

Article Information

Authors: Megan Bishop, Luke Higgins, Gideon Stein

Service: Taxation

2026 Budget - What businesses and investors should know

The 2026-2027 Federal Budget delivers a broad tax reform package the Government aptly describes as the most significant transformation of Australia's tax system in more than 25 years.

Key announced measures include major reforms to capital gains tax and negative gearing (from 1 July 2027), as well as a proposed 30% minimum tax on discretionary trusts (from 1 July 2028). Treasury links these reforms to housing affordability and intergenerational pressures. Housing prices are reported to have risen 407% between April 1999 and April 2026, with median prices increasing from four times to eight times average full-time earnings. Home ownership is also said to have fallen (including sharp declines among younger cohorts), while demographic ageing is expected to concentrate reliance on personal income tax over time.

New measures also include a redesign of tax concessions to promote innovation in Australia designed around encouraging more risk taking, a two year loss carry back of losses for companies with turnover of under \$1 bn (from 1 July 2026), refundable tax offsets for employment related expenses for companies in their first two years (from 1 July 2027) and a redesign of the R&D tax incentive measures (from 1 July 2028).

This article will discuss some of the 'big-ticket' items of the proposed tax reform package and the practical implications of those changes. We anticipate that there will be greater compliance obligations arising out of these developments, at least in the interim, not least on the announcement of the Treasurer Jim Chalmers, committing to expanding the ATO's workforce by another 1,500 staff.

As an important note, the measures discussed in the Budget (and this article) are proposed reforms only. They will require legislation and the final design may differ from the Budget description. Historically, some announced Budget measures have never seen the light of day.

Capital gains tax

Say goodbye to the 50% discount

From 1 July 2027, the 50% capital gains tax (**CGT**) discount is intended to be replaced with cost base indexation for CGT assets held by individuals, trusts and partnerships, returning to a model that taxes 'real' gains (i.e., gains after adjustment for inflation). Treasury's stated rationale is that a flat 50% discount is a blunt proxy for inflation, which can overcompensate some assets and holding periods and undercompensate others.

This proposed reform has been on many wish reformists lists for a while. The 50% discount has always been a policy compromise in the sense that it is simple to administer but economically rough around the edges. In practice, it has become a structural feature of how Australians hold wealth (particularly property and shares) and how advisors structure ownership. Whilst the policy direction is not surprising, the decision to finally pull the trigger on this (noting of course, the proposed reforms may never see the light of day) is still significant.

Early commentary has been quick to criticise these changes; however, whilst that sort of doomsaying makes for good headlines, it oversimplifies what is actually being proposed. In fact, in a highly inflationary economic environment (and recent years have certainly reminded everyone that inflation can return quickly), indexation can produce outcomes that are better than many people assume and better than the flat 50% discount which applied the same haircut regardless of whether inflation was low or high. That is because the indexation method lifts the cost base to reflect inflation, so the taxable gain is the 'real' increase in value.

By way of a simple example, assume you are a top marginal tax rate individual and you buy an asset for \$100 and sell it years later for \$160 (a \$60 nominal gain). If inflation over that period was high enough that the indexed cost base becomes \$140:

- Under the 'traditional' flat 50% discount, the taxable gain is $\$60 \times 0.5 = \30 .
- Under the indexation method, the taxable gain is $\$160 - \$140 = \$20$.

On those assumptions, indexation is actually more favourable. In economic conditions where inflation is doing a lot of the work in terms of asset value appreciation, indexation will be more favourable for asset holders. Of course, the actual mechanism by which indexation will work is yet to be decided upon and the above example is for illustrative purposes only.

Transitional arrangements and end to pre-CGT assets

The Budget sets out transitional arrangements. For assets acquired before 1 July 2027 but sold after that date, the 50% discount applies to the gain accrued *up to* 1 July 2027 (broadly, the value at 1 July 2027 less historical cost base). For gains accruing *from* 1 July 2027, the asset's 1 July 2027 value becomes the new cost base, and indexation (and the minimum tax discussed below) applies to post-commencement gains. Taxpayers can determine the 1 July 2027 value either via a valuation or a specified apportionment formula based on average returns over the holding period, which is to be supported by tools from the ATO.

Importantly, the same approach will apply to pre-20 September 1985 assets: gains earned before 1 July 2027 preserve existing treatment, but post-1 July 2027 gains will be taxed on realisation under the new arrangements. The Budget also states the small business CGT concessions will otherwise continue unchanged.

30% minimum tax on real capital gains

From 1 July 2027, a 30% minimum tax will apply to real capital gains, intended to reduce incentives to 'time' disposals into low-income years (for example, between jobs). Income support recipients, including pensioners, are stated to be exempt from this. In practical terms, taxpayers already at or above a 30% marginal rate on non-capital gains income will not be affected by this (except to the extent the 50% CGT discount will no longer be available).

Practical takeaways

1. those with significant unrealised gains should plan early for the 1 July 2027 valuation process (especially for private assets);
2. record-keeping will become harder and advisors will need systems and methods to track pre- and post-commencement gain components and support any ATO approved formula or other valuation methodology used; and
3. saying goodbye to the 50% CGT discount does not necessarily mean everyone is worse off.

Trust changes

The Budget proposes a 30% minimum tax on the taxable income of discretionary trusts, effective from 1 July 2028. The stated policy aim is to better align the tax paid on trust income with the tax paid by workers and to reduce incentives for income splitting and complex structuring. The Australian Government's 'fairness' narrative is reinforced by the scale of the trust system, with the Budget referencing the 1+ million trusts currently in existence in Australia, including approximately 840,000 discretionary trusts, with discretionary trusts distributing over \$140 billion in the 2022-2023 income year.

The intended operation of this change is that the trustee will pay the minimum 30% tax (on the basis the trustee controls the distributions). Beneficiaries will still include distributions in their returns, but non-company beneficiaries receive non-refundable credits for the tax paid by the trustee, which can offset their current year income tax liabilities. If a beneficiary's marginal tax rate is above 30%, they effectively will pay top-up tax. If it is below 30%, the excess credit is wasted.

Unfortunately one of the things that is ambiguous and unclear in the budget is how the 30% rate will apply to companies. The Budget papers appear to indicate that the trustee will be required to pay the 30% tax but that companies will get no credit at all for it – potentially meaning a tax rate of 55%-60% for company distributions. It is anticipated this measure will see a lot of debate and may alter before implementation.

Importantly, the minimum 30% tax will not apply to primary production income of farms, certain income relating to vulnerable minors, amounts subject to non-resident withholding tax, and income from assets of testamentary trusts existing at budget night. Other excluded vehicles include fixed and widely held trusts, complying super funds, special disability trusts, deceased estates and charitable trusts.

The Budget also flags expanded rollover relief for three years from 1 July 2027 to facilitate restructuring from discretionary trusts into companies or fixed trusts. What that will look like remains to be announced so stay tuned for that.

Negative gearing

Restricted to new builds for residential property

From 1 July 2027, negative gearing for residential property will be limited to new builds. Net rental losses from established residential properties will only be deductible against rental income or capital gains from residential property. Excess losses can be carried forward to future years but can no longer be offset against unrelated income such as wages.

Properties purchased or held prior to Budget night (7:30pm AEST on 12 May 2026) are exempt from the changes until disposed of, including where a contract has been entered into but not yet settled. Properties purchased after that date but before 30 June 2027 may be negatively geared during that interim period but not in subsequent years.

Importantly, the restriction applies only to residential property. Commercial property and other asset classes (including shares) remain subject to existing negative gearing arrangements. The budget paper does not address whether a company holding established residential investment property would be caught by the quarantining rules. The CGT reforms are expressed as applying to assets held by “individuals, trusts and partnerships,” and the negative gearing changes are framed around “residential property” without specifying the entity type. This is a gap that will need to be resolved in the implementing legislation and is likely to generate significant interest from investors who hold (or are considering holding) residential property through corporate structures.

Treasury modelling suggests the reforms will result in housing prices temporarily growing by around 2% less over a couple of years relative to no policy change, with an expected rent increase of less than \$2 per week for a household paying the current median rent. The changes are expected to result in around 75,000 additional owner-occupiers over the next decade.

Startups, venture capital and small businesses

Backing businesses that take risks

The Budget includes over \$3.5 billion of new measures directed at businesses, with a stated objective of reducing the tax system’s bias against risky investments, which Treasury says could increase both the quantity and quality of investment, with positive flow-on effects for productivity, real wages and employment.

A centrepiece of the business package is the reintroduction of a permanent 2-year loss carry back for all companies with up to \$1 billion in turnover, taking effect for income years after 1 July 2026. Under current settings, companies are taxed on profits immediately but do not receive a tax benefit from losses unless and until they return to profitability, by which time the real value of the loss has declined. This asymmetry disproportionately affects start-ups and firms seeking to expand or pivot, while giving large, established firms with existing profits a competitive advantage in absorbing losses from risk-taking. Loss carry back allows companies to generate a refund of tax paid in prior years when a loss is incurred, providing timely cash flow support. The measure is expected to directly benefit up to 85,000 companies each year and is estimated to cost \$2.3 billion over five years from 2025-2026. During the pandemic-era temporary loss carry back, over 70,000 companies accessed the measure, receiving an average cash flow boost of around \$50,000 per business.

From 1 July 2028, the Government will also introduce loss refundability for small start-up companies in their first two years, capped at the amount of employment-related taxes paid (being withholding tax on employee wages and FBT). A critical issue when it comes to implementation for this one will be around the extent to which it might apply to the gig economy, or those industries heavily reliant on a contractor model.

The \$20,000 instant asset write-off will be made permanent from 1 July 2026 for businesses with turnover up to \$10 million. The threshold has effectively been in place since 1 July 2023 but has only ever been extended on a temporary basis. Making the IAWO permanent is estimated to decrease receipts by \$890 million over the forward estimates and save small businesses around \$32 million per year in compliance costs.

On venture capital, the Government will modernise the tax incentive caps for venture capital limited partnerships and early-stage venture capital limited partnerships from 1 July 2027, uplifting them to compensate for inflation since most were last set in 2002 and 2007 respectively. These changes are intended to expand access to venture capital, support later-stage investment and reduce pressure for early divestment as businesses scale.

R&D

A sharper focus on core R&D

The Budget proposes to retarget the Research and Development Tax Incentive (**R&DTI**) by increasing offset rates for core R&D activities while removing supporting activities entirely. One challenge for claimants here is that R&D does not always happen in a singularly or strictly defined process. Supporting activities account for a material proportion of claims. And core R&D activities (at least as currently defined) cannot occur in isolation. In practice, this will require many businesses to fundamentally reassess how their R&D activities are identified, documented and substantiated, with a sharper focus on clearly defined experimental work.

All offset rates are proposed to increase by 4.5 percentage points. For eligible SMEs with turnover below the new \$50 million threshold, the offset rate rises from 43.5% (i.e. 25% company tax rate plus 18.5%) to 48% (i.e. 25% plus 23%). For larger companies, the base non-refundable offset increases from 8.5% above the company tax rate to 13%, with the higher intensity-based offset moving from 16.5% to 21%.

The turnover threshold for the higher-rate SME offset will increase from \$20 million to \$50 million, broadening access for mid-sized firms. For younger SMEs (those operating for less than 10 years), the offset will be refundable at the new 23% rate, while older SMEs will receive the same rate on a non-refundable basis. The loss of refundability for established SMEs is a significant change. Established loss-making companies that have historically relied on R&D cash refunds will need to reassess how their R&D funding is structured going forward.

The minimum R&D expenditure threshold increases from \$20,000 to \$50,000 (with smaller-scale research still eligible if undertaken with a registered Research Service Provider or Cooperative Research Centre), and the maximum expenditure cap for the non-refundable offset rises from \$150 million to \$200 million. The intensity threshold for larger companies to access the higher offset rate is reduced from 2% to 1.5%, which may provide some additional support to larger businesses engaged in substantial core R&D.

The practical outcomes of these reforms will vary across different categories of claimants. Some industries will be harder hit by the exclusion of supporting R&D activities, especially those that require high upfront capital investment or complex prototypes to run experiments. The mining and IT sectors as an example. Others that can outsource for those requirements, especially younger companies that remain eligible for the refundable R&D tax offset, are likely to benefit most from the higher refundable offset rates. Established SMEs and businesses with significant supporting activity claims may see reduced claim values and, in some cases, a material reduction in cash flow support.

These measures are not an expansion. They are intended to deliver \$650 million in savings for the Government over five years. Businesses should also be aware that the Budget signals ongoing scrutiny of R&D claims, placing even greater emphasis on concurrent documentation, technical substantiation and clear identification of core experimental activities.

Individuals

More in the pocket for workers

From 1 July 2027, the Government will introduce a \$250 Working Australians Tax Offset (**WATO**), available to more than 13 million workers. The WATO is directed exclusively to income earned from work (not asset income) and increases the effective tax-free threshold by \$1,785 to \$19,985 (or \$24,985 for workers also receiving the Low Income Tax Offset). This represents the largest permanent increase to the effective tax-free threshold since 2012-2013.

From the 2026-2027 income year, workers will also be able to claim a \$1,000 instant tax deduction for work-related expenses instead of itemising and substantiating individual claims. Workers who incur more than \$1,000 in work-related expenses can still claim in the usual way, and other deductions (such as charitable donations) remain claimable on top. Treasury estimates 6.2 million workers (42% of taxpayers) will benefit, with an average tax saving of \$205 and collective compliance cost savings of \$380 million per year.

These measures supplement previously announced tax cuts that lower the bottom marginal tax rate from 16% to 14% over the next two income years. An Australian worker on average earnings (\$81,245) will receive a combined tax cut of \$1,978 in 2026-2027 and \$2,496 per year from 2027-2028, compared to 2023-2024.

The Government will also increase Medicare levy low-income thresholds by 2.9% for singles, families, and seniors and pensioners from 1 July 2025, amounting to 1 million lower-income Australians continuing to be exempt from or pay a reduced Medicare levy.

Other notable changes

Electric Car Discount recalibrated

The fringe benefits tax exemption for electric vehicles is being wound back as the EV market matures. From 1 April 2027, the full FBT exemption will be replaced with a 25% discount applied to the 20% statutory formula rate for electric cars valued up to the fuel-efficient threshold for the luxury car tax. The full FBT exemption will continue to apply to electric cars valued up to \$75,000 during a transitional period from 1 April 2027 to 31 March 2029.

Simpler PAYG instalments

From 1 July 2027, businesses will have the option to report and pay PAYG instalments monthly, and small and medium businesses will be able to opt in to a dynamic instalment calculation embedded in their accounting software. The ATO will implement an administrative safe harbour so that businesses using the ATO-approved calculation can vary their instalments without risk of interest charges. These changes are expected to save businesses approximately 10,000 hours annually.

Looking ahead

The reforms outlined above remain subject to consultation and legislative implementation, and the detail will matter enormously. We will continue to monitor developments closely and will provide updates as draft legislation and further guidance emerge. In the meantime, please reach out if you would like to discuss how any of these changes may impact you or your business.

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