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CAPITAL GAINS TAX COST BASE PROVISIONS

Financial Implications ($m)

1997-98	1998-99	1999-2000	2000-01
5	80	120	125

Explanation

The Government has decided to amend the *Income Tax Assessment Act 1936* (ITAA) to ensure that, where the established cost base reduction rules do not apply:

- expenditure must be included in the cost base of an asset only to the extent that net revenue deductions are not allowable as a result of the expenditure; and

- the indexed cost base of an asset must be calculated by reducing the indexed expenditure on the asset by any net revenue deductions allowable as a result of the expenditure.

This will apply to the disposal of assets acquired after 7.30 pm AEST, 13 May 1997. It will have no implications for assets acquired prior to 7.30 pm AEST, 13 May 1997. Expenditure undertaken on assets acquired after 7.30 pm AEST, 13 May 1997 will continue to be fully deductible but will no longer be able to benefit from the cost base adjustment.

In principle an item of expenditure should either be deductible for income tax purposes, or included in the capital gains tax (CGT) cost base of an underlying asset, but not both. The CGT provisions reduce costs and expenditures that form part of the cost base to the extent that they are allowable as deductions. Section 82 of the ITAA also specifically attempts to prevent double deductions.

However, anomalies in the current tax treatment have given rise to double deductions in respect of certain capital expenditure items. A taxpayer can effectively claim the cost of the capital expenditure twice — first from income tax under capital allowance provisions, and second from inclusion of expenditure in the cost base of the underlying asset resulting in a reduction in CGT gains, or an increase in CGT losses, when the asset is sold.

Examples where this problem can arise include in respect of expenditure on: extending telephone lines; connecting mains electricity; traveller accommodation; and buildings and structural improvements covered by Division 10D of the ITAA.

To limit the increase in compliance costs arising from this measure, a single calculation will need to be undertaken at the time of disposal of an affected underlying asset. This concession will allow taxpayers to calculate the adjusted indexed cost base of an asset by reducing the indexed expenditure on the asset by the total of any net revenue deductions allowable.

The above material is a full extract of the description of the measure as contained in *Budget Paper No 2: Budget Measures 1997-98*. This paper explains all outlays and revenue measures, and is available from Australian Government Bookshops or from the Treasury Internet site at http://www.treasury.gov.au/budget

CANBERRA
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