. pre-1 July 2027 discount capital gains).

1.102 Generally, there is no CGT discount for the post-1 July 2027 part of any capital gains, as a discount capital gain must not have an indexed cost base (refer section 115-20 of the ITAA 1997) and these amendments extend cost base indexation to foreign residents and temporary residents with a period of Australian residency for CGT events happening on or after 1 July 2027.

1.103 However, consistent with the CGT outcomes for Australian residents under these reforms, the CGT discount continues to be available for capital gains involving new residential or affordable housing, including those post-1 July 2027, where the discount is the chosen treatment. For mixed residents with capital gains relating to new residential or affordable housing, the CGT discount is pro-rated for period of Australian residency during the discount testing period.

Consequential amendments

1.104 Schedule 1 to the Bill makes a range of consequential amendments to the ITAA 1997 to address the consequences of the primary amendments, including adding definitions to the Dictionary and updating notes. Various consequential amendments are discussed in the relevant sections above.

1.105 The following amendments have also been made to ensure the first tranche of CGT reforms works as intended:

- Amendments to the formula in the affordable housing provision to adjust the terms used in the formula to remove reference to ‘the discount percentage that would apply to the discount capital gain apart

from this section' and instead directly reference the 50 per cent discount percentage and the 50 per cent discount percentage (apportioned for period of Australian residency for mixed residents). This ensures that the aspects of the formula providing up to an additional 10 per cent (apportioned for period of Australian residency for mixed residents) for investors in affordable housing operates as intended in situations where paragraph 115-100(e) of the ITAA 1997 is the only paragraph providing a discount percentage above 0 for the gain. Paragraph 115-100(e) provides a percentage if section 115-125 (affordable housing provision) applies to the gain. Where none of the paragraphs in section 115-100 apply, the first tranche of CGT amendments set a default discount percentage of 0 per cent. If the formula were to continue to reference the discount percentage that would apply to the discount capital gain apart from section 115-125, contrary to the intent of the provisions, in such cases, the additional (up to) 10 percentage points lift in the discount percentage would not be available (as the formula provides a nil result).
[Schedule 1, item 50, formula in subsection 115-125(5) of the ITAA 1997]

- In subsection 115-125(6), the reference to 60 per cent is replaced with 'more than 0 per cent'. This is because the affordable housing provisions provide a discount percentage of up to 60 per cent and therefore some taxpayers may not be entitled to the full 60 per cent discount percentage. The amendment ensures that investors in affordable housing do not have to have the full 60 per cent CGT discount to be able to choose to apply cost-base indexation and be subject to the minimum 30 per cent tax instead of the CGT discount.
[Schedule 1, item 51, subsection 115-125(6) of the ITAA 1997]
- Subsections 115-45(4) and (5) requires identification of CGT assets that were acquired less than 12 months before the CGT event (the CGT event happening to the share in the company or the interest in the trust). A new subsection is included to provide that the deemed sale just before 1 July 2027 (in subsections 112-155(2), 112-165(2) and 112-175(2)) is disregarded for the purposes of applying the 12 month rule in subsection 115-45(4) and paragraph 115- 45(6)(a).
[Schedule 1, item 38, subsection 115-45(8) of the ITAA 1997]
- Various changes have also been made to update referencing and otherwise ensure the legislation operates as intended given the changes made by Schedule 1 to the Bill.

[Schedule 1, items 16, 18, 23, and 25, subsections 112-155(4), 112-160(3), 112-165(4) and 112-170(3) of the ITAA 1997]

Commencement, application, and transitional provisions

1.106 Schedule 1 to the Bill commences on the first 1 January, 1 April, 1 July or 1 April to occur after the day the Bill receives Royal Assent.
[Item 2 of the commencement table in clause 2 of the Bill]

1.107 The amendments made by Schedule 1 apply in relation to assessments for the income year that includes 1 July 2027 and later income years.
[Schedule 1, subitem 77(1) of the Bill]

1.108 An application provision is included for subsection 276-345(6) (relates to AMIT unders and overs with discount capital gain) to confirm that the subsection can apply in relation to an assessment for a discovery year that is the income year that includes 1 July 2027 or a later income year even if the base year ends before 1 July 2027.
[Schedule 1, subitem 77(2) of the Bill]

Future amendments

1.109 These amendments are the second tranche of changes to establish the new CGT regime. Matters that are intended to be addressed in further tranches of amendments include:

- the CGT treatment of rollovers and similar concessions (including the concession for beneficiaries receiving assets from deceased estates);
- remaining aspects of the application of the CGT reforms to foreign, mixed and temporary residents;
- interaction issues between the CGT reforms and the value shifting rules in Part 3-95 of the ITAA 1997;
- amendments to ensure that the rules apply appropriately for:
  - consolidated groups;
  - listed investment companies;
  - employee share schemes;
  - demergers; and
  - options, and

- interactions between the deemed sale and reacquisition of CGT assets held before 1 July 2027 and rules requiring the determination of cost base at a point before an asset is realised.