Killing the Australian Dream: The failure of the capital gains tax discount

Submission to the Select Committee on the Operation of the Capital Gains Tax Discount

The CGT discount has made housing unaffordable, increased inequality, distorted lending, and is reducing investment and productivity. It should be scrapped.

Discussion paper

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Summary

This submission will demonstrate that the 50% CGT discount has introduced a distortion to the tax system that favours the wealthy and increases inequality. It acts as an incentive for housing investors that allows them to outbid prospective owner-occupiers and placed home ownership outside the reach of many.

There is now a growing body of evidence that shows that investor demand for housing that has pushed up prices and forced many families into a lifetime of renting. But this evidence points to the solution. As has been seen in Victoria in recent years, and in changes to macroprudential rules a decade ago, when policies that discourage investors are put in place, house price growth slows, and housing becomes more affordable.

The biggest single incentive for investors is the CGT discount. By scrapping it, the federal government will advantage first home buyers, helping more Australians into a home of their own.

Building more houses will expand housing supply and make housing more affordable. Federal, state, and local governments have made changes designed to encourage more supply and we recommend that should continue. But building more houses will require extensive resources and considerable time. Increasing supply is the slowest, most expensive way to make housing more affordable.

The CGT discount has also distorted bank lending. Since its introduction banks now lend much more to mortgages at the expense of businesses. This has consequences for business investment and productivity.

The CGT discount is causing real harm to Australians and the Australian economy. For this reason, we recommend that it be scrapped.

Introduction

In 1999, the Howard government made one of the most consequential and little understood tax changes of the past 40 years: introducing the capital gains tax discount. A capital gain is essentially the profit accrued from selling an asset – whether it is a property or shares in a company. Prior to the changes, capital gains were taxed by accounting for inflation over the period during which the asset had been held. The changes meant that instead, any realised capital gains on asserts that had been held for more than 12 months are entitled to a 50% tax discount. Realising a capital gain occurs when the asset is sold. This is distinct from accruing a capital gain which happens when the asset goes up in value but has not yet been sold.

While media commentary regularly focuses on “negative gearing”, the ability for investors to keep half of the capital gain from a property investment without paying tax has been a major driver of housing becoming increasingly unaffordable and rising wealth inequality in Australia. The changes turned Australian housing into a speculative investment. Where previously house prices rose largely in line with household incomes, since the introduction of the capital gains tax (CGT) discount they have risen well beyond incomes. Investors have taken advantage of a tax system designed to allow them to reduce their taxable income through negative gearing while holding a property and reduce the tax liability when they sell that property. If negative gearing is the grass fire of the housing affordability crisis, then the CGT discount was the can of petrol poured over the flames.

This paper will outline the changes to the taxation of capital gains and why the 50% discount is unwarranted and has introduced a distortion to the tax system that has reduced housing affordability, increased wealth inequality and distorted the lending market. It will also explore the policy changes that have a demonstrated record of reducing investor activity in the housing market, which are a necessary part of improving housing affordability.

Concessional taxation of capital gains

CAPITAL GAINS ARE TAXED DIFFERENTLY

Income from capital gains is taxed in a unique manner. Other forms of income are taxed at a marginal rate. Examples of this include income from wages, or interest earned from a bank account, or rent from an investment property. All these are included as income and taxed in the same way.

Taxing at a person's marginal rate is the rate of tax paid when you earn an additional dollar of income. Under Australia's progressive marginal tax system, the marginal rate increases as income increases.

Capital gains are treated differently. They are subject to the CGT discount, which means only half the capital gain is subject to income tax. The other half is tax free. Capital gains are one of the only forms of income that are taxed concessionally. The other exception might be earnings from a superannuation account, which are taxed at a different rate and subject to different rules than income. Superannuation, however, is not taxed concessionally but rather taxed in a different way, in a different system.

Before 1999, capital gains were discounted in line with inflation so only the real capital gain was subject to tax. This was also unusual. No other form of income is only subject to real gains. For example, Australia taxes nominal wages – wages that have not been adjusted for inflation – rather than real wages.

In the Australian system, rather than indexing tax brackets to inflation so that only real wages are taxed, nominal wages are taxed and then the federal government periodically gives tax cuts. Without these tax cuts, Australian taxpayers would suffer bracket creep, meaning when their wages increased, often in line with inflation, they would pay more tax relative to the buying power of their wages. It is important to note that long-run analysis of income tax brackets and tax rates since 2001 show that Australian taxpayers have been overcompensated for bracket creep.[1] This means they have paid less tax under the system where they get periodic tax cuts than they would have paid if their tax brackets had been indexed to inflation.

[1] Grudnoff (2018) *Bracket creep: The Imaginary Monster*, https://australiainstitute.org.au/report/bracket-creep-the-imaginary-monster/

This also means that those earning capital gains have been overcompensated for bracket creep on capital gains even without the benefit of the CGT discount. The CGT discount therefore comes on top of this compensation.

CAPITAL GAINS ARE LUMPY

One argument for taxing capital gains concessionally is that multiple years of capital gains can occur in a single year. This means that income from capital gains comes in lumps, and, because of the progressive nature of income tax, this lumpiness could push income from capital gains into higher tax brackets than would otherwise be the case were the capital gains taxed in the year they occurred.

Taxing unrealised capital gains would solve this problem of lumpiness. This is where capital gains are taxed in the year the gain occurs rather than in the year when the capital gain is realised, that is, when the asset is sold. A recent proposal to tax unrealised capital gains in superannuation funds with balances over $3 million, however was met with strong opposition.

MORE CHOICE IN WHEN CAPITAL GAINS ARE EARNED

Someone who earns income from capital gains has more choice in when the capital gain is earned compared with other forms of income. This is because capital gains tax is only paid when the asset is sold, and the capital gain is realised.

It is not always the case that people have complete freedom on when they sell. It may be that they need to sell the asset and realise the capital gain, perhaps because they need the income now. But it is also true that capital gains offer flexibility that many other forms of income do not.

The advantage of this flexibility is that the capital gain could be realised in a year when the person has less other taxable income, which because of our progressive income tax means they pay less tax on the capital gain. For example, someone might wait until they retire from work before realising a capital gain.

CGT DISCOUNT AND ENCOURAGING INVESTMENT

One of the justifications the Howard government gave for the CGT discount was that it would encourage investment. Politicians and pundits claim that capital gains and investment are closely interlinked and taxing capital gains concessionally will encourage people to invest more.

If the CGT discount was meant to encourage investment it failed given the growth in private business investment since the introduction of the CGT discount. The average annual growth rate of private business investment since the introduction of the CGT discount is 40% lower than before the introduction of the CGT discount (5.7% versus 9.4%).[2]

The CGT discount is not well tailored to encouraging investment. It applies to all assets including those that are not investments in the economic sense. For example, it applies to second-hand assets. Someone who buys a residential property that was built sometime in the past and then after several years sells that property could get the tax advantage of the CGT discount, even though no additional housing was created from this transaction. There was simply a change in the ownership of the existing housing stock.

The same is true for shares that were not bought as part of the original float from the company. If a company issues new shares to raise capital that it uses to invest in the business, this can be considered investment. But buying shares from another person is simply a change of ownership with no new investment involved.

PASSIVE VERSUS ACTIVE INCOME

Income from capital gains is known as passive or unearned income. This is distinct from active or earned income, which comes from producing something. Active or earned income includes wages or profit in a business you are involved in.

There is an economic argument for taxing active income at a lower rate than passive income. Active income directly adds to a country's total output, increasing the goods and services available to consumers. Taxing active income at a lower rate encourages this type of activity.

In the 1940s, Australia taxed some passive or unearned income from property at higher rates than wages.[3] The CGT discount reverses this by taxing capital gains, a passive form of income, at a concessional rate.

[2] ABS (2025) *Australian National Accounts: National Income, Expenditure and Produce, June 2025*, https://www.abs.gov.au/statistics/economy/national-accounts/australian-national-accounts-national-income-expenditure-and-product/jun-2025

[3] Davidson (2015) *A brief history of tax: Part 1 Income tax, the great leveller*, https://needtoknowconsulting.org/2015/01/08/a-brief-history-of-tax-part-1-income-tax-the-great-leveller/

NO STRONG CASE FOR TAXING CAPITAL GAINS CONCESSIONALLY

Taxing capital gains concessionally does not encourage investment and it is a regressive policy, only helping those who can buy property or shares and not those whose income is the result of labour and active participation in a business. If there are serious concerns that the lumpiness of capital gains is a problem, then the Parliament should think on better ways to overcome this problem without resorting to a blanket discount.

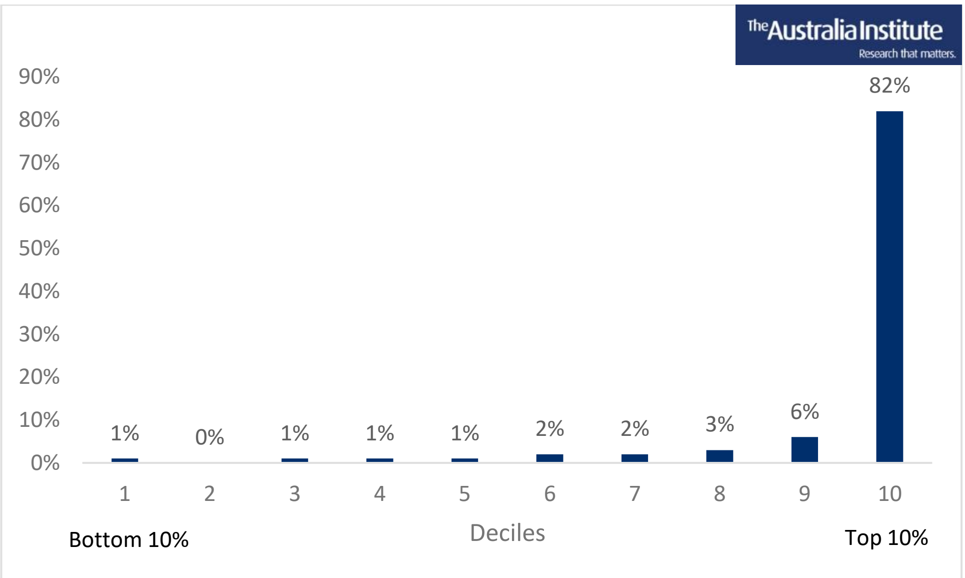
As will be discussed below, there is evidence that high income earners are increasingly structuring their tax affairs so they earn more of their income as capital gains. This shows that people believe that income from capital gains are one of the lowest taxed forms of income.

CGT discount and inequality

INCOME AND AGE

The CGT discount was not merely a technical change in how income is taxed. The discount introduced a distortion to the taxation system that has real-world ramifications. The CGT discount makes inequality worse. Its benefits are skewed to high income earners with 82% of the benefit going to the top 10% of income earners. Half of income earners get only 4% of the benefit. The distribution of the CGT discount is shown in Figure 1.

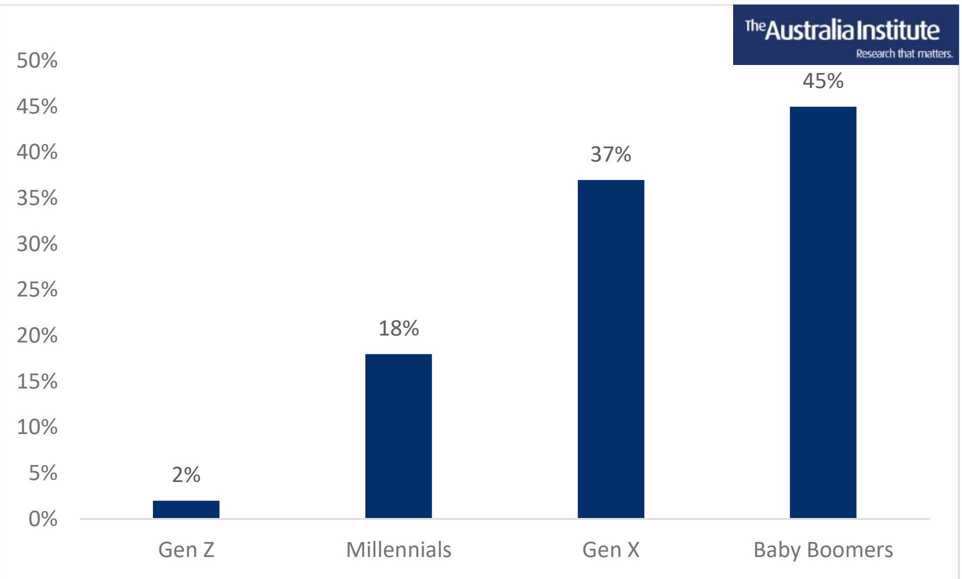
Figure 1: Distribution of the CGT discount by income decile, 2021-22



Source: Australian Treasury (2024) 2024-25 Tax expenditure and insight statement

The CGT discount also disproportionately benefits older people. The generation that gets the biggest benefit are the Baby Boomers. They receive 45%, followed by Gen X, which receives 37%. Millennials receive much less, only 18%, while Gen Z receives only 2%. Figure 2 shows the benefits of the CGT discount by age groups.

Figure 2: Distribution of the CGT discount by age groups, 2021-22[4]



Source: Australian Treasury (2024) 2024-25 Tax expenditure and insight statement

HOUSING INEQUALITY

The CGT discount is also driving housing inequality. As discussed below, the CGT discount is a major cause of the housing affordability crisis, because it has increased investor demand for housing.

More dwellings owned by investors means more rental properties and fewer owner-occupiers. Home ownership rates have been falling since the introduction of the CGT discount. At the same time rental rates have been rising, particularly to private landlords.

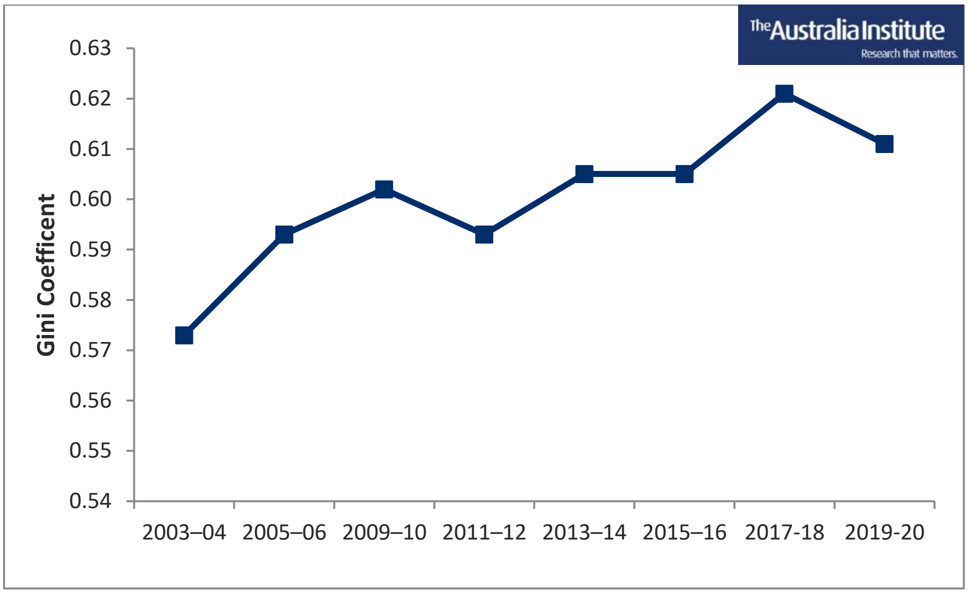
From 1999-2000, the year that the CGT discount was introduced, until 2019-20, the most recent year for which we have data, home ownership rates fell 4.4%. This represents 440,000 fewer households owning their home. For context, the total number of private dwellings in Brisbane is 518,664.[5]

The growing number of investment properties also makes wealth inequality worse. The Gini Coefficient, which is the most common measure of wealth inequality, is showing a deterioration in equality since 2004. A higher Gini Coefficient means a less equal distribution. Figure 3 shows the Gini Coefficient from 2003-04 to 2019-20 (latest ABS data).

[4] Gen Z are people under 30. Millennials are people aged 30 to 44. Gen X is people aged 45 to 59. Baby boomers are people aged 60+

[5] ABS (2022) *Australian census of population and housing, Brisbane, 2021*, https://abs.gov.au/census/find-census-data/quickstats/2021/LGA31000

Figure 3: Gini Coefficient 2003-04 to 2019-20



Source: ABS, *Household Wealth and Wealth distribution, Australia 2003-04 to 2011-12* and ABS, *Household Income and Wealth, 2013-14 to 2019-20*.

In 2025, Australia Institute research examined the growth in Australians wealth by asset type.[6] Eighty percent of Australians' wealth comes from three asset classes: the family home, superannuation, and other property. Other property includes residential property that is not the family home. This is dominated by investment properties but also includes things like holiday homes. It is important to note that the family home is exempt from capital gains tax.

From 2002 to 2022 this category of "other property" was the fastest growing of these asset classes. It grew at an average annual rate of 7.7%. The majority (53%) of the increase went to the wealthiest 10% of households, with just 7% going to the poorest half of Australian households.

As home-ownership rates fall, a smaller proportion of people own their home, which in turn increases wealth inequality. The CGT discount is playing a significant role in this process.

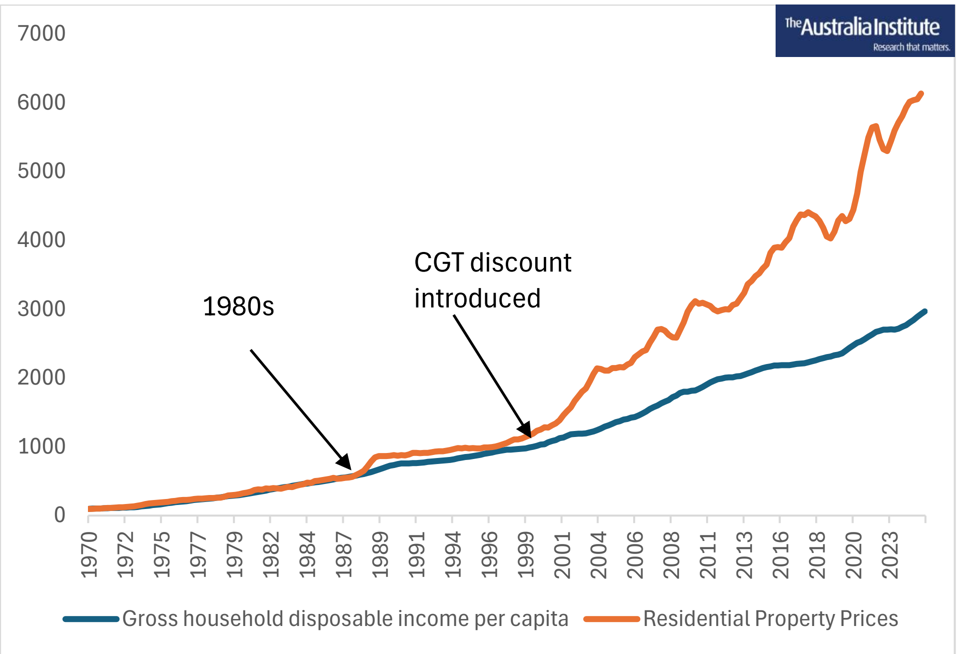
[6] Grudnoff (2025) *Wealth inequality by asset type: What's driving wealth inequality*, https://australiainstitute.org.au/report/wealth-inequality-by-asset-types-whats-driving-wealth-inequality/

The CGT discount and housing affordability

HOUSE PRICE GROWTH AND INCOMES

House prices began to rapidly increase in the early 2000s. As Figure 4 shows, house prices rose in line with household income from 1970 until 2000, other than a brief increase due to the 1980s asset boom. From September 1989 till March 2000, property prices increased at an average annual rate of 4.2%. From March 2000 till June 2025, they increased at a much more rapid annual rate of 15.3%. This is more than three and a half times faster than the pre-2000s rate – and well ahead of household income. From 2000 till 2025 house prices have almost increased fivefold while wages have doubled, increasing by just 120%.[7] A house worth $200,000 in 2000 would be worth about $1,000,000 in 2025 if it increased at the average rate.

Figure 4: Index of Residential Property Prices and Household Disposable Income per capita (1970 = 100)



Source: ABS (2025) National Accounts, BIS (2025) *Australia – Selected residential property prices*, https://data.bis.org/topics/RPP/BIS%2CWS_SPP%2C1.0/Q.AU.N.628?view=observations

When house prices grow faster than incomes, housing becomes less affordable.

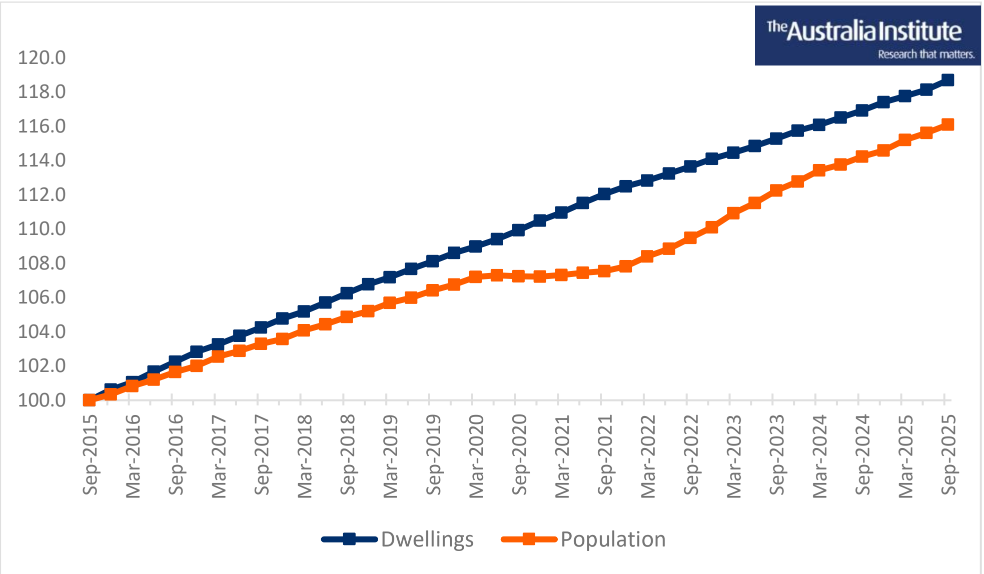
[7] ABS (2025) *Wage Price Index, Australia, September 2025*, https://www.abs.gov.au/statistics/economy/price-indexes-and-inflation/wage-price-index-australia/sep-2025

CAUSES OF THE HOUSING AFFORDABILITY CRISIS: HOUSING SUPPLY AND POPULATION

Pundits regularly assert that the housing affordability crisis was caused by a combination of strong population growth (high demand), and low rates of building new housing (low supply). Some claim the only solution is to build more houses.

But what does the data show about the housing affordability crisis? The population over the last 10 years has increased by 16%.[8] In order to house this increase in population, the number of dwellings would need to increase by at least 16%. But the number of dwellings has increased by more than that at 19% as Figure 5 shows.[9] This means that dwellings have been increasing faster than the population over the last 10 years.

Figure 5: Index of Population and Dwelling Stock (Sep 2015 = 100)



Source: ABS (2025) *National, state and territory population, March 2025*. ABS (2025) *Australian National Accounts: National Income, Expenditure and Product, September 2025*. ABS (2025) *Total Value of Dwellings, September 2025*.

As discussed above house prices started increasing rapidly around the year 2000. This is more than 10 years ago. What happened to the rate of growth in the population and dwellings before the last 10 years?

[8] ABS (2025) *National, state and territory population, March 2025*, https://www.abs.gov.au/statistics/people/population/national-state-and-territory-population/latest-release. This has been extended to the September quarter using population estimates from ABS (2025) *Australian National Accounts: National Income, Expenditure and Product, September 2025*, https://www.abs.gov.au/statistics/economy/national-accounts/australian-national-accounts-national-income-expenditure-and-product/latest-release

[9] ABS (2025) *Total Value of Dwellings, September 2025*, https://www.abs.gov.au/statistics/economy/price-indexes-and-inflation/total-value-dwellings/latest-release

While quarterly data on the number of dwellings only goes back to September 2011, we do have very accurate data on the number of dwellings from the census. If we compare the 2001 census, which was the census closest to when house prices started to rapidly increase, with the most recent census in 2021, we can calculate how much the population has increased in relation to the increase in the number of dwellings.

Over the 20 years from 2001 to 2021 the population increased by 33% while the number of dwellings increased by 39%.[10] This again shows that the number of dwellings grew faster than the population. This makes it unlikely that the housing affordability crisis has been caused by a lack of housing supply and rapid population growth.

It is important to note that increasing the supply of housing will put downward pressure on the price of housing. Regardless of the actual cause of the crisis, additional supply can help to fix it. For this reason, all levels of government can work to encourage more supply.

But rapidly increasing supply will take time and resources. Housing takes time to build and requires significant resources including materials and labour. The more resources we dedicate to building housing, the less resources available to build other projects. Rapidly increasing the supply of housing is the slowest and most expensive solution to housing affordability.

THE IMPACT OF THE CGT DISCOUNT AND NEGATIVE GEARING ON HOUSE PRICES

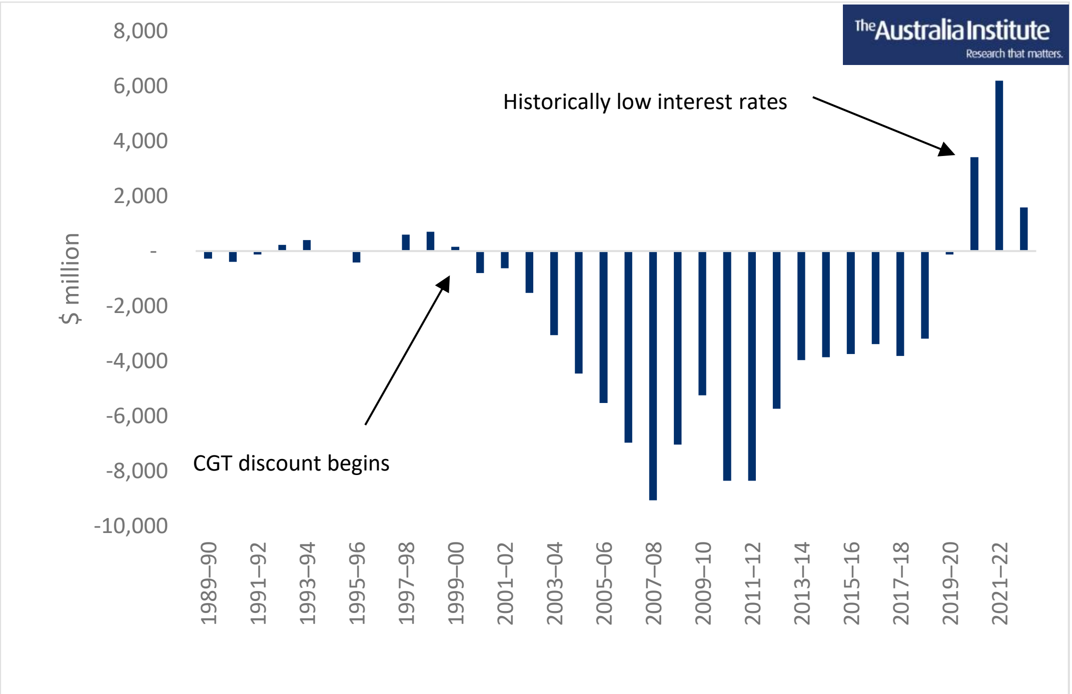
If it was not a lack of housing and a rapidly rising population, what was the cause of the housing affordability crisis?

The answer is the introduction of the CGT discount in September 1999. The effect can be seen in the net rental position, which is all rental income minus all rental costs. If it is positive, then on average people are making a profit on renting out their properties. If it is negative, known as negative gearing, then on average they are making a loss from renting out their properties.

Before the introduction of the CGT discount the net rental position was close to zero. Some years it was positive and some years it was negative. After the introduction of the CGT discount negative gearing increased rapidly. This is shown in Figure 6.

[10] ABS (2002) *Census of Population and Housing: Classification Counts, Australia, 2001*, https://www.abs.gov.au/ausstats/abs@.nsf/PrimaryMainFeatures/2022.0. ABS (2022) *Housing: Census*, https://www.abs.gov.au/statistics/people/housing/housing-census/2021#data-downloads. ABS (2022) *Population: Census*, https://www.abs.gov.au/statistics/people/population/population-census/2021

Figure 6: Net rental position



Source: ATO (2025) *Taxation statistics 2022-23, Individuals, Table 1*, https://www.ato.gov.au/about-ato/research-and-statistics/in-detail/taxation-statistics/taxation-statistics-2022-23/statistics/individuals-statistics

Negative gearing increased after the CGT discount because interest payments on investor mortgages are a cost. As house prices boomed, investor mortgages became larger and so did their interest bill. In recent years positive gearing has become more common because of the historically low interest rates during the pandemic. This is expected to disappear as interest rates started increasing in May 2022.

Negative gearing might seem to be a poor investment strategy. Being negatively geared means you are losing money on the investment. The loss reduces the owner's taxable income, but they only get part of the loss back. As an investment this only makes sense if they expect to make a large capital gain when they sell the property. This capital gain needs to be larger than the accumulated losses. Without the large capital gain the investment does not make sense.

This is why the CGT discount is so important. The CGT discount reduces the amount of tax paid on the capital gain, meaning investors keep more of it, making the investment more profitable. The lower the amount of capital gains tax, the larger the ongoing rental loss investors are willing to make and the higher the property price they are willing to pay. This also means that those who are negatively geared are betting on house prices continuing to rise. The more they are negatively geared, the more rapid the house price increase they are betting on. They are literally betting that housing will continue to get more unaffordable.

SCRAPPING THE CGT DISCOUNT WILL MAKE HOUSING MORE AFFORDABLE

The solution to the housing affordability crisis is to scrap the CGT discount, or at the very least restrict it to the purchases of newly produced assets such as newly built houses or apartments.

There are two strong examples that show that investor demand for housing has been pushing up house prices. They also show that reducing investor demand has slowed property price increases to less than the growth in income and therefore made housing more affordable. These examples include recent land tax changes in Victoria and changes to macroprudential regulations a decade ago.

VICTORIAN LAND TAX CHANGES

Land lax changes were announced in the May 2023 Victorian State budget and came into effect in January 2024. Land tax is not paid on people's principal place of residence (family home) but is paid on investment properties.[11]

The changes included:

- Reduced land tax thresholds for investment properties from $300,000 to $50,000.
- A fixed charge of $500 for landholdings between $50,000 and $100,000.
- A fixed charge of $975 for landholdings above $100,000.
- An increase in land tax rate of 0.1% for general taxpayers with holdings above $300,000 and trusts with landholdings above $250,000.

These changes were expected to raise an additional $4.7 billion in revenue over four years. They are temporary and are slated to end in June 2033.[12]

[11] State Revenue Office Victoria (n.d.) *Costs of buying and owning a property*, https://www.sro.vic.gov.au/buying-property/costs-buying-and-owning-property

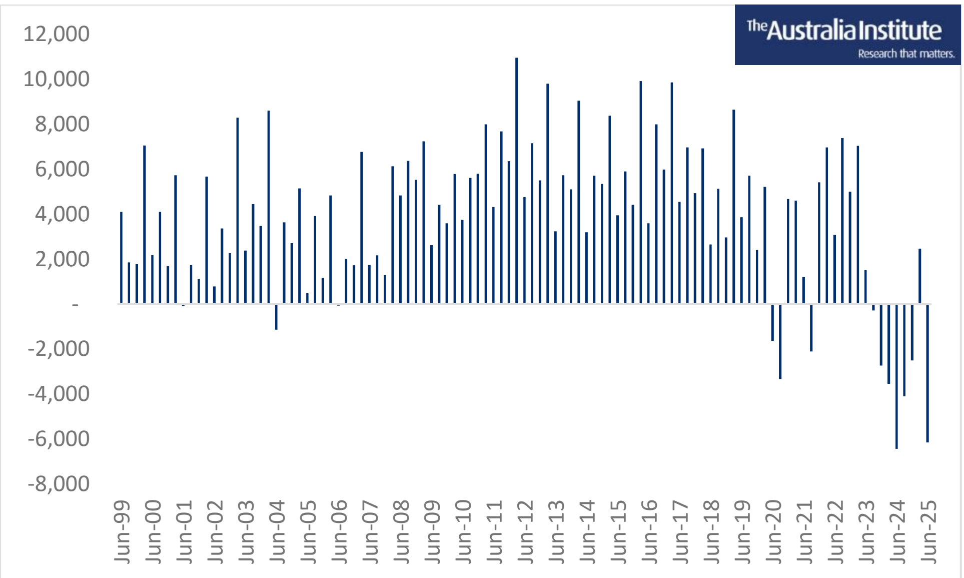
[12] Victorian Government (2023) *COVID Debt Repayment Plan*, https://s3.ap-southeast-2.amazonaws.com/budgetfiles202324.budget.vic.gov.au/2023-24+State+Budget+-+COVID+Debt+Repayment+Plan.pdf p19

It was estimated that an investor with an unimproved property[13] valued at $500,000 would pay an additional $1,175 in tax.[14] The change sparked warnings that large numbers of investors would sell their properties.[15]

Investors exited the market

It appears there was a behavioural response. If we use total active residential bonds[16] as a proxy for the number of investment properties, then there was a net sell off of properties by investors. The quarterly data shows a change after the announcement of the additional taxes in May 2023. The increase in the number of total active residential bonds was significantly lower in the June 2023 quarter, which is the quarter when the change was announced. This was followed by an unprecedented drop in the number of active bonds, as shown in Figure 7.

Figure 7: Quarterly change in total active residential bonds, Victoria



Source: Victoria State Government (2025) *Rental Report statistics - June quarter 2025*, https://www.dffh.vic.gov.au/publications/rental-report

The fall in the total number of active residential bonds is shown in Figure 8.

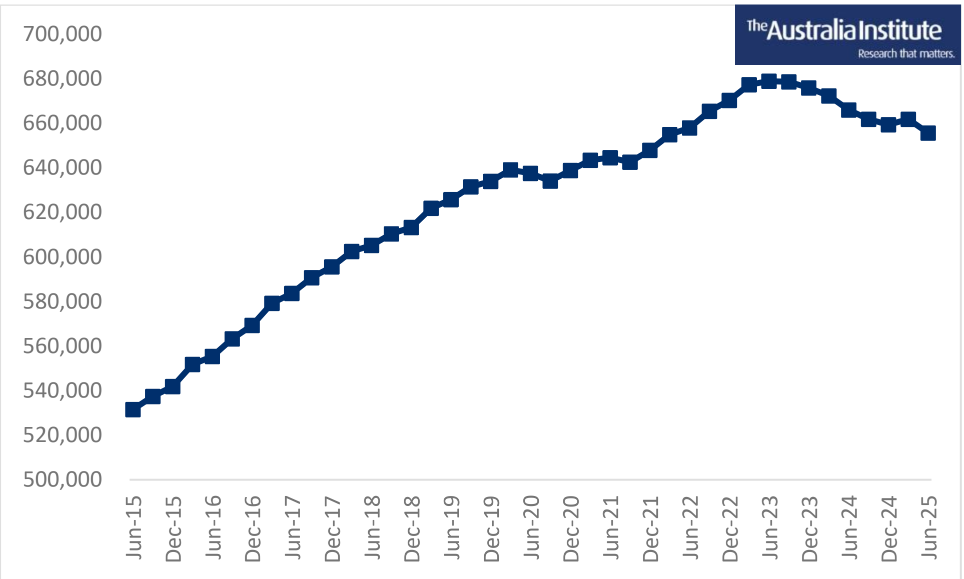
[13] The unimproved value is the value of just the land without the value of any buildings or structures.

[14] Ryan (2024) *How many Victorian investors have sold due to higher land taxes?*, https://www.realestate.com.au/insights/how-many-victorian-investors-have-sold-due-to-higher-land-taxes/

[15] Hughes (2023) *Property investors threaten to quit Victoria as housing taxes double*, https://www.afr.com/wealth/personal-finance/property-investors-threaten-to-quit-victoria-as-housing-taxes-double-20230620-p5di33

[16] These are the number of bonds held for residential properties. Bonds are security deposits paid by renters in case they breach the tenancy agreement.

Figure 8: Total number of active residential bonds, Victoria



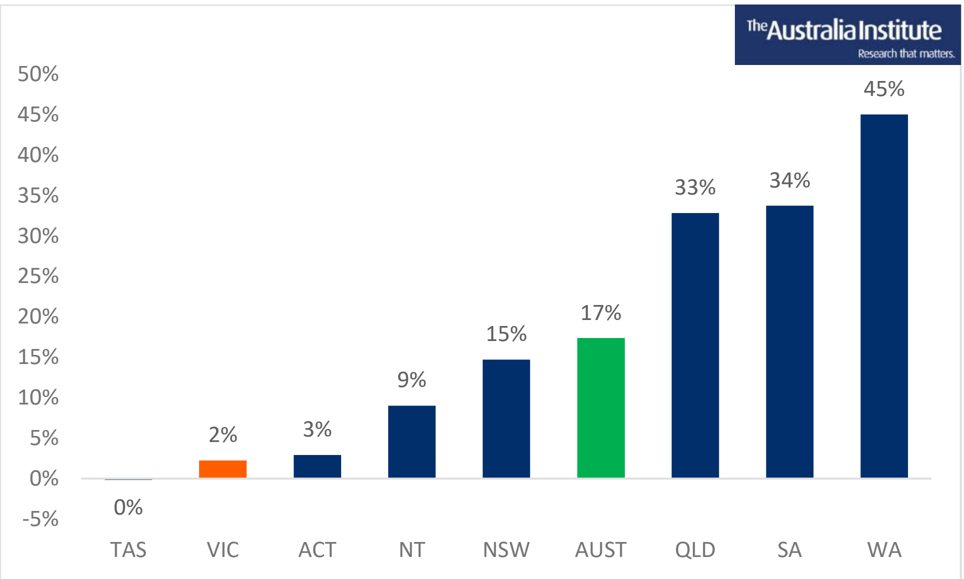
Source: Victoria State Government (2025) *Rental Report statistics - June quarter 2025*, https://www.dffh.vic.gov.au/publications/rental-report

Property investors getting out of the Victorian market couldn't take the houses with them; instead, they sold them. With investors leaving the market, they were selling to owner occupiers, particularly first home buyers.

Impact on residential property prices

From March 2023, the quarter before the announced changes to land tax, until September 2025, the most recent quarter of data, average residential dwelling prices increased only 2% in Victoria. This compares with 17% for average dwellings across Australia and as much as 45% in WA, as shown in Figure 9.

Figure 9: Increase in mean price of residential dwellings from March 2023 to September 2025



Source: ABS (2025) *Total Value of Dwellings, September 2025*, https://www.abs.gov.au/statistics/economy/price-indexes-and-inflation/total-value-dwellings/sep-quarter-2025

In March 2023, average residential dwelling prices in Victoria were the third highest, behind New South Wales and the Australian Capital Territory. By September 2025 they had fallen to be fifth highest, with Queensland and Western Australia now more expensive than Victoria. Only South Australia, Tasmania and the Northern Territory have lower average prices.

This slower rate of house price growth has allowed more first home buyers to purchase property in Victoria. Housing has become more affordable.

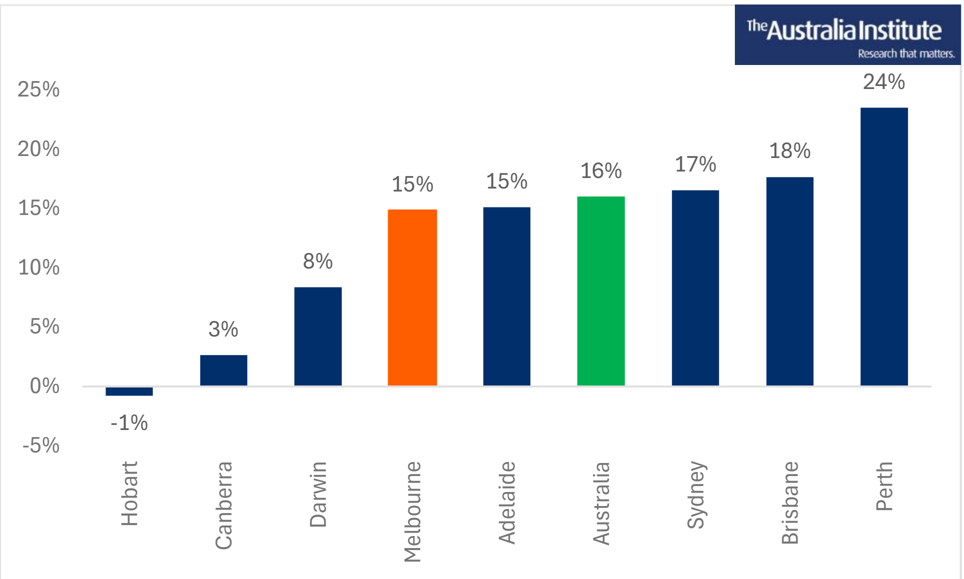
Impact on rents

When these tax changes were made, commentators claimed rents would increase.[17] They argued that by reducing the number property investors, there would be fewer rental properties, creating a shortage and pushing up rents. They also argued that property investors would pass on the increase in tax to tenants by increasing rents.

Neither of these seem to have occurred. From March 2023 to September 2025, rents increased by 15% in Melbourne. This was slightly less than the 16% increase for the average for all Australian capital cities and higher than only Hobart, Canberra, and Darwin, as shown in Figure 10.

[17] Waters (2023) *Tax slug for Victorians with investment properties or holiday homes*, https://www.theage.com.au/politics/victoria/tax-slug-for-victorians-with-investment-properties-or-holiday-homes-20230522-p5dadg.html

Figure 10: Increase in rents by capital city from March 2023 to September 2025



Source: ABS (2025) *Consumer Price Index, Australia, September Quarter 2025*, https://www.abs.gov.au/statistics/economy/price-indexes-and-inflation/consumer-price-index-australia/sep-quarter-2025

In order to understand why rents didn't increase, we need to consider what was happening to all the houses that investors were selling.

Traditionally, aspiring first home buyers rent before they buy. While they're renting, they save up a deposit. When they have a big enough deposit, they go to a bank, get a mortgage and buy a house. This means that a significant number of successful first home buyers go from being renters to being owner occupiers.

Imagine a scenario where a family has just saved up enough for a deposit and they're now ready to buy a house. At this moment their landlord decides to sell the house they're renting.

The family like the house and decide to buy it. After winning the auction, the rental market loses one rental property. That property stops being a rental and now houses an owner-occupier. But at exactly the same time, the number of people wanting a rental property decreases by one.

In this example the number of rental properties went down by one but the number of families renting also went down by one, which is not likely to have a large impact on rents. This appears to be exactly what has happened with rents increasing largely in line with the rest of the country.

Investors are also not likely to be able to pass on the increase in tax as an increase in rent because the rental price is determined by supply of rental properties and the demand for rental properties. Landlords can't simply increase rents just because taxes have increased.

Impact on building new housing

Commentators also argue that restricting investors will reduce the number of new properties getting built. Over time this would reduce the number of dwellings and make housing less affordable.

There is no reason to believe this would happen. The overwhelming majority of properties that are sold to investors are existing housing stock, not new builds. Over the last 12 months, 82% of new investor mortgages were for existing dwellings.[18]

Some newly built houses are sold to investors, and if this does create a problem, it can be easily fixed. The capital gains tax discount could be restricted to investors who buy new dwellings. This change would mean that any investor who was considering buying a newly constructed dwelling would not be put off by the change in the CGT discount. In fact, investors who wanted to continue to invest in residential housing would be encouraged to buy new dwellings, which could lead to an increase in demand for newly built dwellings.

MACROPRUDENTIAL REGULATIONS

There is another important example that shows how investor demand for housing is an important driver of high house prices: changes to macroprudential regulations.[19]

In 2014, the Australian Prudential Regulation Authority (APRA) determined that demand for investor loans — which were high by historic standards — posed a risk to the stability of the Australian financial system. They were concerned more risky forms of lending were increasing rapidly, and these loans were over-inflating the value of housing in Australia and creating a bubble.

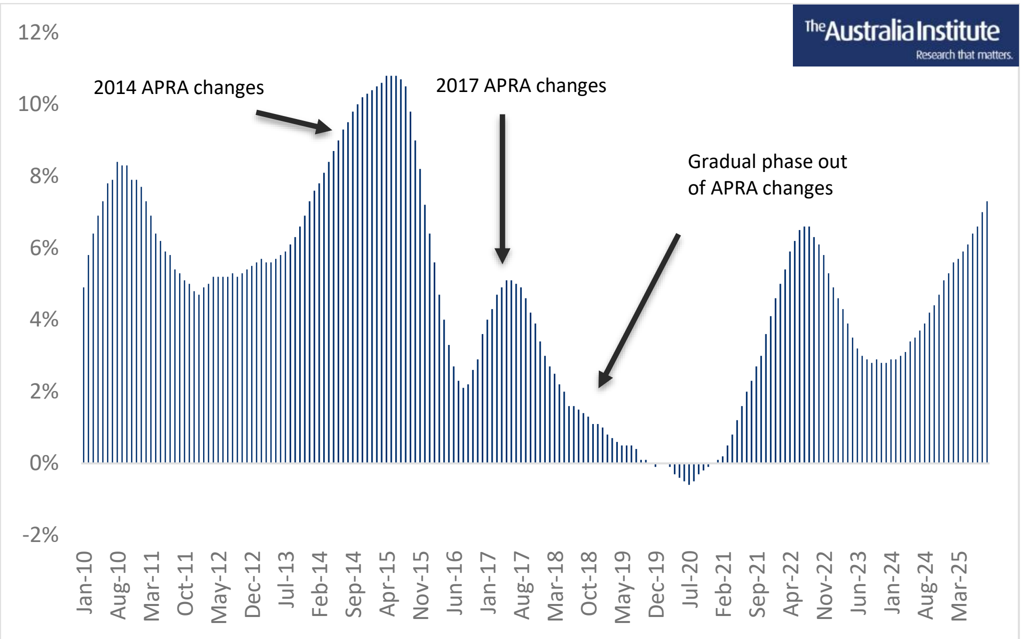
To deal with this risk, in December 2014 APRA announced regulations to restrict investor lending to 10% annual increases. They also required lenders to have a 2% buffer above the loan rate when calculating a borrower's capacity to repay the loan and increased supervisory intensity on higher risk forms of lending – this mostly impacted owner-occupiers who were taking out interest only loans.

Initially, these policies worked as intended. As shown in Figure 11, growth in investor loans fell after the 2014 changes. However, by the end of 2016, growth in investor loans bounced back. To counteract this, in April 2017 APRA introduced a stricter, 30% limit on the share of interest-only loans a lender could offer.

[18] ABS (2025) *Lending Indications, September 2025*, https://www.abs.gov.au/statistics/economy/finance/lending-indicators/sep-quarter-2025

[19] The following is a summary of Grudnoff (2025) *Macro reforms for housing affordability*, https://australiainstitute.org.au/report/macro-reforms-for-housing-affordability/

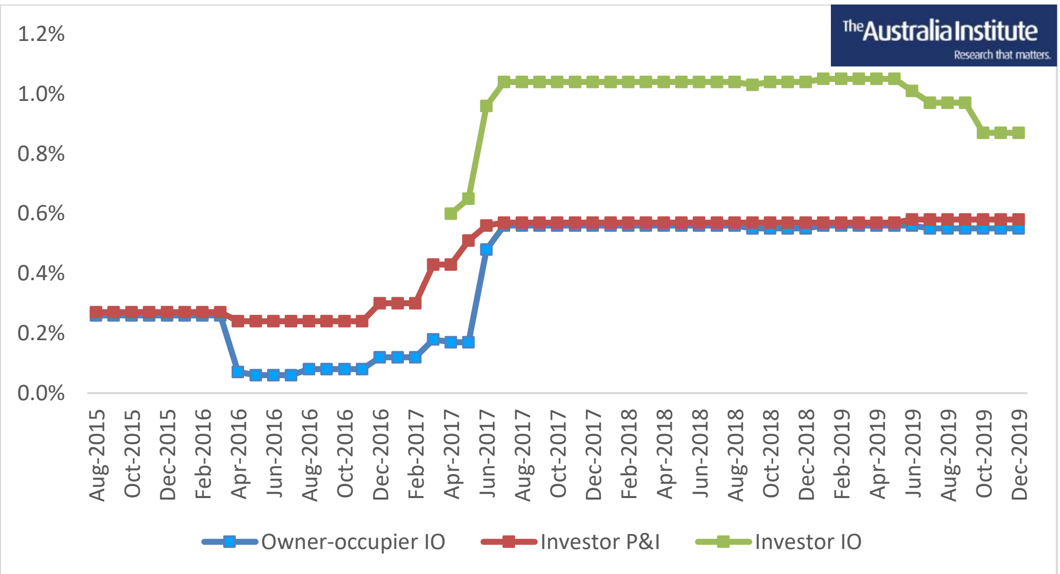
Figure 11: Annual investor housing credit growth



Source: Australian Bureau of Statistics (2024) *Lending indicators: December 2024, Table 13*, https://www.abs.gov.au/statistics/economy/finance/lending-indicators/latest-release

To meet this requirement, lenders increased the interest rates they charged on investor loans, which had the effect of reducing demand for this type of loan. This increased rates for both interest-only (IO) and principal and interest (P&I) investor loans. Lenders also increased interest rates on owner-occupier IO loans, which they considered to be a threat to their stability. Lenders charged an extra 50 basis points (0.5%) in interest on owner-occupier IO loans and investor P&I loans. They charged an extra 100 basis points (1%) on investor IO loans. This is shown in Figure 12.

Figure 12: Increase in interest rates compared to advertised owner-occupier P&I rate



Source: RBA (2025) *Indicator Lending rates*, https://www.rba.gov.au/statistics/tables/#interest-rates

The higher interest rates were effective at limiting investor loans. The growth in loans to investors fell over the two-year period from September 2017 to September 2019. This trend continued even after April 2018 when APRA began to phase out the changes because they no longer saw the number of investor loans as a threat to Australia's financial system.

Recently APRA has been concerned about the current growth in investor loans, which is now growing faster than at any point since 2015. In November 2025, APRA announced new macroprudential policy settings that no more than 20% of new lending can go to borrowers with debt-to-income ratios of greater than six times.[20] This is not expected to have a large impact as only about 7% of new lending is to borrowers with debt-to-income ratios of greater than six times.

The 2014 to 2018 macroprudential policy regulations had an important impact on house prices. In the three years from 2017 to 2019, house prices fell by 9% — this was the largest decrease since 1989. Governments have introduced many policies they claim are about making housing more affordable, but this change, made not to make housing more affordable but because the regulator was worried about financial stability, had the biggest impact. When investor demand fell housing became more affordable.

Both this example and tax changes in Victoria show that when there is a reduction in investor demand, housing becomes more affordable. The federal government has the largest policy lever that can discourage investor demand: the CGT discount.

Scrapping the CGT discount will reduce investment demand across the country. As investors exit the market, these properties will be bought by owner-occupiers including first home buyers. Housing will become more affordable and home ownership rates will rise. All this can be achieved without expending huge quantities of resources building new housing. It would also be achieved much faster.

[20] APRA (2025) *Activation of debt-to-income limits as a macroprudential policy tool*, https://www.apra.gov.au/activation-of-debt-to-income-limits-as-a-macroprudential-policy-tool

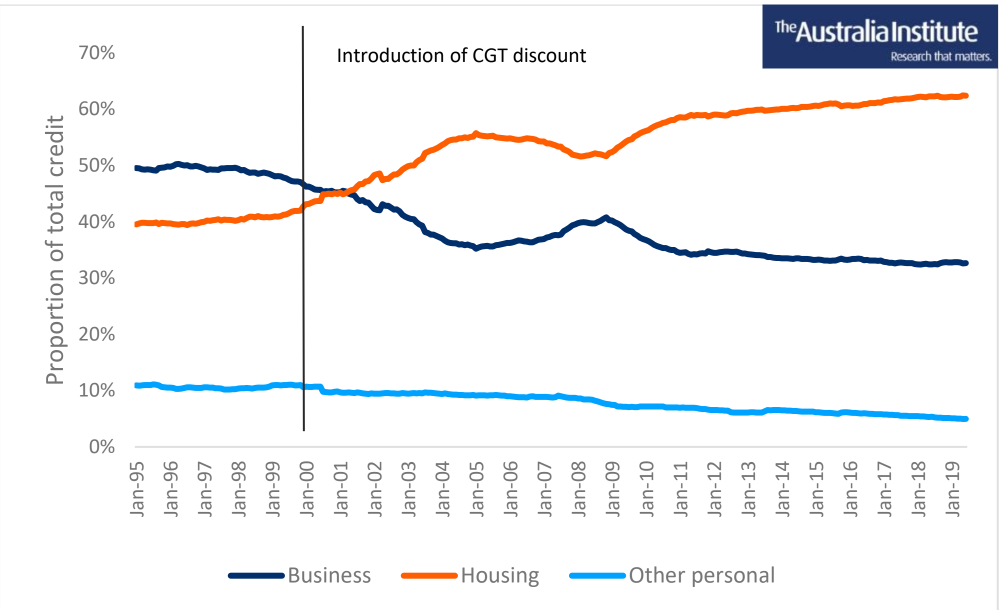
CGT discount is distorting the economy in negative ways

The CGT discount has also distorted the economy in other ways, including reducing business access to lending and changing how high-income earners structure their tax affairs.

MORTGAGES CROWDING OUT BUSINESS LENDING

Rapidly rising house prices has reshaped who banks lend money to. Before the introduction of the CGT discount, lending to business made up the largest proportion of credit. In September 1999 business lending made up 47% of all credit and lending for housing made up 42% of all credit. Today business lending makes up only 33% of credit, while housing makes up 62% of credit, as shown in Figure 13.

Figure 13: Proportion of lending going to business, housing, and other personal



Source: RBA (2025) *D2 Lending and Credit Aggregates*, https://www.rba.gov.au/statistics/frequency/fin-agg/2025/

As house prices have rapidly increased, housing debt has also increased. Banks have been keen to lend increasing amounts to mortgages for two important reasons.

The first is that mortgages are very profitable. The big four banks make $200,000 profit on average for a 30-year home loan for owner-occupiers.[21] Increasing that profitability is the

[21] Richardson (2024) *Profit in home lending*, https://australiainstitute.org.au/report/profit-in-home-lending/

larger loan sizes and the longer time it takes to pay them off. The second reason is that mortgages involve lower risk for the bank. They are secured against an asset that has been rapidly increasing in price over the last 25 years. If, for whatever reason, the borrower cannot continue to pay the mortgage, the house can be sold to recoup the outstanding balance of the loan. Banks also find it relatively easy to assess the credit worthiness of borrowers, which reduced the banks' risk due to a reduction in the chances of default.

By comparison, business loans come with higher risks. Businesses often don't have access to the same high-quality assets to use as collateral. Business loans are harder to assess for credit worthiness. There are larger information asymmetries as businesses can differ greatly from each other. Banks have been happy to fill the growing demand in the mortgage market and been lending less to businesses. But this has had consequences for the wider economy, including Australia's productivity.

Most businesses borrow when they invest and so the restrictions on their ability to borrow have made it harder for them to raise the revenue needed to invest. Figure 14 shows private business investment as a percentage of GDP since 1959. It shows that recent levels of investment are low by historic standards.

Figure 14: Total private business investment as a percentage of GDP, Sep 1959 to Jun 2025

Source: ABS (2025) *Australian National Accounts, June Quarter*, https://www.abs.gov.au/statistics/economy/national-accounts/australian-national-accounts-national-income-expenditure-and-product/jun-2025

Figure 15 below shows the same as Figure 14 above but zooms in to show private investment as a proportion of GDP since the introduction of the CGT discount. Investment initially increased during the mining boom but then collapsed to historically low levels for the last 10 years.

Figure 15: Total private business investment as a percentage of GDP

Source: ABS (2025) *Australian National Accounts, June Quarter*, https://www.abs.gov.au/statistics/economy/national-accounts/australian-national-accounts-national-income-expenditure-and-product/jun-2025

Low levels of investment are linked to low levels of productivity. A study from the Reserve Bank of Australia found that the slowdown in investment and productivity was worse in debt dependent sectors, suggesting debt markets are contributing to the problem.[22] Policies that slow the rise in house prices will, over time, reduce the size of the mortgage market and force banks to lend more to other areas including business.

DISTORTING HOW HIGH-INCOME EARNERS ARE STRUCTURING THEIR TAX AFFAIRS

There are many different forms of income. People can earn income from returns on investments, renting out an investment property, interest on bank accounts, as well as many other ways. But most people earn the majority of their income from wages.

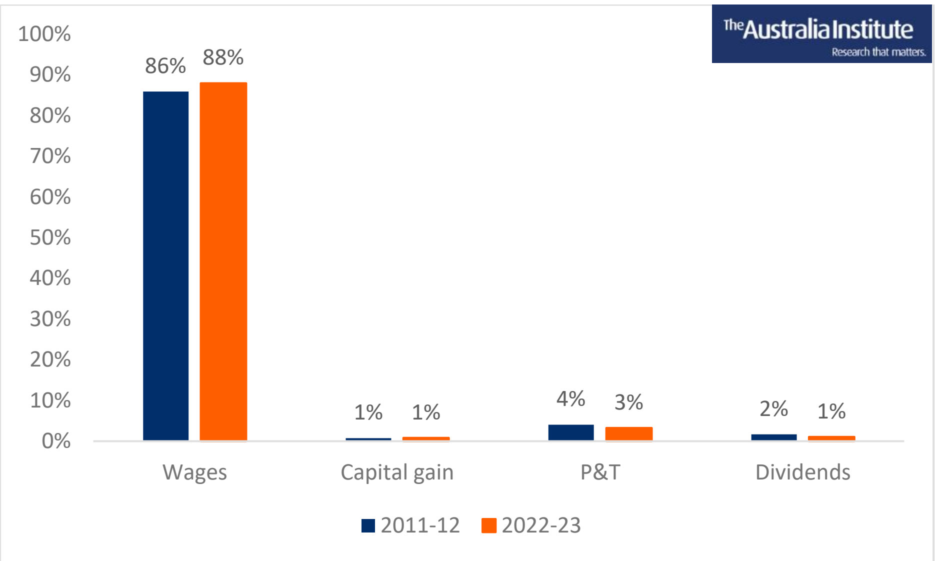
There are some exceptions; for example, the main sources of income for people who are retired is investment returns from things like their superannuation, and government benefit including the age pension.

Analysing the most recent taxation statistics for 2022-23, we can look at the sources of income for people who earn between $90,001 and $100,000. For this group, 88% of their gross income comes from wages. Figure 16 shows four sources of income for this group including wages, capital gains, income from partnerships and trusts, and income from

[22] Hambur & Andrews (2023) *Doing less, with less: Capital Misallocation, Investment and Productivity Slowdown in Australia*, https://www.rba.gov.au/publications/rdp/2023/pdf/rdp2023-03.pdf

dividends. This is not an exhaustive list and so all four of these forms of income don't add to 100%. It also shows how the proportion of these incomes have hardly changed between 2011-12 and 2022-23.

Figure 16: Proportion of selected forms of income to gross income for those earning between $90,001 and $100,000 for 2011-12 and 2022-23

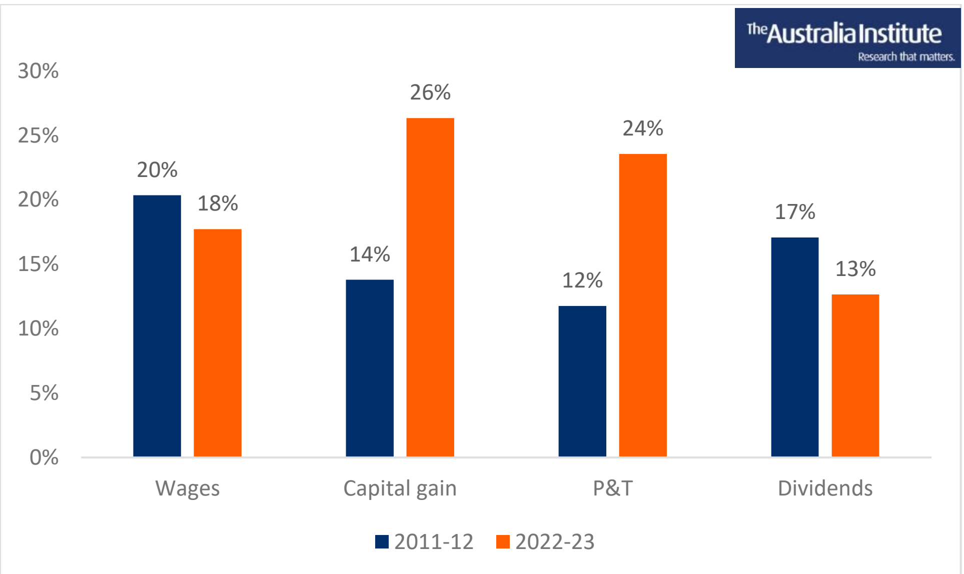


Source: ATO (2014) Taxation Statistics 2011-12 and ATO (2025) Taxation Statistics 2022-23

We can see that wages dominate their gross income over the 11-year period.

Doing the same analysis for very high-income earners reveals that they earn their income in different ways and that their earnings changed over the same 11-year period. Figure 17 below only includes those who have earned more than $1 million per year.

Figure 17: Proportion of selected forms of income to gross income for those earning more than $1 million for 2011-12 and 2022-23



Source: ATO (2014) Taxation Statistics 2011-12 and ATO (2025) Taxation Statistics 2022-23

People earning more than $1 million per year receive a much smaller proportion of their income from wages. Instead, capital gains and income from partnerships and trusts are far more important. It also shows that capital gains and partnerships and trusts have become more important over time.

Over the 11 years from 2011-12 to 2022-23, the proportion of income from partnerships and trusts has doubled and now account for almost a quarter of their gross income (24%). Income from capital gains has almost doubled and now accounts for just over a quarter of their gross income (26%). Together, these two forms of income now make up half of all their gross income. This is up from about a quarter of their income (26%), 11 years ago.

People on very high incomes have more flexibility on the sources of their income. Earning it as capital gains and from partnerships and trusts has important tax implications. Partnerships and trusts are regularly used to minimize tax, and the CGT discount means income from capital gains are discounted by 50%.

Conclusion

In 1970, the average dwelling price in Australia was equivalent to 7.9 years of average household disposable income. In 1999, 29 years later, this had risen to just 9.1 year. Now some 26 years since the introduction of the capital gain tax discount, the average dwelling price in Australia is equivalent to 16.7 years of the average household disposable income.

The increase is not coincidental. Prior to the introduction of the 50% CGT discount, housing in Australia was based around owner-occupiers and the desire for people to own their own home – the great Australian dream. The CGT discount turned the housing market into a casino – but one where the existing players had the odds stacked in their favour. Negative gearing, which had previously been no more likely to occur than positive gearing, became common tax accountant advice, because the CGT discount lowered the threshold required to recover lost income and profit from property investment.

Soon after the introduction of the discount, banks began advertising to people, telling them to make use of the equity in their home to buy investment properties, and unsurprisingly house prices took off and housing affordability fell.

After 25 years of evidence, we can now draw conclusions about the CGT discount – it has failed to deliver more housing stock and failed to reduce either house prices or rents. Policy makers who attempt to address the housing affordability crisis in this country by continuing a policy that has been in place during the precise period the crisis has occurred are very much attempting to do the same thing over again and expecting a different result.

This submission has demonstrated that the 50% CGT discount introduced a distortion to the tax system that favours the wealthy and increases inequality. This incentive for housing investors has allowed them to outbid prospective owner-occupiers and placed home ownership outside the reach of many.

For the first time since WWII a majority of Australian in their early 30s do not own a home. This paper demonstrates that the first step to repair this situation is to undo the damage introduced in 1999 with the capital gains tax discount.

We recommend scrapping the capital gains tax discount.