# Capital Gains Tax Indexation and Asymmetric Real Loss Recognition

Presentation to the Melbourne Economic Forum, 27 August 2026

**James Giesecke**
Professor, Centre of Policy Studies
James.Giesecke@vu.edu.au

**Jason Nassios**
Assoc Prof, Centre of Policy Studies
Jason.Nassios@vu.edu.au

**Centre of Policy Studies**
**Victoria University**
Level 1, 300 Queen St
Melbourne Victoria 3000
vu.edu.au/cops

***Presentation based on:***

*Giesecke, J. A. and J. Nassios (2026), "Effective Capital Gains Tax Burdens Under Asymmetric Recognition of Real Losses", Centre of Policy Studies Working Paper No. G-373, Victoria University, August 2026.*

VICTORIA UNIVERSITY
MELBOURNE AUSTRALIA

CoPS
SINCE 1975

# 1. The stated policy objective

**BUDGET PAPER NO. 1**

> "This returns the CGT regime to its original intent of taxing real capital gains, appropriately compensating taxpayers for inflation."

Australian Government, Budget Paper No. 1, Statement 4, p. 155.

**BUDGET TAX REFORM WEBPAGE**

> "This reform means that investors will only pay tax on their real capital gain, restoring the original intent of the CGT arrangements."

Australian Government, Budget 2026–27, Tax reform webpage.

**TREASURER'S BUDGET-NIGHT STATEMENT**

> "Returning to indexation will mean in future, only real capital gains are subject to tax…"

The Hon Jim Chalmers MP, media release, 12 May 2026.

**BUDGET TAX EXPLAINER**

> "Returning to indexation based on the CPI aligns with the original intent of the CGT regime…Applying these changes broadly across assets ensures the CGT settings are broadly asset neutral…"

Australian Government, Negative Gearing and Capital Gains Tax Reform, p. 2.

**LATER RESTATED IN TRANCHE 2**

**"…cost base indexation to ensure only real gains are subject to taxation."**

Exposure Draft Explanatory Memorandum, CGT adjustments (tranche 2), paragraph 1.4.

# 2. Reform: one distortion removed, another created

## Current system

- Tax **nominal gains** after netting nominal losses.
- Apply the **50% CGT discount** to eligible gains.
- Inflationary gains remain partly taxable.

## New system

- From 1 July 2027, index the cost base for inflation.
- Tax gains above the **indexed** cost base.
- Recognise losses only below the **original nominal** cost base.

## Symmetric system

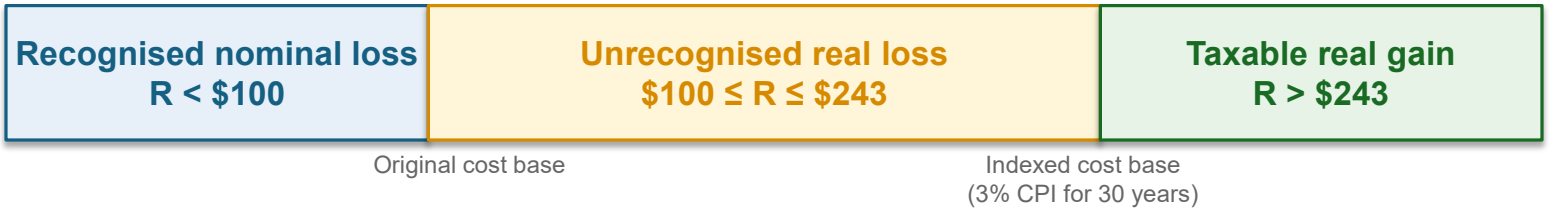
- Tax the portfolio's **net real gain**.
- Recognise real gains and real losses **symmetrically**.
- No tax where purchasing power is unchanged.

**Policy question: does indexation, when asymmetrically implemented, necessarily reduce the CGT burden on a diversified portfolio?**

Answer: No. Asset-by-asset indexation, with nominal loss recognition, can create a larger expected burden than the current system.

# 3. Why the loss-recognition asymmetry matters

**Tax treatment of a single asset, purchased for $100: The asset's value (R) after 30 years, with 3% annual inflation, must fall in one of three CGT zones:**




**<u>Example:</u> A two-asset portfolio can have no overall real gain, and yet still generate a positive (realisation-contingent) tax liability:**

**Asset A** $100 → $300 — **Real gain: +$57**
**Recognised tax base: +$57**

**Asset B** $100 → $186 — **Real loss: −$57**
**Recognised tax base: $0**

**Portfolio**

Terminal value: $486
CPI-adjusted cost: $486

Net real gain: $0
New-system tax base: +$57

**The asymmetry in loss recognition turns cross-sectional dispersion into a tax base variable.**

# 4. Who faces the new loss-recognition wedge?

| Holding structure | Current CGT regime | New CGT regime (from 1 July 2027) |
|---|---|---|
| **Resident individual (direct holdings)** | Nominal gains/losses netted; 50% discount for eligible nominal gains. | **DIRECT:** Indexed gains; losses still nominal. This is the case modelled in the paper. Real losses that are not also nominal losses are unrecognized. |
| **Individual partner (partnership assets)** | Nominal gain/loss attributed to each partner. Each partner applies CGT rules applicable to them. | **DIRECT:** Each individual partner applies the new rules to their share of partnership assets. Real-but-not-nominal losses are unrecognised. |
| **Ordinary trust (fixed/unit/discretionary)** | Trust calculates and nets gains/losses. Gains attributed to beneficiaries. | **FLOW-THROUGH:** Trust first recognises asset gains/losses. Real-but-not-nominal losses are unrecognised Omitted real losses are gone, before flow through. |
| **Managed fund / ETF (trust, AMIT, CCIV)** | Fund nets recognised gains and losses. Resulting capital gain components are passed through to investors. | **FLOW-THROUGH:** Trust first recognises asset gains/losses. Real-but-not-nominal losses are unrecognised Omitted real losses are gone, before flow through. |
| **Company** | Nominal gains/losses at company level; no 50% discount. | **NOT AT ENTITY LEVEL:** No new indexation regime for companies. **INDIRECT HOLDINGS**: potential vehicle-level exposure through trusts, AMITs and other attribution vehicles. |
| **Complying super fund (including SMSF)** | Fund-level nominal netting. One-third discount on eligible gains. | **NOT AT ENTITY LEVEL:** Super retains existing framework. Direct holdings, not exposed**. INDIRECT HOLDINGS**: potential vehicle-level exposure through trusts, AMITs and other attribution vehicles. |

**Key points:** Asset-level recognition occurs before pooling. Omitted real losses cannot be restored later.

# 5. Central experiment and calibration

## Portfolio experiment

- Large equal-weight portfolio of personally held CGT assets.
- Expected capital-price path is centred on CPI: **g = 0**.
- Tax is calculated **asset by asset** and aggregated across the portfolio.
- Burden is reported as a share of terminal portfolio value.

## Central calibration

| | |
|---|---|
| Inflation | **π = 3% p.a.** |
| Individual asset log return volatility | **σ = 30% p.a.** |
| Marginal tax rate | **t = 47%** |
| Holding period | **T = 5–100 years** |

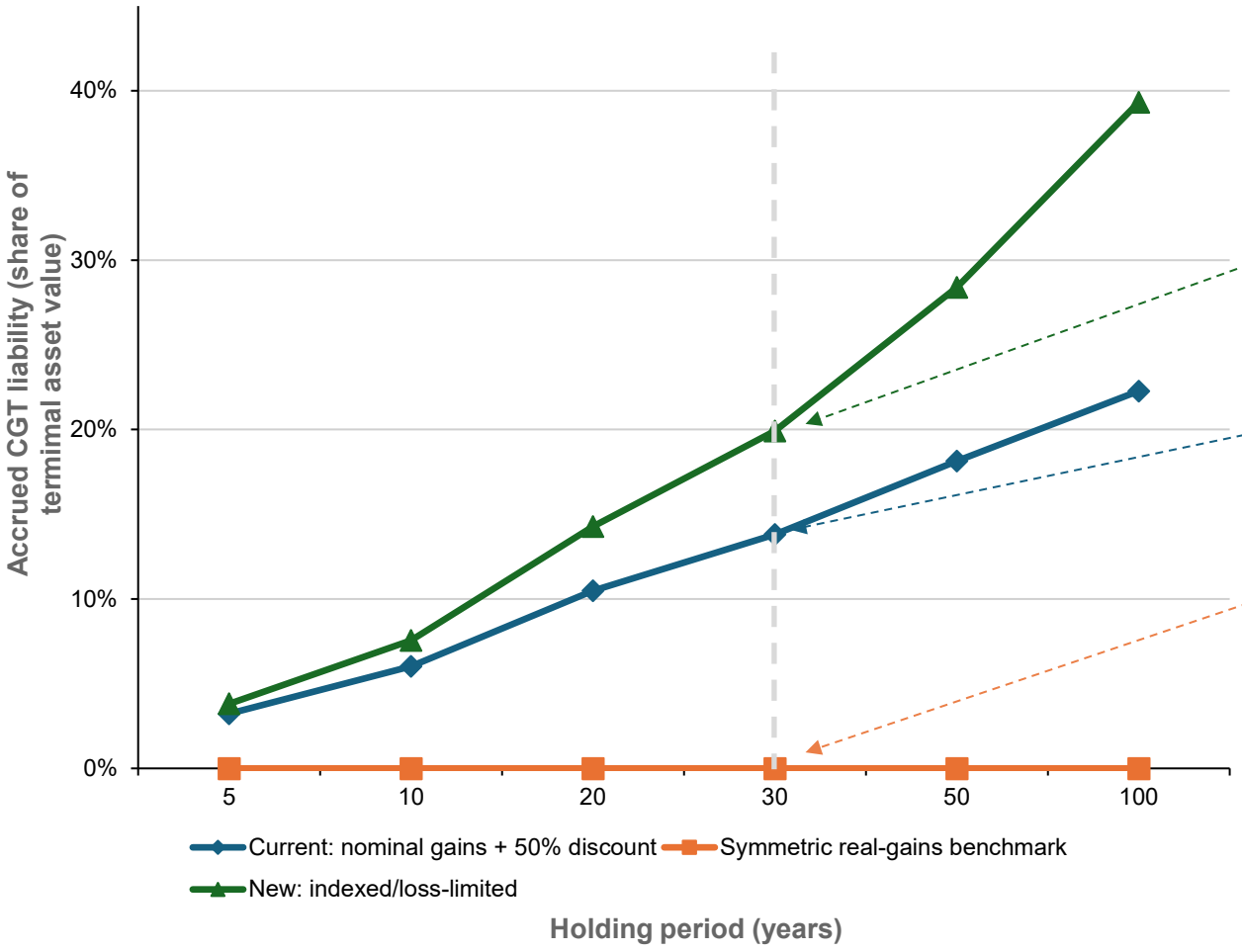
**Purpose**

Hold the expected real capital-price gain at zero, then ask how each tax design treats inflation and the dispersion of individual asset returns.

**Scope**

We are implementing a tax design experiment. Dividends, retained profits, and the 30% minimum CGT tax floor are outside the model.

# 6. Central result: new system has highest burden




**At 30 years:**

**19.9%**
new system

**13.8%**
current system

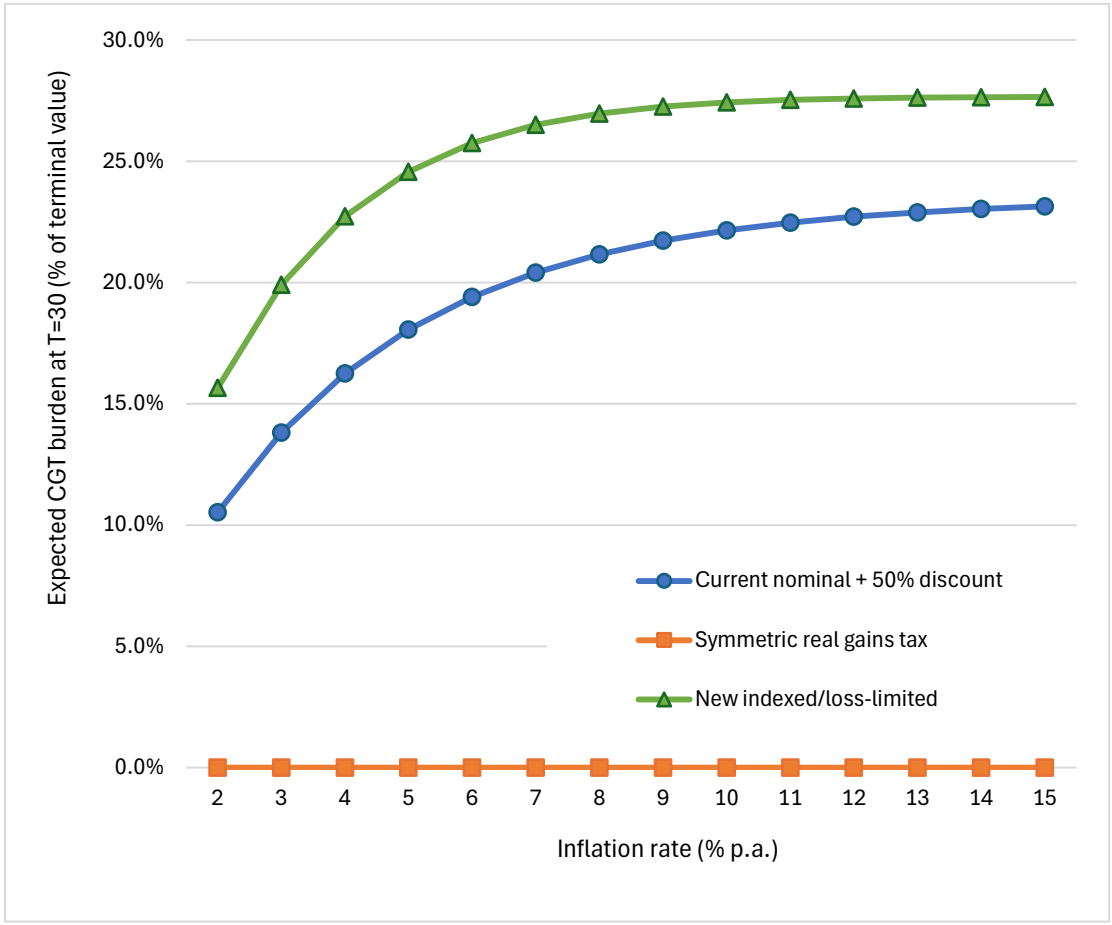
**0%**
symmetric benchmark

**New minus current:**

**+6.1 percentage points of terminal value**

*Source: Giesecke and Nassios (2026).*

# 7. Inflation sensitivity: new system remains above current system




*T = 30, g = 0, t = 47%, σ = 30%.*

## Interpretation

- **Current system:** higher inflation creates larger taxable nominal gains.
- **New system:** higher inflation widens the band of unrecognised real losses.
- **Across 2–15% inflation,** the new system remains above the current system.

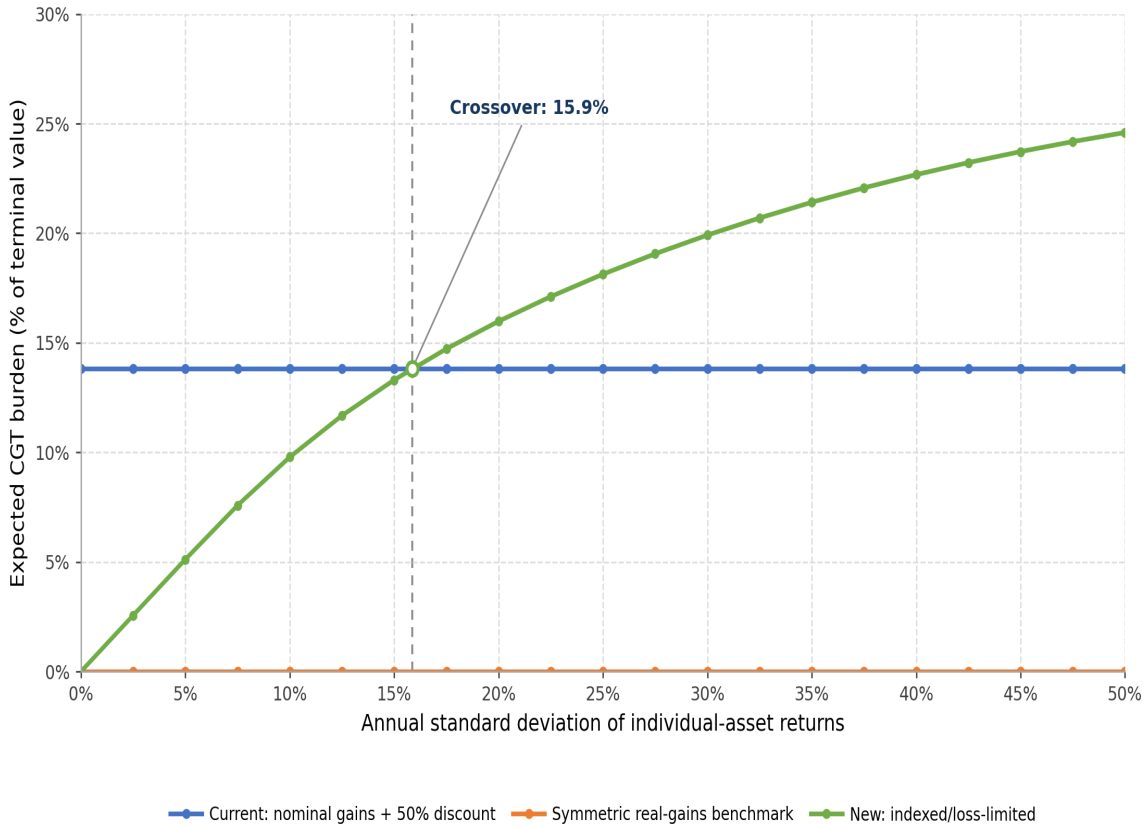
**Indexation does not make the new system inflation-neutral for a dispersed portfolio.**

Source: Giesecke and Nassios (2026).

# 8. Volatility sensitivity: ranking reverses at σ ≈ 15.9%

## 30-year burden as individual-asset return dispersion varies

*Central calibration: π = 3%, g = 0, t = 47%, T = 30*




**Crossover**

**15.9%**

new = current

**Illustrative σ = 10%**

**9.8%**

new system
(13.8% current)

**Central σ = 30%**

**19.9%**

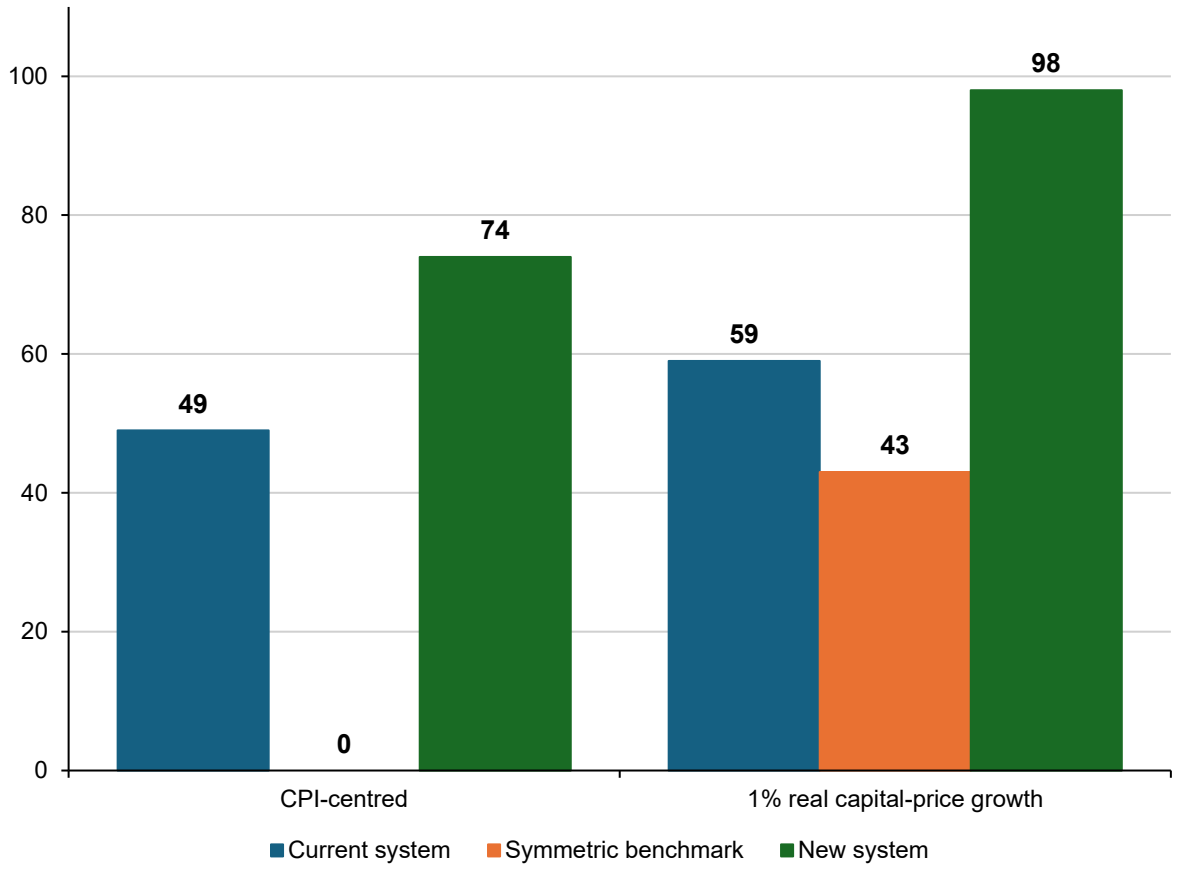
new system
(13.8% current)

**Asset-level dispersion becomes a tax parameter.**

*Source: Giesecke and Nassios (2026).*

# 9. Translating terminal burdens into annual tax drag

Equivalent annual CGT wedge (basis points per year) (central case)




## Reform effect

**+24 bp/yr**

CPI-centred case

**+39 bp/yr**

1% real-growth case

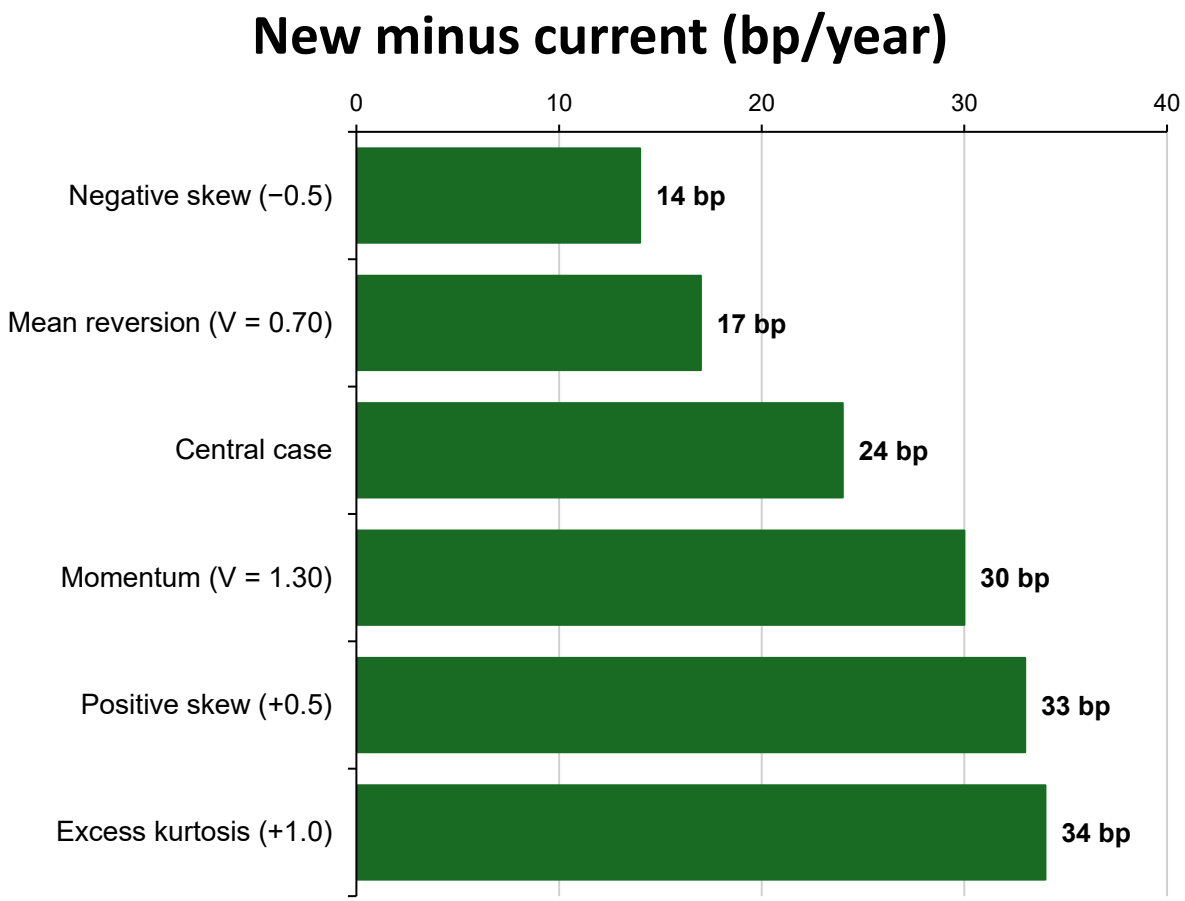
## Interpretation

The deferred terminal liability is equivalent to a persistent reduction in the investor's annual after-tax return.

*Source: Giesecke and Nassios (2026)*

# 10. At the central calibration, the ranking is robust to alternative return processes

Change in annual wedge relative to current system




**Across the reported tests**

**64 - 84**

new-system wedge (bp/year)

**49**

current-system wedge (bp/year)

*Source: Giesecke and Nassios (2026).*

# 11. Policy implications

## Inflation neutrality

- **Current system:** inflation directly creates taxable nominal gains.
- **New system:** inflation widens the band of unrecognised real losses.
- Only the symmetric real gains tax is inflation neutral.

## Capital allocation

- Higher within-sector return dispersion raises the effective CGT wedge.
- Riskier sectors may require higher pre-tax returns.
- The reform can therefore affect investment and its sectoral allocation.

## Reform design

- Indexation is coherent only if real losses offset real gains.
- Tax the taxpayer's **net real gain** - not the upper tail of asset outcomes.
- Symmetric real-gains taxation is the clean system.

**Next extension**

Estimate sector-specific dispersion wedges and introduce them into VURMTAX to quantify effects on real GDP, real consumption, investment, output, employment, etc.

# 12. Conclusion

1

## The current system can tax pure inflation.

13.8% of terminal value at 30 years; long-run upper bound of 23.5% at the top marginal rate.

2

## The new system can be more burdensome.

19.9% at 30 years in the central case because some real losses are not recognised.

3

## The CGT design principle should be symmetry.

Index real gains and recognise real losses on the same basis, so CGT applies to net real gains.

**A move to indexation is justified only if real losses are recognised together with real gains.**