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Real Estate Institute of Australia

2 August 2006

General Manager
Superannuation, Retirement and
Savings Division
The Treasury
Langton Crescent
PARKES ACT 2600

Dear General Manager

The Treasurer announced proposed changes to superannuation arrangements to simplify and streamline superannuation arrangements.

The Real Estate Institute of Australia (REIA) has some concerns about the proposed changes and a submission is enclosed for consideration by Government.

I would welcome the opportunity to discuss the submission.

Yours sincerely

Bryan Stevens
Chief Executive Officer
Real Estate Institute of Australia

Enclosure:
1. REIA Submission on Superannuation Changes Proposed by Government dated 2 August 2006

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Real Estate Institute of Australia

REIA SUBMISSION TO GOVERNMENT ON PROPOSED CHANGES TO SUPERANNUATION IN THE FEDERAL BUDGET 2006/07

PROPOSAL

1. The Real Estate Institute of Australia (REIA) proposes that Government consider the following changes to proposals contained within the recent Federal budget in order to provide for relevant and sustainable superannuation arrangements:

   a. retain maximum limits for individuals to annually access their superannuation benefits, in order to ensure superannuation funds are not prematurely exhausted by a minority of people who may not be able to properly manage their funds;
   b. provide incentive for individuals to save through superannuation and remain in the workforce by removing taxation of funds in an individual's superannuation scheme, rather than exempting personal income tax on withdrawals from the age of 60 years old;
   c. reassess individuals' concessional deductible contributions to allow for their greater saving capacity later in their working life rather than introducing a universal threshold across their entire working life;
   d. reform Government policy on retirement income to include four pillars, ie pension, mandatory savings, voluntary savings, and home ownership;
   e. allow individuals access to their voluntary contributions in superannuation, with defined limits, for the purpose of a deposit to purchase their principal place of residence; and
   f. introduce a sliding scale for capital gains tax (CGT) and also allow unencumbered property to be "rolled" into an individual's superannuation scheme in order to stabilize the property market, promote self-funded retirement, and improve housing affordability.

INTRODUCTION

2. The REIA is the peak national professional association for the real estate industry in Australia. The REIA has eight members comprised of the State and Territory real estate institutes, through which about 80% of real estate agencies are collectively represented. Additionally, the REIA has formal strategic alliances with the National Real Estate Franchise Association which includes all the major franchises in Australia, and with the Australian Commercial Property Agents Association which includes all the major commercial companies in Australia. The REIA represents the full spectrum of real estate agents across Australia.

3. The REIA acknowledges the proposal of the Government to simplify superannuation arrangements and welcomes the opportunity to comment on these proposals. However, the REIA has some concerns which are shown below.

ISSUES WITH PROPOSALS

Incentive to Work

4. The Government Intergenerational Report 2002/03 concluded that men aged 60 to 64 years old are much more likely to leave the workforce altogether on ceasing full-time work than to opt for part-time work. In response, the Government has inter alia consistently indicated the need for older Australians to remain in the workforce. In the recent budget proposals, Government is offering an incentive *not* to work through tax exemptions from superannuation for those people over 60 years old. In a future of an ageing population and shrinking tax base, it would seem that any tax incentives should be set at a later age than 60 years old in order to encourage people to stay in the workforce. Perhaps the threshold for tax-free superannuation benefits should be set at not less than 65 years old?

5. Moreover, the removal of tax from funds taken out of a superannuation scheme may be, in part, inflationary. Retirees may see this as a windfall and choose to use the extra funds (otherwise previously representing tax payments) for retail spending on trips, white goods, cars, boats etc. However, if tax concessions are alternatively only limited to funds whilst *inside* the superannuation scheme, the benefits cannot be immediately accessed because the benefits are effectively "locked up" in the superannuation fund. Therefore, there is less likelihood of inflationary consequences but there remains a clear incentive to "save" through superannuation funds.

Superannuation Limits

6. There are no longer any Reasonable Benefit Limits and no minimum or maximum amounts that may be taken out of a superannuation fund. This leaves room for individuals, albeit probably a minority who cannot properly manage their superannuation funds, to use all of their superannuation with years still remaining in retirement. When their funds are effectively exhausted, individuals may opt to apply for a pension from the Government. This would be very costly to the Government at a time when there is an ageing population and shrinking tax base. This is particularly concerning in the context of the Government Intergenerational Report 2002/03 which showed projections of a gap between Commonwealth spending and revenue with spending exceeding revenue in around 15 years.

Concessional Deductible Contributions

7. Government has proposed raising the amount of concessional deductible contributions allowed by younger people to $50,000 pa and decreasing the amount of concessional deductible contributions allowed by people over 50 years old to $50,000 pa (down from $100,587pa). Government has sensibly proposed a transitional period for people aged 50 and above to allow those planning to retire soon to make larger contributions.

8. The REIA considers that a universal threshold of $50,000 pa for all ages does not sufficiently recognise the realities of people's ability to utilise this arrangement which will ultimately adversely affect their ability to provide for self-funded retirement. In their early years, people are likely to be paying off HECS debt, travelling overseas, buying a first home, raising a family, establishing their home, and establishing

a business. It is highly unlikely that the majority of people will have money left over to contribute up to $50,000 in concessional deductible contributions to their superannuation scheme. Additionally, people in their 20's and 30's pay relatively little attention to their future needs in superannuation. Conversely, people aged in their 50's have an increased awareness of superannuation at a time when they will have reduced debts including their home mortgage or paid it off, have children starting to leave home, and increased their financial assets. They would need to use this opportunity to contribute significantly and probably in increasing amounts from the age of 50 to 65 years old, particularly to make up for their earlier inability to make significant contributions. Therefore, it is suggested that the threshold for concessional deductible contributions be retained at about $75,000 - $100,000 pa for people over 50 years old.

9. Anecdotally, the REIA is aware that as a result of proposed changes to superannuation, some financial planners are already advising their clients that they consider using interest only mortgages on their primary place of residence and place extra funds in their superannuation with a view to withdrawing a lump sum at retirement to pay off the principal part of the loan. This is not the intended purpose of superannuation and in many cases may lead to a reduction in availability of superannuation funds for living.

10. A case study example is shown below including Charts 1 and 2.

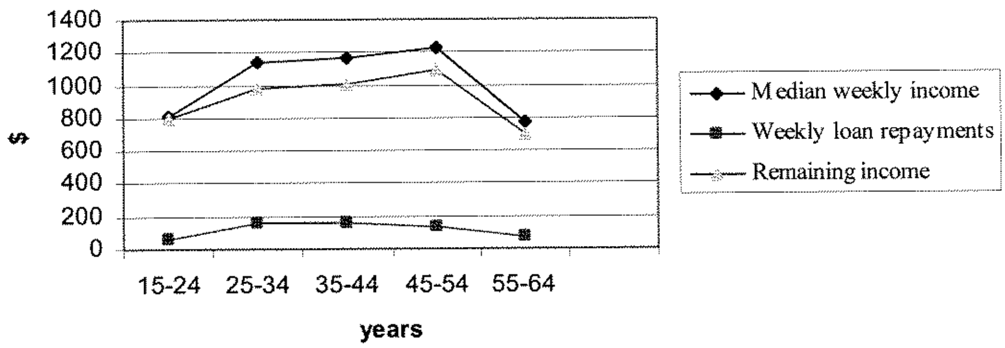

Chart 1: Income and liabilities

Based on household characteristics, and assets and liabilities data, reported by the ABS (Household Wealth and Wealth Distribution 2003-04, Cat. No. 6554.0), median weekly income increases markedly in the 25 -34 year age group, and then only slightly until it peaks in the 45 – 54 year age group. Income declines significantly in the 55 – 64 year age group, presumably as people begin to retire. The total liabilities, including property, study, credit card, vehicle and investment loans, are already quite sizeable in the 15 – 24 year age group, then almost double in the 25 – 34 year age group, remaining steady through the 35 – 44 year age group, before a slight decline in the 45 – 54 year age group, and a major decline in the 55 – 64 year age group. The relationship between income and liabilities is such that remaining income to meet other financial expenditure is lowest at age 15 – 24, and plateaus in the 25 – 34 and 35 – 44 age groups. It reaches a peak in the 45 – 54 age group, and declines significantly as individuals begin to retire in the 55 – 64 year age group. The financial (liquid) assets (excluding superannuation and property assets) of individuals also increase significantly as they move through the lifecycle. A major increase begins in the 35 – 44 year age group, and, as with available income, peaks in the 45 – 54 year age group.

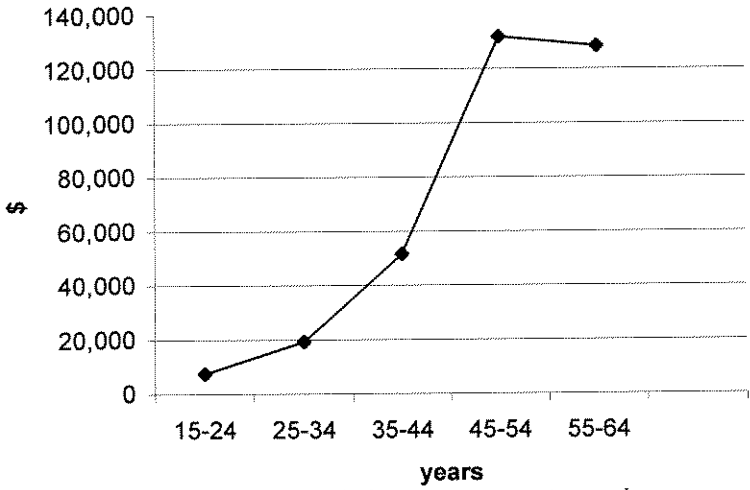

Chart 2: Financial (liquid) assets, excluding superannuation and property

Simplified Superannuation

11. The benefits of the proposed changes to superannuation recently indicated by Government include:

a. increased retirement benefits; and encouragement to save,
b. greater incentive to work and save; and
c. a simplified scheme with reduced costs to funds (which hopefully will be passed onto superannuation members).

12. The REIA considers that not all these benefits will be realised because the proposals will potentially:

a. encourage retirees to spend more of their "windfall" superannuation than they would have done under current taxation arrangements, which may have a detrimental effect on inflation;
b. encourage people to retire earlier because their retirement benefits have been increased substantially from the age of 60 years old; and
c. cause younger people who are working to resent retirees over the age of 60 years old because they no longer effectively pay taxes (on their superannuation income) and the personal income tax burden is almost completely shifted to the young; and

13. Moreover, there should be no taxation concessions to relevant retirees with government pensions from unfunded untaxed schemes including the CSS and PSS, because they have already received assistance through generous government contributions over the life of the scheme. It would be more appropriate to make concessions to government pensions by annual indexation to Average Weekly Earnings rather than to the Consumer Price Index.

OTHER PROPOSALS

Government's Retirement Income Policy

14. The Government policy on retirement income includes a three pillar approach:

a. a taxpayer funded means-tested age pension for people who are unable to fully support themselves in retirement;
b. a minimum level of compulsory employer superannuation contributions made in respect of employees; and
c. voluntary private superannuation and other savings, supported by incentives to save for retirement and incentives to stay engaged with the workforce.

The policy objective is to assist and encourage people to achieve a higher standard of living in retirement than would be possible from the age pension alone.

15. A major omission from debate on superannuation and self-funded retirement is that retirement largely explicitly assumes home ownership. If a home is not owned at retirement, a retiree would need a superannuation fund of at least $200,000 yielding 5% pa to pay for a modest rent of $200 pw. A fourth pillar is missing from Government policy and public debate on superannuation and self-funded retirement, ie home ownership. Home ownership and the accompanying social benefits will reduce the burden on Government pensions and welfare, including aged care infrastructure.

16. Research shows that home ownership confers cultural benefits, social stability, economic welfare and community development. Research also shows that home owners are less likely to have health problems with consequent savings for government budgets and work force productivity.

17. A home is also the cornerstone of wealth creation. Wealth creation is the major part of voluntary savings in Government policy. Wealth gives people financial freedom and the ability to make life-style choices including education for children and self-funded retirement. Individual wealth reduces the need for, and reliance on, a range of Government financial assistance programs. Any investment portfolio should be balanced with a range of different investments to spread the inevitable risks associated with achieving future earnings, particularly since the majority of superannuation funds invest in the share market. Similarly, entrepreneurs create wealth by taking risk in small business which buy or lease property for business, and these businesses often constitute a large part of their superannuation. There are about 1.3 million small businesses in Australia. A major incentive for first home buyers, last home downsize buyers, investors and small businesses are the taxation arrangements.

18. Housing affordability has been at historical lows since 1995. Home ownership in terms of owner-occupied dwellings fell from 69% in 1986 to 67% in 2001. A CEDA report in 2001 showed home ownership for 25-34 year olds dropped 10% from 1981 to 1996. A NATSEM report in 2003 showed that home ownership for 25-39 year olds dropped from 64% in 1989 to 54% in 1999. The decline in home ownership substantially increases the reliance on rental properties that do not provide any equity for the tenant.

19. First home ownership as a proportion of total home buyers is about 19% as at April this year. For the period July 2002 to June 2005 the average has been 15% compared to an historical average of about 22% for 1991 to 2002.

20. The REIA welcomes and acknowledges the Government's commitment to home ownership and wealth creation, eg First Home Owners Grant Scheme and negative gearing. Impediments to home ownership are largely at the State and local government levels, eg stamp duty, planning processes, and infrastructure charges. However, the Federal Government is able to better inform public awareness and commitment to home ownership by directly acknowledging this in Government policy. The REIA proposes that Government adopt an explicit fourth pillar to retirement income policy, ie home ownership.

Early Access to Superannuation

21. House prices in Australia have moved constantly upwards since mid-1996 and market conditions are making it increasingly difficult for both first homebuyers and low income earners to enter the property market.

22. In response to concerns that a significant sector of the Australian community may be unable to become home owners due to decreasing housing affordability, the REIA commissioned a report on Early Access to Superannuation for Home Purchase by professor Julian Disney, Director of the Social Justice Project, University of New South Wales during March 2003.

23. The report explores the potential for people not otherwise able to purchase a home to achieve full ownership before or upon retirement through access to their voluntary superannuation contributions and concludes that such a scheme represents an important opportunity that could enable a larger proportion of lower and middle income earners to realise home ownership, underpinning self-funded retirement.

24. A scheme for early access to superannuation would not only enable earlier home ownership in the under 40 age group, it will have the added benefit of encouraging participants to make additional voluntary superannuation contributions as a means of saving for a home. In doing so, this process will expose the cohort to the importance of saving for retirement while also enabling personal wealth creation through the generation of increased asset equity.

25. This housing wealth can be unlocked through the development and promotion of supporting strategies able to convert the asset wealth of a retiree into either imputed or actual income. Currently, the wealth may be unlocked through a downsize sale, leasing the property or through other means such as a reverse mortgage.

26. In order to ensure that the raison d'être of superannuation is preserved; a scheme for access to superannuation could involve several important principles, eg:

a. access is only available to first home buyers;
b. access is for the purpose of providing or augmenting a deposit for a home;
c. only voluntary savings in the superannuation scheme are available;
d. there must be a certain level of funds in the scheme; and
e. the home must be owner-occupied for a period of time before sale or lease.

Capital Gains Tax (CGT)

27. REIA put a submission to the international comparison review of Australian taxes in which it proposed changes to CGT through a sliding scale and/or expanding small business concessions on CGT to include individuals. This would:

a. help stabilize the real property market in the future by providing disincentives for short term investment combined with incentives for long term property investment;
b. promote self-funded retirement; and
c. free up supply of property which should help affordability.

A copy of the full proposal is enclosed.

28. REIA considers that either or both modifications to CGT would provide benefits for self-funded retirees and help reduce future reliance on the Government for welfare and income support programs for retirees, particularly with an aging population and shrinking tax base.

29. REIA has proposed:

a. a model of declining CGT over a 10-year period – the rate of CGT would be 75% in year 1 and would decline on a linear sliding scale to 30% in Year 10 and would remain at that level thereafter;
b. adapting the small business 15-year CGT exemption to allow individuals of 55 years or over and retiring, or who were permanently incapacitated, and who had owned an asset continuously for 15 years to be exempt from CGT. (Currently the best an individual can do who is ineligible for a small business concession is to be eligible for the CGT 50% discount); and
c. increasing the retirement exemption for capital gains from a lifetime limit of up to $500,000 to a maximum of $1,000,000.

30. The benefits from the declining CGT model would be:

a. an incentive for property investors to hold the property for at least six years if CGT in excess of the current 50% is to be avoided;
b. after 10 years, the CGT liability would still be at the taxpayer's marginal rate but would be calculated on 30% of the realised capital gain rather than 50%;
c. helping to curtail 'off-the-plan' speculative property investment and 'get rich quick' schemes; and
d. the 10-year period is greater than the historical period of about seven years between property booms.

31. The benefits of the 15 year CGT exemption for individuals would be as follows:

a. individuals on about average wages cannot simply "save" for retirement. With the assistance of negative gearing, individuals would be able to invest for self-funded retirement;

b. with the prospect of 100% CGT exemption after 15 years of ownership, the number of individuals investing in property in the longer term would probably increase;

c. there would be an incentive to sell property at retirement, thereby freeing up property supply; and

d. future reliance on the Government for welfare and income support programs for retirees would be substantially reduced.

SUMMARY

32. The REIA welcomes Government initiatives to simplify superannuation arrangements and assist individuals in their retirement through beneficial taxation arrangements. Whilst many of the initiatives are attractive to individuals, they do not appear to achieve major Government objectives. Indeed, they are potentially inflationary, offer incentives for people to leave the workforce and permit superannuation savings to be squandered.

33. The REIA has proposed alternative measures to meet Government objectives including changes to taxation of superannuation, restrictions on access to superannuation, adjustment to Government policy on retirement income, and a sliding scale of CGT which is linked to superannuation

Prepared by:

Secretariat
Real Estate Institute of Australia

2 August 2006

Enclosure:
1. REIA Proposal on Capital Gains Tax dated 15 September 2005

Real Estate Institute of Australia

REIA PROSPOSAL FOR CHANGE TO CAPITAL GAINS TAX

PROPOSAL

1. The REIA proposes that there may be merit in developing changes to Capital Gains Tax (CGT) through a sliding tax scale and/or expanding small business concessions on CGT to include individuals, in order to help stabilize the real property market in the future and help to provide for self-funded retirement.

BACKGROUND

2. A healthy and steady property market is good for the socio-economic development of Australia. REIA has advocated policies which are designed to sustain a healthy property market largely on the basis of the life-cycle of home ownership and wealth creation through property investment and provision for aged care. The REIA continues to advocate to Government that home ownership should be "the fourth pillar of superannuation".

3. CGT is often analysed and criticised in the media and public debate largely because it is seen to have contributed significantly to the property boom and made housing less affordable. The Prime Minister has publicly stated that "... people have argued from time to time, perhaps not as loudly, for an alteration in the existing capital gains tax regime for housing, once again it's not an argument that's ever found any favour with me and I think unlikely to find favour with anybody in my Government" (Address to CSR on 21 March 2005). The REIA welcomes this statement by the Prime Minister but recognises that there may be merit in the evolution of CGT as socio-economic circumstances dictate.

4. Two significant events may give cause to review CGT. Firstly, the property boom post mortems and secondly the ageing population in Australia which was highlighted by Government in the Intergenerational Report. This paper outlines scope for change which might be considered by Government in order to:

- a. help stabilize the real property market in the future by providing disincentives for short term speculation, combined with incentives for long term property investment, and eventual reward for selling the property thereby also freeing up supply, and
- b. promote self-funded retirement including superannuation.

DRIVERS FOR CHANGE IN CGT

5. One of the primary objectives of the Federal Government is to ensure stable, sustainable economic growth for Australia. Policies that are helping to achieve a sound sustainable domestic economy in a dynamic global economy are the monetary policy driven by the Reserve Bank of Australia (RBA) and the Government's drive for taxation, industrial relations, and social reform.

6. Since May 2002, through five upward adjustments in interest rates and rhetoric to talk down property investment, the RBA has been able to assist slowing a very rapid growth in domestic demand to a more sustainable trend. Household spending has declined, the rate of debt growth, which had reached unprecedented levels has slowed, and the unsustainable rate of growth in the housing sector between 1997 and 2003 has abated. The 'soft landing' of the housing sector is expected to result in a much more sustainable level of growth for housing construction, and home purchases by owner-occupiers and investors in the foreseeable future.

7. The major tax reforms introduced by the Government in the last two Budgets (2004-05 and 2005-06) have, *inter alia,* reduced the tax burden on the majority of tax-payers and provided an opportunity for increased savings and investment. Among the tax reforms, the Government stated that the abolition of the superannuation surcharge would simplify the operation of the superannuation system, boost the savings of affected individuals, and provide incentives for individuals to make additional voluntary savings through the superannuation system. This in turn, would help reduce the future burden of social welfare payments from the Federal Budget. The Government has expressed concern about the budgetary implications of the rapidly increasing proportion of Australia's population nearing, or having reached retirement age. REIA considers that additional tax reforms through simple yet significant modifications to the existing CGT laws could provide additional benefits for self-funded retirees and further reduce future reliance on the Government for welfare and income support programs for retirees.

8. In response to the Government Inquiry into First Home Ownership, the Productivity Commission stated in their report of March 2004 that, in relation to the need for a review of aspects of the personal income tax regime that may have recently contributed to excessive investment in rental housing, "The focus of the review should be on the Capital Gains Tax provisions. However, it should also assess 'second best' options for addressing distortions in incentives to invest in housing and other asset markets, including: restrictions on negative gearing and changes to the capital works deduction provisions for buildings. Pending such a review, it would not be appropriate to make housing-specific changes to negative gearing rules or to capital gains tax arrangements". There has been no review.

CAPITAL GAINS TAX

Key Aspects of CGT

9. It is apparent from the 135 pages of the ATO 2003-04 Guide to CGT that there are many factors and circumstances that determine the amount of CGT payable when a CGT event happens. Most CGT events involve a CGT asset. The most common CGT assets are land and buildings, shares in a company, or units in a unit trust. Less well-known assets include contractual rights, options, foreign currency, leases, licences and goodwill.

10. Some CGT events, such as the disposal of a CGT asset, happen often and affect many different taxpayers. Other CGT events are rare and affect only a few taxpayers, for example, those concerned directly with capital receipts and not involving a CGT asset.

11. CGT is payable on any capital gains made that are included in a taxpayer's annual tax return. There is no separate tax on capital gains. It is a component of the taxpayer's income tax. Currently, CGT is generally payable on a taxpayer's **net capital gain** at the taxpayer's marginal rate.

12. Net capital gain is the difference between total capital gains for the year and total capital losses (from business and other assets), less any relevant **CGT discount or concessions.** Any capital gains made during a year must be included as assessable income in an income tax return.

CGT Discount and Concessions

13. If a CGT event that gives rise to a capital gain happened after 21 September 1999 and the asset has been owned by the taxpayer for at least 12 months, a CGT discount of 50% may be applicable to individuals (including partners and partnerships) and trusts. This discount is not available for companies. There are further rules for beneficiaries entitled to a share of a trust capital gain.

14. Special rules apply to depreciating assets that have limited effective lives and can reasonably be expected to decline in value over the time they are used.

15. In addition, concessions are available for small business. The following concessions are available *only* for small business.

a. The **small business 15-year exemption** provides a total exemption for a capital gain on a CGT asset if the asset has been owned continuously for at least 15 years and the relevant individual is 55 years old or over and retiring, or is permanently incapacitated. This concession applies to active assets only, ie assets that are part of the business.

b. The **small business 50% active asset reduction** provides a 50% reduction of a capital gain. An active asset is one that is part of the business. Rental income is specifically excluded from the definition of active asset.

c. The **small business retirement exemption** provides an exemption for capital gains up to a lifetime limit of $500,000. If the recipient is under 55 years old, the amount must be paid into a superannuation (or similar) fund.

d. The **small business rollover** provides a deferral of a capital gain if a replacement asset is acquired. However, a capital gain may be made equal to the deferred gain if the replacement asset is disposed of or its use changes in particular ways. In this case the deferred capital gain is in addition to any capital gain made on disposal of the replacement asset.

The Purpose of CGT Concessions

16. Informal advice to REIA from the Commonwealth Treasury was that the CGT concessions for small business were introduced to specifically assist owners of small business to either expand their business or to provide for their self-funded retirement. The policy is in recognition of the contribution of small business to the national economy including employment, and the difficulty experienced by many small business people of adequately providing for their self-funded retirement whilst simultaneously needing to reinvest in their business ventures.

17. Treasury also advised that these concessions were considered to be inappropriate for individuals because generally, individuals are able to more readily acquire assets specifically for their self-funded retirement.

POSSIBLE CHANGES TO CGT

18. Against this background and the great range of possible scenarios that could be formulated for modelling possible changes to CGT, a pragmatic approach has been adopted to provide two models:

a. a simple model for modifying CGT applicable to a real property CGT asset event is proposed, and

b. the concessions to small business are examined with a view to determining possible changes to the CGT legislation that may also be appropriate for individuals as further incentives to promote the acquisition of **real property** to assist self-funded retirement.

A "Rate of Declining CGT" Model

19. The graph at Annex A shows a model that would meet the objective of taxing speculative investors at higher rates of CGT compared to long-term investors. Key features of the model are:

a. It is simple.

b. If a speculator in real property bought off-the-plan with a view to making quick capital gains by selling within four years for example, the CGT payable within 1 year would be 75% after which the rate would decrease on a linear sliding scale to 60% at the end of Year 4.

c. The rate of CGT payable on realisation of a sale of real property would decline over a 10-year period to 30% by Year 10 and would remain at that level thereafter. The 10 year period will ensure that the investment is outside the limits of the historical period between property booms of about seven years.

d. The model clearly provides an incentive for investors in property to hold the investment for at least 6 years if CGT in excess of the current 50% rate is to be avoided.

e. The final rate of 30% CGT after 10 years means that the tax liability would still be at the taxpayer's marginal rate but would be calculated on 30% of the realised capital gain rather than 50%.

Such a model would potentially curtail "off-the-plan" speculative property investment and "get rich quick" schemes. It provides an incentive for individuals to invest in property in the longer term with a view to making a significant contribution to their self-funded retirement.

20. Given the precedent of excluding individuals and large companies from the CGT concessions to small businesses, it should be feasible for a model of declining CGT on property for individuals to be considered as a realistic possibility.

Possible Adaptations of the Concessions to Small Business

21. REIA supports each of the existing CGT concessions for small business. It is suggested, however, that the first concession, namely the small business 15-year exemption be modified to include individuals. This change would therefore allow an individual of 55 years or over and retiring, or who was permanently incapacitated, and who has owned an asset for at least 15 years to be exempt from CGT. Currently, the best that an individual can do who is ineligible for a small business CGT concession is to be eligible for the CGT 50% discount.

22. If the change suggested in Paragraph 22 was introduced, individuals would be encouraged to invest in property for the longer term. With the assistance of negative gearing to enable individuals to invest in property that they otherwise would not be able to afford, combined with the prospect of a 100% CGT exemption after 15 years of ownership, could be expected to have a significant effect on increasing the number of individuals investing in property for the longer term. There is also an incentive to sell property at retirement. Moreover, by selling property of long standing to "roll over" gains into a superannuation fund, this would help to free up the supply of property particularly in inner city suburbs.

23. It would also seem appropriate that the lifetime limit of $500,000 on the small business retirement exemption be raised significantly. That limit was introduced into the legislation in July 1997 and has not been changed since that time. However, over the last eight years the CPI has increased 23%, full-time adult average total weekly earnings have increased 40%, median weekly house rents have risen approximately 40% and median house prices in Sydney and Melbourne have risen 114% and 93% respectively. It would therefore, be appropriate that the limit of $500,000 be increased to $1,000,000 where it could remain for say five years before being reviewed again.

LIKELY IMPACTS ON THE FEDERAL BUDGET

24. Because of the complexities of estimating CGT across the range of asset classes, it is difficult to determine the order of magnitude that the proposed model of a rate of declining CGT on property might have on the Federal budget. This will need to be costed.

25. Table 1 illustrates the number of individuals, companies and funds that have paid tax on net capital gains for the tax years 1997-98 to 2002-03.

Table 1. Net Capital Gains Subject to Tax, 1997-98 to 2003-03.

	1997-98	1998-99	1999-00	2000-01	2001-02	2002-03
Taxable individuals No.	734,282	809,787	857,458	1,176,926	919,083	663,045
Taxable companies No.	12,614	14,160	15,922	14,508	14,246	12,064
Taxable funds No.	40,326	47,263	56,781	76,172	70,148	50,792
Total number with capital gains No.	**787,222**	**871,210**	**930,176**	**1,267,606**	**1,003,477**	**725,901**
Net capital gains $m	17,462	19,889	21,068	16,516	13,019	10,743
Tax payable on net gains $m	**3,779**	**5,224**	**5,329**	**4,230**	**3,598**	**3,253**

Source: ATO, Taxation Statistics.

26. From Table 1, the total number of taxpaying entities (individuals, companies and funds) that were liable for, and paid CGT on their net capital gains, steadily increased in the years immediately preceding the introduction of "A New Tax System (*ANTS*)" in July 2000 and reached a peak in 2000-01. The introduction of *ANTS* not only brought in the GST but changes to CGT as well, and there is little doubt that these major changes to Australia's taxation system impacted on the number of taxpayers claiming net capital gains at that time. Another major influence was the beginning of the unprecedented rapid escalation in property prices that began in 1998-99 and continued through to the end of 2004. Apart from showing the movements from year to year in tax payable on net capital gains, Table 1 shows that the annual amounts of tax payable on net gains ranged from $3.2 billion to $5.3 billion. REIA is unable to determine what effect the proposals outlined in this paper may have on these estimates.

SUMMARY

27. REIA supports recent Government action to remove the superannuation surcharge to encourage individuals to make additional voluntary savings through the superannuation system for self-funded retirement. However, by making some simple yet significant changes to the CGT laws, additional incentives could be provided to individuals for increasing their contributions towards self-funded retirement and further reducing the burden of social welfare and income support programs for retirees in the Federal budget.

28. There are two broad possibilities for change: first, a declining rate of CGT, and second, expanding small business CGT concessions to individuals.

Prepared by:

Secretariat
Real Estate Institute of Australia

15 September 2005

Annex:
A. Rate of Declining CGT

ANNEX A TO
REIA PROPOSAL FOR CHANGE TO CGT
DATED 15 SEPTEMBER 2005