**2 June 2026**

Australia 2026/9

# Tax Insights

## Tax Reform No. 1 Bill 2026: CGT and negative gearing changes for property funds

On 28 May 2026, the Australian government introduced Treasury Laws Amendment (Tax Reform No. 1) Bill 2026.

Relevant to property funds, the bill introduces legislation to implement the Federal Budget 2026-27 announcements in respect of:

- Negative gearing limitations; and
- Capital gains tax (CGT) discount changes.

### Key takeaways for property funds

While it is expected that further issues will emerge, key takeaways for property funds include:

- The 30% minimum tax changes are only applicable to individuals;
- The capital loss application ordering rules generally reduce deferred capital gains (eligible for the 50% discount) prior to non-discount gains (other than potentially any pre-1 July 2027 capital gains);
- Quarantined deductions are applied against gross capital gains (in contrast to the normal application of deductions to net capital gains after applying any 50% discount);

- The exclusion from the negative gearing limitations applies to “widely held unit trusts,” which would need to be attribution managed investment trust (AMITs), or “fixed trust” (which very few trusts would satisfy). Given that this is such a long standing and well-known issue, it is hard to understand the choice to adopt this definition in present day drafting;

- A beneficiary in receipt of residential dwelling income distributions can be subject to the negative gearing quarantining rules (e.g., interest on a loan used to fund the investment);

- On-campus student accommodations are excluded from the definition of residential dwelling. It is not clear whether manufactured housing would be a residential dwelling or potentially carved out as a “other mobile home”;

- The reversal of the cost base indexation for certain beneficiaries (e.g., companies or foreign residents) can give rise to adverse outcomes, for example if the trust has significant capital losses that would have eliminated the net capital gain, but which cannot be applied against the capital gain reflecting indexation amounts. Our view is that a trustee should be able to choose not to apply indexation at the trust level. This could also reduce compliance costs of calculating indexation amounts that are ultimately ignored;

- There does not seem to be a requirement to reverse indexation for the purposes of calculating the “fund payment” of a withholding managed investment trust (MIT). Presumably this will be introduced at a later time; and

- The explanatory memorandum (EM) at example 1.6 refers to indexation generally being based on the quarter in which a payment is made, rather than when it is incurred. This does not seem to reflect the drafting in section 960-275(1B). It can be envisaged that capturing the dates of physical payments, as opposed to the date that the relevant expenditure was “incurred” could be a difficult exercise requiring reference back to contracts or cash journals.

## CGT amendments

### Application of CGT amendments

The CGT amendments apply to CGT events on or after 1 July 2027, and assessments for an income year that includes 1 July 2027, regardless of whether an entity has adopted a substituted accounting period. For example, the changes would apply for the income year commencing on 1 January 2027 for a 31 December early balancing entity (although the key date will still be 1 July 2027).

There may therefore be a requirement to separately recognise CGT events arising before 1 July 2027 in respect of the income year that includes 1 July 2027 as a separate category of capital gains for which the CGT discount is available.

### Assets held prior to 30 June 2027: Cost base modification and deferred gains (or losses)

An asset held by a trust before 1 July 2027 is deemed to be sold just before 1 July 2027 and reacquired on 1 July 2027 for market value, or based on an apportionment of consideration from post 1 July 2027 “realisation events” (any CGT event other than CGT event E4, E10, or G1), based on a methodology to be set out in a legislative instrument (not released to date).

The deemed reacquisition results in a modification to the asset’s cost base, and any capital gain (or loss) on the deemed disposal is disregarded. The deemed sale and reacquisition is disregarded for the purposes of satisfying the 12-month holding requirement to apply the CGT discount or indexation.

The "deferred" gain or loss is then required to be recognised at the time of any realisation event occurring on or after 1 July 2027.

In the income year in which a realisation event occurs, two amounts are therefore required to be recognised:

- An amount equal to the initial deferred gain or loss; and
- The capital gain (or loss) arising in respect of the realisation event (reflecting the 1 July 2027 modified cost base).

However, the time of the CGT event in respect of a deferred capital gain will be just before 1 July 2027, such that the deferred capital gain will potentially be eligible for the 50% CGT discount at the time of the realisation event.

Deferred capital gains are only recognised for trusts if, at the end of the income year of the realisation event:

- At least one beneficiary is an Australian resident individual; or
- At least one beneficiary is another trust (other than a complying superannuation entity) to which "section 115-120 does not apply."

Section 115-120 applies where the trustee is subject to tax under section 98 in respect of a foreign resident individual, for example where the trust is not a withholding MIT and a foreign resident individual is a beneficiary.

Where a deferred capital gain cannot be recognised, the 50% discount will not be available for any part of any capital gain in relation to a CGT event occurring on or after 1 July 2027 unless the asset is a new residential dwelling or affordable housing (refer below).

A deferred capital gain is also not recognised if the asset is a new residential or affordable housing dwelling and section 115-102 applies to all of the beneficiaries of the trust. This would be the case where all the beneficiaries are Australian resident individuals (not another trust) and the trustee has not made a choice not to apply section 115-102 (such that the CGT discount method applies rather than the indexation method).

## Capital gain categories: Use of capital losses and quarantined deductions

There will be four new categories of capital gains:

- Deferred non-residential capital gains: Capital gains for deemed CGT events just before 1 July 2027 (other than deferred residential capital gains);
- Deferred residential capital gains: Residential capital gains for deemed CGT events just before 1 July 2027;
- Non-residential capital gains: Capital gains for CGT events on or after 1 July 2027 (other than residential capital gains); and
- Residential capital gains: Residential capital gains for CGT events on or after 1 July 2027.

These categories are relevant for the order of use of current year capital losses and prior year net capital losses, and the application of quarantined negative gearing deductions (refer below).

Any residential capital gain is determined based on the proportion of "residential accommodation days" (days on which a "residential dwelling" (refer below) is used, or held, for the provision of residential accommodation) in the relevant ownership period, being:

- Residential accommodation days on or after 1 July 2027, for the determination of "non-deferred" residential capital gains; and
- Residential accommodation days before 1 July 2027, for the determination of deferred residential capital gains.

The above formula therefore requires historical daily records of the use of a residential dwelling for the entire holding period occurring prior to 1 July 2027, which may not be readily available, noting that there was previously no requirement to record this information.

Current year capital losses (and prior year net capital losses) are applied against the capital gains categories in the order shown above. This generally therefore results in the reduction of deferred capital gains (that are eligible for the CGT discount) prior to the reduction of other gains. There is an ability to choose which capital gains are reduced within a category, such that capital losses can be first applied to (non-deferred) residential capital gains that are not eligible for the 50% CGT discount (i.e., residential capital gains in relation to CGT events occurring on or after 1 July 2027 for dwellings that are not new residential or affordable housing dwellings as well as assets not held for 12 months).

Quarantined amounts relating to negative gearing are then applied, first to any deferred residential capital gains, and then to non-deferred residential capital gains. As quarantined deductions are therefore applied to "gross" capital gains, rather than being deductible against net capital gains (i.e., after the application of the CGT discount), as is the case for deductions generally. It is not stated, but presumably there is an ability to choose which capital gains are reduced within a category, such that quarantined amounts can be first applied to (non-deferred) residential capital gains that are not eligible for the 50% CGT discount (i.e., residential capital gains in relation to CGT events occurring on or after 1 July 2027 for dwellings that are not new residential or affordable housing dwellings).

## Residential dwellings and new residential dwellings

The definition of "residential dwelling" is relevant to:

- The definition of residential capital gain (refer above);
- The definition of new residential dwelling (see below);
- Determining quarantined deductions for using or holding certain residential dwellings as residential accommodation (refer below);
- Identifying non-quarantined residential dwellings (refer below); and
- Identifying gains from the sale of residential dwellings on revenue account for the purposes of reducing quarantined deductions (refer below).

A "residential dwelling" means a "dwelling" (including a unit of accommodation that is a building or is contained in a building, and consists wholly or mainly of residential accommodation) other than any of the following:

- A caravan, mobile tiny home, or other mobile home;
- A hotel, motel, inn, hostel, or boarding house;
- A dwelling providing accommodation to students in connection with a school or an education institution that is not a school;
- A boat or other marine vessel; or
- A dwelling in a class of dwellings determined by the minister by legislative instrument (none released to date).

A residential dwelling is also taken to include any of the following things to the extent that the thing is available for use by an occupant of the dwelling:

- Land adjacent to the dwelling; and
- A garage, storeroom, or other structure associated with the dwelling.

Based on the above, it would appear that build-to-rent, co-living, retirement village units, and purpose-built student accommodation that is not "connected with" a university would normally constitute residential dwellings. It is less clear whether manufactured housing would be included or potentially carved out as an "other mobile home."

A residential dwelling will be a "new residential dwelling" if it meets the requirements set out by legislative instrument (not released to date). Based on the budget announcement, the legislative instrument is expected to cover dwellings constructed on vacant land and circumstances where existing properties are demolished and replaced with a greater number of dwellings, and exclude dwellings that have been previously sold, unless first owned by the builder and not occupied for more than 12 months.

The meaning of "affordable housing dwelling" and the requirements to access the (up to) 60% CGT discount remain unchanged.

## Distribution of discount capital gains

**Pre-1 July 2027 CGT events, including deferred capital gains**

The 50% CGT discount for Australian resident individuals and trusts will continue to apply for CGT events prior to 1 July 2027.

As the time of the CGT event in respect of a deferred capital gain will be just before 1 July 2027, a deferred capital gain of a trust will also potentially be eligible for the 50% CGT discount at the time of a realisation event on or after 1 July 2027.

**New residential dwellings**

Pursuant to section 115-102, the 50% CGT discount remains available for an Australian resident individual that is a beneficiary of a trust with a post-1 July 2027 discount capital gain in respect of a new residential dwelling provided that each interposed entity is "a trust, other than a superannuation fund or a public unit trust" (within the meaning of section 102P) or a partnership (refer section 115-102(4)). This tracing rule replicates the existing section 115-125(3)(a) and (c) in relation to affordable housing. The existing section 115-125(3)(b), which specifically included "a managed investment trust," has not been reflected in section 115-102(4). Section 115-125(3)(b) has also been repealed as part of the amendments. (Both sections do include an MIT in the trust definition via a note although that does not appear to affect the apparent public unit trust exclusion).

The EM at 1.140 states that the tracing rule in section 115-102 applies where a "trust's gain was made directly or indirectly through a trust, a public unit trust or a partnership" and so it seems that public unit trusts are meant to be included (rather than excluded, as a strict reading of section 115-102(4) would suggest). The interpretation in the EM also appears contrary to the drafting of existing section 115-125 which seems intended to exclude public unit trusts and then specifically include MITs. This suggests that there is a drafting error in the EM or the legislation which would need to be amended, or otherwise section 115-102(4) would need to be interpreted in accordance with the clear statement in the EM (although this may be difficult given the drafting). The amendments also appear to create the same issue for tracing pursuant to section 115-125(3) in respect of affordable housing.

The minister may make a legislative instrument to determine additional types of CGT asset for which the 50% discount will remain available (none have been released to date).

It is intended that a trustee can make a choice not to apply section 115-102 in respect of the sale of a new residential dwelling, in which case indexation would apply in respect of expenditure on or after 1 July 2027 (see below). If a trustee makes this choice, an Australian resident beneficiary will not be able to apply the 50% CGT discount.

The drafting in respect of the ability of a trustee to make a choice not to apply section 115-102 refers to the discount capital gain included in the assessable income of the beneficiary, suggesting that the trustee's choice is made on a beneficiary-by-beneficiary basis. This would not be consistent with the EM or section 114-30 setting out the requirements to apply the indexation rules, which provides that section 115-102 must not apply to "the capital gain" in respect of a new residential dwelling asset. It therefore seems like the choice is supposed to be made by the trustee in respect of the capital gain at the trust level.

## Indexation

The indexation method will generally apply to Australian resident individuals and trusts in relation to expenditure incurred on or after 1 July 2027 that is included in the cost base of an asset that has been held for 12 months or more, other than expenditure included in the "third element" (costs of owning the CGT asset). The deemed sale and reacquisition of assets held prior to 1 July 2027 (refer above) operates to deem expenditure equal to the modified cost base to be incurred on 1 July 2027, and therefore eligible for indexation from this date. The deemed sale and reacquisition is, however, disregarded for the purposes of satisfying the 12-month holding requirement to apply indexation.

For costs of acquisitions payable in instalments, the EM (in example 11.6) provides that each instalment is treated as a separate amount of expenditure incurred at the time it is paid, and indexation will be based on the Consumer Price Index for the quarter in which the instalment payment was made. This seems inconsistent with new section 960-275(1B) which refers to the quarter in which expenditure was incurred as well as the note to section 114-10(1) which provides that "[g]enerally expenditure is indexed from when it is incurred. The exception is when there is an acquisition that did not result from a CGT event (but this is limited to a CGT asset that is a share in a company or unit in a unit trust - see section 960-275(1C) and (3)). The first element in this case is indexed from when the expenditure was paid." It can be envisaged that capturing the dates of physical payments, as opposed to the date that the relevant expenditure was "incurred" could be a difficult exercise requiring reference back to contracts or cash journals.

**Choice to apply indexation**

A trust can make a choice not to apply section 115-102 in respect of a new residential dwelling (which would otherwise facilitate the 50% CGT discount being available for Australian resident individuals), in which case the indexation method will apply.

An Australian resident individual that includes a discount capital gain in respect of the sale of a new residential dwelling by a trustee that has made a choice not to apply section 115-102 (such that the trustee applies the indexation method), will not be eligible to apply the 50% discount (i.e., the choice made by the trustee also applies to the beneficiary).

Australian resident individuals that would otherwise be able to apply a 60% discount in respect of the sale of an affordable housing dwelling can also make a choice not to apply section 115-125 (which would otherwise facilitate the CGT discount applying), in which case the indexation method is applied. It is noteworthy that the full 60% discount only applies where the dwelling was acquired on or after 1 January 2018, the individual has been an Australian resident since acquisition, the dwelling has been used to provide affordable housing on every day during the ownership period, and the ownership period is at least three years.

Section 115-125(6) also provides the trustee with the ability to make the choice not to apply section 115-125, which would then also apply to the beneficiary, although in many cases the trustee may not know whether the Australian individual investor meets the continuous residency requirement (such that the full 60% discount applies, subject to the trust meeting the other requirements). As discussed above in relation to new residential dwellings, the choice seems intended to apply in respect of the capital gain at the trust level (although the drafting could suggest that a choice is made for each discount capital gain included in the assessable income of a beneficiary).

**Requirement to “reverse” cost base indexation**

There is a requirement to reverse cost base indexation amounts in the following circumstances:

- The inclusion of a capital gain by a beneficiary that is not entitled to indexation (e.g., where the beneficiary is an Australian company or a foreign resident);
- The calculation of tax payable by a trustee under section 98 (e.g., in respect of the present entitlement of a foreign resident to trust income);
- Where the trustee has made a choice not to apply the 50% CGT discount for the sale of a new residential dwelling or the 60% discount for the sale of an affordable housing dwelling (refer above); or
- For the purposes of determining a trustee’s taxation amount under section 99A (no beneficiary is presently entitled to trust income).

There does not seem to be a requirement to reverse indexation for the purposes of calculating the “fund payment” of a withholding MIT. Presumably this will be introduced at a later date.

In the above circumstances, the relevant capital gain is modified based on the following assumptions:

- The cost base did not include indexation amounts; and
- Capital losses, carry forward net capital losses, and quarantined amounts would still be the same and were not available to reduce the additional capital gain resulting from ignoring cost base indexation.

Amendments have also been included to facilitate the operation of the rules in a situation where a trust has no net capital gain for the income year but would have had a net capital gain based on the above assumptions. In this case the relevant capital gain would be expected to equal the cost base indexation amounts.

The requirement to distribute capital gains reflecting a reversal of cost base indexation amounts to certain beneficiaries can give rise to adverse outcomes, for example if the trust has significant current year losses or carry forward net capital losses that would have eliminated the net capital gain, but which cannot be applied against the capital gain reflecting indexation amounts.

Pursuant to the amendments, the commissioner will, by legislative instrument (not released to date), require trustees to provide information to beneficiaries to enable compliance with their CGT obligations. Trustees that are required to provide an annual investment income report are excluded from the new reporting requirements.

On the basis that the separate categorisation of capital gains as residential capital gains or non-residential capital gains is relevant to Australian resident companies, or even some foreign residents, in applying quarantined amounts, it would appear that indexation amounts would need to be disclosed separately for each of these categories.

## Negative gearing limitations

### Application

The negative gearing amendments apply in relation to the 2028 income year and later income years (i.e., earliest application is 1 January 2027 for a 31 December early balancer).

### Exclusions

#### Excluded dwellings

Deductions in relation to "using or holding residential dwellings as residential accommodation" are not subject to quarantining to the extent that:

- An ownership interest in the dwelling was held prior to 12 May 2026 (non-quarantined residential dwellings). For these purposes entering into a contract to acquire the dwelling is deemed to create an ownership interest; or
- The dwelling is a new residential dwelling (see above).

Legislative instruments may determine exclusions for using or holding dwellings for a particular "activity or purpose" or a particular kind of "business or enterprise." No legislative instrument has been released to date, but the EM suggests that an example of residential dwellings that could be determined in relation to a business or enterprise could include using or holding residential dwellings as rental properties to provide social or affordable housing.

#### Excluded entities

Complying superannuation entities and "widely held unit trusts" (as defined in section 272-105 of schedule 2F) are excluded from the negative gearing limitations.

AMITs are deemed to be widely held unit trusts.

Importing the widely held unit trust definition brings with it the long-standing issue regarding the ability for a trust (other than an AMIT) to meet the "fixed trust" requirement included in section 272-105(1)(a). It has long been recognised that very few trusts would meet this requirement, leading to the Australian Taxation Office issuing Practical Compliance Guideline 2016/16 providing a non-binding administrative concession allowing trustees to "manage the trust's tax affairs as if the commissioner had exercised the discretion [in section 272-5(3)] to treat beneficiaries as having fixed entitlements to income and capital of the trust," as required in order to qualify as a "fixed trust" and to meet the "closely held" restriction (see below).

Given that this is such a long standing and well-known issue, it is hard to understand the choice to adopt this definition in present day drafting of amendments.

Aside from the "fixed trust" requirement, a trust cannot be "closely held." Broadly, a trust will be closely held where 20 individuals (grouping relatives as a single deemed individual), have, directly or indirectly and for their own benefit, "fixed entitlements" to 75% or more of the income or capital of the trust or there are no individuals that have such "fixed entitlements."

### Quarantined deductions

Any non-deductible "quarantined amount" for an income year is determined as follows:

- Determine any excess of otherwise deductible amounts over assessable income relating to the using or holding of residential dwellings as residential accommodation.
- Reduce this amount by:
  - Any excess of assessable income over deductible amounts relating to using or holding:
    - Non-quarantined residential dwellings (i.e., acquired pre-12 May 2026);
    - New residential dwellings; or
    - Dwellings covered by a relevant legislative instrument; and
  - Any gain from a realisation event occurring in relation to a residential dwelling held on revenue account (including post-12 May 2026 residential dwellings that are not new residential dwellings).

A beneficiary of a trust that includes assessable income in relation to the net (taxable) income of the trust referable (either directly or indirectly through one or more interposed partnerships or trusts) to using or holding of residential dwellings is taken to have directly derived assessable income from using or holding of residential dwellings. This can be seen to have two implications:

- The assessable income is included in the determination of any quarantined amount of the beneficiary; and
- Additional deductions of the beneficiary may need to be included in the determination of any quarantined amount of the beneficiary, for example interest deductions in respect of loans used to fund the investment in the trust.

The quarantined amount can then be applied (in order) against deferred residential capital gains and (non-deferred) residential capital gains, noting that capital losses and prior year net capital losses are applied to capital gains ahead of the application of quarantined amounts and in the following order:

- Deferred non-residential capital gains;
- Deferred residential capital gains;
- Non-residential capital gains; and
- Residential capital gains.

It is not stated, but presumably there is an ability to choose which capital gains are reduced within a category, such that quarantined amounts can be first applied to (non-deferred) residential capital gains that are not eligible for the 50% CGT discount (i.e., residential capital gains in relation to CGT events occurring on or after 1 July 2027 for dwellings that are not new residential or affordable housing dwellings).

Any remaining unapplied quarantined amount is treated as “an amount relating to using or holding residential dwellings as residential accommodation” for the next income year. Unlike carry-forward losses of a trust or company, such carry-forward quarantined amounts are not subject to any sort of continuity of ownership requirements.

## Distribution statement disclosures

For income years including 1 July 2027 and later income years, it appears that a trustee will need to separately disclose the following in respect of the CGT discount, indexation, and negative gearing limitations (ignoring affordable housing for simplicity):

- Discount deferred non-residential capital gains (discount percentage is 50%);
- Discount deferred residential capital gains (discount percentage is 50%);
- Discount non-residential capital gains: Pre-1 July 2027 (discount percentage is 50%);
- Discount residential capital gains: Pre-1 July 2027 (discount percentage is 50%);
- Discount component;
- Deferred non-residential capital gains (non-discount);
- Deferred residential capital gains (non-discount);
- Non-residential capital gains: Pre-1 July 2027 (non-discount);
- Non-residential capital gains: Post-1 July 2027—excluding indexation;
- Residential capital gains: Pre-1 July 2027 (non-discount);
- Indexation component—non-residential capital gains: Post-1 July 2027 (can reduce capital gains for beneficiaries that are entitled to indexation);
- Residential capital gains: Post-1 July 2027—excluding indexation and excluding new residential dwellings;
- Indexation component—residential capital gains: Post-1 July 2027 and excluding new residential dwellings;
- Discount new residential dwelling capital gains—no trustee choice (discount percentage is 0% at trust level);
- New residential dwelling capital gains—trustee choice not to apply section 115-102—excluding indexation;
- Indexation component—new residential dwelling capital gains; and
- Net income from using or holding residential dwellings as residential accommodation.

There does not appear to be a choice for a trustee not to apply indexation in the calculation of relevant capital gains. Amendments to provide such a choice would reduce compliance costs for trusts that only have beneficiaries that are not entitled to indexation (e.g., companies and/or foreign residents) by alleviating the trustee of the requirement to calculate indexation components which are ultimately ignored.

As stated in the EM, the CGT and negative gearing amendments “are expected to result in some transitional and ongoing compliance costs for individuals and businesses.”

## Contacts

**Wei-Ee Cheah**
Partner
Tel: +61 3 8486 1532
weicheah@deloitte.com.au

**Andrew Saunderson**
Partner
Tel: +61 2 9322 3083
asaunderson@deloitte.com.au

**Abdol Mostafavi**
Partner
Tel: +61 2 8260 6600
amostafavi@deloitte.com.au

**Michael Barone**
Partner
Tel: +61 2 9322 3532
mbarone@deloitte.com.au

**Richard Lambkin**
Partner
Tel: +61 2 9322 5788
rlambkin@deloitte.com.au

**Matthew Gould**
Partner
Tel: +61 3 9671 8628
mgould@deloitte.com.au

**Richard Buchanan**
Partner
Tel: +61 3 633 77113
ribuchanan@deloitte.com.au

**Sue Ann Khoo**
Partner
Tel: +61 2 9255 7628
sueannkhoo@deloitte.com.au