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Australian Government
Australian Taxation Office

Guide to capital gains tax 2005

To help you complete your tax return for 1 July 2004–30 June 2005

Covers:
- how to work out whether you are subject to capital gains tax
- how to calculate your capital gain or capital loss.

If you are a resident personal investor with a capital gain or capital loss only from shares, units or a managed fund, you can use the shorter *Personal investors guide to capital gains tax 2005* instead of this guide

For CGT tools and calculators, including for demergers, visit **www.ato.gov.au**

OUR COMMITMENT TO YOU

The information in this publication is current at May 2005.

In the taxpayers' charter we commit to giving you information and advice you can rely on.

If you try to follow the information contained in our written general advice and publications, and in doing so you make an honest mistake, you won't be subject to a penalty. However, as well as the underpaid tax, we may ask you to pay an interest charge.

We make every effort to ensure that this information and advice is accurate. If you follow our advice, which subsequently turns out to be incorrect, or our advice is misleading and you make a mistake as a result, you won't be subject to a penalty or an interest charge although you'll be required to pay any underpaid tax.

If you feel this publication does not fully cover your circumstances, please seek help from the Tax Office or a recognised tax adviser. Since we regularly revise our publications to take account of any changes to the law, you should make sure this edition is the latest. The easiest way to do this is by checking for a more recent version on our website at **www.ato.gov.au**

YOUR RIGHTS

It is important that you are aware of your rights and obligations when dealing with the Tax Office.

When we make a decision about your tax affairs, we will tell you about your rights and obligations in relation to that decision. We will also give you contact details in case you have any queries or need more information.

There is information under 'Your rights' on the Tax Office website at **www.ato.gov.au** To get a printed copy of the *Taxpayers' charter – what you need to know* (NAT 2548), phone our distribution service on **1300 720 092**.

HOW SELF-ASSESSMENT AFFECTS YOU

Self-assessment means the Tax Office uses the information you give on your tax return to work out your refund or tax debt. You are required by law to make sure you have shown all your assessable income and claimed only the deductions and tax offsets to which you are entitled. The Tax Office does not take any responsibility for checking the accuracy of the details you provide in your tax return. However, at a later date the Tax Office may examine the details contained in your tax return more thoroughly by reviewing specific parts, or by conducting an audit on your tax affairs.

What are your responsibilities?

It is your responsibility to lodge a tax return that is signed, complete and correct. Even if someone else – including a tax agent – helps you to prepare your tax return, you are still legally responsible for the accuracy of your information.

What if you lodge an incorrect tax return?

Our audit programs are designed to continually check for missing, inaccurate or incomplete information. If you become aware that your tax return is incorrect, you must contact us straight away.

Initiatives to complement self-assessment

There are a number of initiatives administered by the Tax Office which complement self-assessment. Examples include:

- if you take reasonable care with your tax affairs, you will not receive a penalty for honest mistakes – but please note that an interest charge on omitted income or over-claimed deductions and tax offsets could still be payable
- the process for applying for private rulings
- your entitlement to interest on early payment or over-payment of a tax debt
- the process for applying for an amendment if you find you have left something out of your tax return.

Do you need to ask for a private ruling?

If you are concerned about the way a tax law applies to your personal tax affairs, you can ask for a private ruling by completing an *Application for a private ruling for individuals* (NAT 4106–3.2001). You should lodge your tax return by the due date, even if you are waiting for the reply to your application. You may need to request an amendment to your tax return once you have received the private ruling.

We publish all private rulings on our website. What we publish will not contain anything that could identify you. For more information on private rulings, including application forms, visit the Tax Office website at **www.ato.gov.au**

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Guide to capital gains tax 2005

CONTENTS

ABOUT THIS GUIDE

The *Guide to capital gains tax 2005* explains how **capital gains tax** works and will help you calculate your **net capital gain** or **net capital loss** for 2004–05 so you can meet your capital gains tax obligations. There are worksheets at the back of the guide to help you do this.

WHO SHOULD USE THIS GUIDE?

An individual, company, trust or superannuation fund can use this guide to work out their capital gains tax.

A company, trust or superannuation fund that is required to complete and lodge a *Capital gains tax (CGT) schedule 2005* should use the schedule included at the back of this guide. Part C explains when a schedule must be lodged.

If you have a small business, you should get the publication *Guide to capital gains tax concessions for small business* (NAT 8384).

> Individuals may prefer to use the shorter, simpler *Personal investors guide to capital gains tax 2005* (NAT 4152–6.2005) if, during 2004–05, they only:
> - sold some shares
> - sold some units in a managed fund, and/or
> - received a distribution of a capital gain from a managed fund.

This guide does not deal fully with the capital gains tax position of:
- a company that is the head company of a consolidated group – the rules that apply to members of a consolidated group modify the application of the capital gains tax rules. For more information about the consolidation rules, or if you have technical tax enquiries, visit our website or phone the Tax Reform Infoline on **13 24 78**
- an individual or entity whose gains or losses are included as part of its income under other provisions of the tax law – for example, from carrying on a business of share trading (see the fact sheet *Carrying on a business of share trading*, available on our website)
- an individual or entity that is a non-resident of Australia.

PUBLICATIONS AND SERVICES

To find out how to get a publication referred to in this guide and for information about our other services, see the inside back cover.

UNFAMILIAR TERMS

Some of the terms used in this guide may be new to you. Specific terms are shown in **red** when first used and are explained in **Definitions** on page 123.

INTRODUCTION

This guide will help you work out whether any of the assets you own (or may own in the future), and any events that happen to you are subject to capital gains tax (CGT). Where they are, it tells you how to work out your capital gain or capital loss. It also covers what records you need to keep.

> **NEW TERMS**
>
> We may use some terms that are new to you. These words are printed in **red** the first time they are used and explained in **Definitions** on page 123. Generally they are also explained in more detail in the section where they first appear.
>
> While we have sometimes used the word 'bought' rather than 'acquired', you may have acquired an asset subject to capital gains tax (a **CGT asset**) without paying for it (for example, as a gift or through an inheritance). Similarly, we refer to 'selling' such an asset when you may have disposed of it in some other way (for example, by giving it away or transferring it to someone else). Whether by sale or by any other means, all of these disposals are **CGT events**.

YOUR TAX RETURN

Whether you are an individual or an entity (company, trust or fund), if you have a capital gain or capital loss for 2004–05, this guide will help you to complete the capital gains item on your tax return.

WORKSHEETS

You may wish to use the two CGT worksheets provided at the back of this guide to help you keep track of your records and make sure you pay no more CGT than necessary.

There is:

- a **Capital gain or capital loss worksheet** for working out your capital gain or capital loss for each CGT 'event', and
- a **CGT summary worksheet** to help you summarise your capital gains and capital losses and produce the final net amount you need to include on your tax return.

You can tear out these forms and complete them as you work through the guide.

CAPITAL GAINS TAX SCHEDULE

If you are a company, trust or fund with total capital gains or capital losses of more than $10,000 this **income year**, you must complete a *Capital gains tax (CGT) schedule 2005 (CGT schedule)*. Partnerships and individual paper tax preparers are not required to lodge a schedule.

The CGT schedule is explained in detail in **part C** and is provided at the back of this guide.

WHAT'S NEW

The Tax Office is providing new, easy-to-use online tools to take some of the complexity out of capital gains tax.

The *Capital gains tax checklist* gives you an easy way to determine possible CGT consequences now and in the future.

Use the checklist's question and answer format to determine:

- whether you are likely to have a capital gain or capital loss in the current income year
- whether you are likely to have a CGT event in the future, and
- what sort of records you need to keep.

To get the checklist, visit our website and select 'For Tax Professionals', then click on 'Tax Professionals homepage'. From the menu on the left, under 'Tax topics explained', select 'Capital gains tax', select 'CGT for tax professionals' and click on 'Capital gains tax checklist'.

Capital gains tax updates, available through the above link, give you information on the latest CGT developments including:

- changes and proposed changes to the law
- new Tax Office rulings and determinations
- new ATO interpretative decisions (ATO IDs), and
- new online CGT resources.

The *Basic capital gains tax issues for legal professionals* guide provides detailed information on the CGT consequences of some common legal transactions. Topics covered include conveyancing, wills and the administration of deceased estates, family law, litigation and compensation issues and record keeping.

To get the *Basic capital gains tax issues for legal professionals* guide, visit our website and select 'For Tax Professionals', then click on 'Tax Professionals homepage'. From the menu on the left, under 'Your tax practice', select 'Industries and business types', then select 'Industries L–Z' and click on 'Legal practitioner's essentials'. From this page, click on 'Capital gains tax information'.

Changes and proposed changes to the law

There are a number of recent and proposed CGT changes to bear in mind when calculating your capital gain or capital loss.

Foreign exchange gains and losses

Recent legislation dealing with foreign exchange (forex) gains and losses generally applies from 1 July 2003. The legislation introduces CGT events K10 and K11. These CGT events mean that short-term forex gains or losses arising under a transaction for the acquisition or disposal of certain capital assets are integrated into the tax treatment of the capital asset or are matched to the character of the gain or loss that would arise from the disposal of the asset. For the rules to apply, the due date for payment must be within 12 months of acquiring the asset or disposing of it. Taxpayers could choose, generally by 16 January 2004, not to have this rule apply so forex gains and losses were instead assessable or deductible.

For more information, see *Forex – the 12 month rule* on our website.

Shares in foreign companies

Legislation has been passed to reduce capital gains and capital losses made on certain disposals by Australian companies of their shares in foreign companies to the extent that there is an underlying active business. The legislation may also reduce attributable income arising from certain CGT events happening to shares owned by a controlled foreign company (CFC) in a foreign company.

The changes only apply if:

- the company held a direct voting percentage in the foreign company of at least 10%, and
- the shares were held by the company for a continuous period of at least 12 months in the two years before the CGT event.

The changes apply to CGT events happening on or after 1 April 2004. For more information, phone the Business Infoline on **13 28 66**.

Foreign residents investing in Australian fixed trusts

Changes have been made to the tax treatment of foreign residents making capital gains and capital losses in respect of interests owned in certain Australian trusts. In brief, the changes mean:

- capital gains and capital losses made on or after 21 March 2005 by a foreign resident from a CGT event happening to an interest in a fixed trust are disregarded if at least 90% of the underlying assets of the trust do not have the necessary connection with Australia
- capital gains made by a foreign resident on or after 21 March 2005 in respect of their interests in a fixed trust are disregarded if the gains relate to a trust asset without the necessary connection with Australia
- distributions of foreign source capital gains from the trustee of a trust (other than a corporate unit or public trading trust) on or after 21 March 2005 to a beneficiary that is a foreign resident are disregarded for the purposes of CGT event E4.

For more information, phone the Business Infoline on **13 28 66**.

Worthless shares

The law has been changed to allow shareholders to choose to make a capital loss where either a liquidator or an administrator declares in writing that shares are worthless. Previously, the law only allowed shareholders to make such a choice if a liquidator made the declaration. The new law also applies to other financial instruments relating to companies. The change applies to declarations made after 21 March 2005. For more information, see chapter 5.

Testamentary gifts

On 11 May 2004, as part of the 2004 Budget, the Government announced that it proposes to remove the condition that a testamentary gift of property to a deductible gift recipient must be independently valued at greater than $5,000 before a CGT exemption can apply to the gift. The Government's intention is that the change will apply to gifts made after the date the amending law receives Royal Assent.

Rollover for transition to superannuation safety arrangements

The Government has introduced legislation into Parliament to allow CGT **rollover** for certain mergers of superannuation entities. The rollover will apply to mergers caused by trustees not satisfying the licensing requirements under the new superannuation safety arrangements. The Government's intention is that the change will commence on 1 July 2004 and operate for a two-year period.

CGT implications for employee shares and rights under a corporate restructure

The law has been changed so that if employee shares or rights are exchanged for replacement shares or rights in a new company under a corporate restructure that happens on or after 1 July 2004, automatic rollover relief may be available so that there is no taxing point under the **employee share scheme** income tax rules. Corporate restructures affected include mergers, **demergers** and 100% takeovers. The CGT provisions have been amended to ensure that no unintended capital gain or capital loss arises where this rollover relief applies .

For more information about this, see our fact sheet *Employee share schemes – rollover relief on a corporate restructure*, available on our website.

Non-resident individuals with shares in listed investment companies

The Government has introduced legislation into Parliament that will give non-resident individuals access to the concession for shareholders in listed investment companies. The concession is proposed to apply to dividends distributed on or after the date of Royal Assent.

For more information, phone the Business Infoline on **13 28 66**.

Individuals with employee shares or rights who cease to be residents

The Government has introduced legislation into Parliament to ensure that a person who ceases to be a resident will not be taxed on the same gain under both the employee share provisions and the CGT provisions. The legislation is expected to apply to persons who cease to be residents on or after the date of Royal Assent.

Individuals with employee shares or rights who become residents

The Government has introduced legislation into Parliament to clarify the CGT rules applying to individuals with employee shares or rights who become residents. The legislation is expected to apply to CGT events that happen on or after the date of Royal Assent.

For more information, phone the Business Infoline on **13 28 66**.

Capital gains tax treatment of options

On 27 May 2005, the Government announced proposed changes to the CGT legislation on options. The new law will ensure that the provisions concerning options and capital proceeds will now apply to options for the creating, granting or issuing of assets, and their renewal or extension, in the same way as they apply to options for the disposal of assets or the issuing of shares. The amount paid for such an option plus any amount paid to exercise it will now be included in the CGT cost base of the newly acquired asset.

The Government intends the changes to apply to options exercised on or after 27 May 2005. Transitional amendments will ensure a similar treatment for pre-CGT options except where such options were last renewed or extended on or after 20 September 1985.

BUDGET ANNOUNCEMENTS

Blackhole expenditure

On 10 May 2005, as part of the Budget, the Government announced proposed changes that will allow a deduction over five years for certain capital expenditure, known as 'blackhole' expenditure, incurred by businesses carried on for a taxable purpose. The new provisions will apply as a last resort if the expenditure does not have tax treatment or is denied a deduction. Blackhole expenditure will also be recognised by increasing the range of expenditure that forms the **cost base** of an asset for CGT purposes. The Government's intention is that the changes will apply to certain blackhole expenditure incurred on or after 1 July 2005.

Marriage breakdown rollover

On 10 May 2005, as part of the Budget, the Government announced proposed changes that will extend the scope of the marriage breakdown CGT rollover. The rollover will also apply to:

- assets transferred to a spouse or former spouse under a binding financial agreement or arbitral award under the Family Law Act 1975 or a similar agreement or award under a corresponding foreign law
- assets transferred under a written agreement under a state, territory or foreign law relating to de facto marriage breakdowns where the agreement is similar to a binding financial agreement.

Amendments will also be made to ensure that the **main residence exemption** interacts more appropriately with the marriage breakdown rollover relief and ensure that marriage breakdown cash settlements do not give rise to CGT liabilities.

The Government's intention is that the changes will apply to CGT events that happen after the date of Royal Assent of the amending legislation.

International tax reform

On 10 May 2005, as part of the Budget, the Government announced that it proposes to provide further reforms to Australia's international tax arrangements. These include:

- a reintroduction of the foreign income exemption for temporary residents. This will ensure no capital gain or capital loss arises on the disposal of foreign assets by a person who is a resident for four years or less. The Government's intention is for the change to generally have effect for the first income year after the date of Royal Assent of the amending legislation
- amending the CGT rules as they apply to non-residents by narrowing the range of assets on which a non-resident is subject to Australian CGT to real property and the business assets of Australian branches of a non-resident. Also the integrity of the measure will be protected by applying CGT to non-portfolio interests in interposed entities, where the value of such an interest is wholly or principally attributable to Australian real property. The Government's intention is to introduce this legislation before the end of the 2005–06 income year and for the changes to apply to CGT events happening after the date of Royal Assent of the amending legislation.