



Australian Government  
Australian Taxation Office

# Capital gains tax on sale of rental properties



When you sell or dispose of a rental property you may make a capital gain or loss. This will depend on when you acquired the property.

## If you bought property before 20 September 1985

You are exempt from capital gains tax (CGT). CGT came into effect from 20 September 1985.

However, an addition or improvement, such as renovating a house, is a [major capital improvement](#) and treated as a separate CGT asset if its original cost is both:

- **more than** 5% of the amount you receive when you dispose of the asset
- **more than** the improvement threshold for the income year in which you dispose of the asset.

[Calculate the capital gain or loss](#) by comparing the cost base of the improvements to the proceeds of sale that are reasonably attributable to the improvements.

## If you bought the property on or after 20 September 1985

You may make a capital gain or capital loss when you dispose of a rental property.

If the capital proceeds (sale price) are **more than** the cost base, the difference is a capital gain. If they are **less than** the cost base, you need to calculate the reduced cost base.

If the reduced cost base is **more than** the capital proceeds, the difference is a capital loss. If it is **less than** the capital proceeds, there isn't a capital gain nor a capital loss.

## Working out cost base or reduced cost base

The cost base is usually the cost of the property when you bought it, plus any costs associated with acquiring, holding and selling it. The cost base is made up of [5 elements](#)

### Element 1 – Money paid or property given for CGT asset

This includes the total money paid (or required to be paid) for the rental property and the market value of property given (or required to be given) to acquire the asset. For example, the purchase price to acquire the asset.

### Element 2 – Incidental costs of acquiring, selling or disposing of the asset

For example, stamp duty, legal fees, valuation fees.

These costs are **not included** if you:

- claimed a tax deduction for them in any year, or
- can claim a tax deduction for them because the period for amending the relevant income tax assessment has not expired.

### Element 3 (cost base) – Costs of owning the CGT asset

For example, insurance costs, rates and land taxes.

Balancing adjustment amount.

These costs are **not included** if you:

- can claim a tax deduction for them in any income year

- can claim a tax deduction for them because the period for amending the relevant income tax assessment has not expired
- acquired the asset before 21 August 1991.

### Element 4 – Capital costs to increase or preserve the value of your asset or to install or move it

For example, costs for building a new pergola.

### Element 5 – Capital costs of preserving or defending your title or rights to your CGT asset

For example, legal fees to defend your ownership of the rental property.

These costs are **not included** if you:

- acquired the asset after 31 May 1997, and
- can claim a tax deduction for them in any income year, or
- can claim a tax deduction for them because the period for amending the relevant income tax assessment has not expired.

How to calculate a reduced cost base:

1. Include all elements of the cost base except the third element, which changes to be the balancing adjustment amount – for example, the sale of depreciating assets in the rental property would be part of the balancing adjustment.
2. Don't apply indexation to any elements of the reduced cost base.

## Capital works deductions

You need to subtract any capital works deductions if you acquired the rental property after 13 May 1997 and you either:

- claimed a deduction for them in any income year
- have not yet claimed a deduction because the period for amending the relevant income tax assessment has not expired.

## Depreciating assets

A depreciating asset is considered a separate asset from the property for CGT purposes. When calculating your capital gain or loss, the value of a property's depreciating assets at the time of

purchase and at sale are removed from the cost base and capital proceeds.

## Working out your capital gain

There are 3 methods for working out your capital gain. If eligible for more than one of the calculation methods, you can choose the method that gives you the best result – that is, the smallest capital gain.

These are:

1. **Discount method** – reduce your capital gain by 50% for resident individuals where the asset was **held for 12 months or more** before the CGT event.
2. **Indexation method** – increase the cost base by applying an indexation factor based on the consumer price index (CPI). This method is only available for assets purchased **before 11.45am** (legal time in the Australian Capital Territory) on 21 September 1999 and held for 12 months or more **before** the relevant CGT event.
3. **The 'other' method** – subtract the cost base from the capital proceeds if the asset was owned for **less than 12 months**. In this case, the indexation and discount methods do not apply.

## Timing of a CGT event

The timing of a CGT event tells you which income year to report your capital gain or loss and may affect how you calculate your tax liability. The date of the CGT event for your property is the date you enter a contract for the sale or disposal, **not** the settlement date. If there is no contract, the CGT event takes place when the change of ownership occurs.

## Inherited property

If you inherit property, there are special rules for calculating your [Cost base of inherited assets](#)

## Apportioning gain or loss

If you are a co-owner of an investment property, any capital gain or loss is apportioned to your share of the ownership interest in the property.

### Main residence

#### If your rental property was your main residence

Generally, your main residence is exempt from CGT. A property stops being your main residence once you stop living in it. However, you can choose to continue treating it as your main residence for CGT purposes even though you no longer live in it:

- for up to 6 years if it is used to produce income (the 6 year rule)
- indefinitely, if it is not used to produce income.

You can't treat any other property as your main residence for the same period (except for a limited time if you're moving to a new house – up to 6 months).

You make the choice to treat a property as your main residence when you prepare your tax return for the income year you enter a contract to sell the property.

If you use your former home to produce income for more than 6 years in one absence, it's subject to CGT for the period after the 6 year limit.

#### If your property is your main residence and you use part of it to produce income

If you rent out part of your home or run a business from home, you do not get the full main residence exemption from capital gains tax (CGT). You aren't entitled to the full main residence exemption when you:

- acquire the property on or after 20 September 1985 and used it as your main residence, and
- would be allowed a deduction for interest (had you incurred it) on money borrowed to acquire the property (interest deductibility test).

#### Value of home when first used to produce income rule

To work out your capital gain, you need to know the market value of your property at the time you first used it to produce income if **all** of the following apply:

- you acquired the property on or after 20 September 1985
- you first used the property to produce income

after 20 August 1996

- when a CGT event happens to the property, you would get a partial exemption as you used the property to produce assessable income during the period you owned it (and the 6 year rule doesn't apply).
- you would have been entitled to a full exemption if the CGT event happened to the property immediately before you first used it to produce income.

Use our [Capital gains tax property exemption tool](#) to calculate the percentage of your exemption.

**Note:** Remember if you have used your property to earn income and are eligible for a CGT exemption or rollover, including the main residence exemption, you need to make the election in your tax return.

### Record keeping

You must keep records relating to your ownership and all the costs of acquiring, holding and disposing of property such as, contract of purchase and sale, stamp duty and major renovations.

Records are generally required to be held for at least 5 years after the sale of the property (or year you declare a capital gain). If you make a capital loss, once you've offset the loss against a capital gain, keep your records for a further 2 years.

For more information on record keeping, refer to [Tax-smart tips for your investment property](#).

### Foreign resident

There are special CGT rules if you're a foreign resident for tax purposes. These rules come into effect when you sell residential property in Australia.

**Example: sale of a rental property**

Brett purchased a residential rental property on 1 July 1998, for \$350,000 of this \$12,000 was attributed to depreciating assets. He also paid \$20,000 for pest and building inspections, stamp duty and solicitor's fees.

For the next few years, Brett incurred the following expenses on the property:

Interest on money borrowed	\$10,000
Rates and land tax	\$8,000
Deductible (non-capital) repairs	\$15,000
<b>Total</b>	<b>\$33,000</b>

Brett can't include the expenses of \$33,000 in the cost base, as he claimed a deduction for them.

When Brett decided to sell the property, a real estate agent advised him that if he spent around \$30,000 on renovations, the property would be valued at around \$600,000. The renovations were completed on 1 October 2019 costing \$30,000, while the property was still rented.

On 1 February 2020, he sold the property for \$600,000 (of which \$4,000 was attributed to depreciating assets).

Brett claims a capital works deduction of **\$254** ( $\$30,000 \times 2.5\% \times 124 \div 366$ ) for the renovations.

Brett works out his cost base as follows:

• Purchase price of property (less depreciating asset \$12,000)	\$338,000
<i>plus</i>	
• Pest and building inspections, stamp duty and solicitor's fees on purchase of the property	\$20,000
• Capital expenditure (renovations) \$30,000 less capital works deduction \$254	\$29,746
• Real estate agent's fees and solicitor's fees on sale of the property	\$12,500
<b>Cost base unindexed</b>	<b>\$400,246</b>

Brett deducts his cost base from his capital proceeds (sale price):

• Proceeds from selling the house (less depreciating assets \$4,000)	\$596,000
<i>less</i>	
• Cost base unindexed	\$400,246
<b>Capital gain</b>	<b>\$195,754</b>

He decides the discount method gives him the best result, so he uses it to calculate his capital gain:

$$\$195,754 \times 50\% = \$97,877$$

Brett must also make balancing adjustment calculations for his depreciating assets. Because he used the property **100%** for taxable purposes, he won't make a capital gain or capital loss from the depreciating assets.

### Example: main residence for part of the ownership period

Vrinda bought a house on 1 July 2005 for \$350,000 and moved in immediately. On 1 July 2015, she moved to a new house (that she treated as her main residence) and began to rent out her old house. She had a valuation done at the time for \$500,000 for her old house.

She sold the old house (rental property) for \$650,000. Its contract for sale was signed on 1 July 2018. Vrinda acquired the old house on 1 July 2015 and uses its market value of \$500,000 (value at the time of first use for producing income) as the first element of her cost base.

Vrinda also has incidental costs for \$15,000 for acquiring/selling the property. Vrinda makes a capital gain of \$135,000. Since she owned her old house for at least 12 months, she chooses to use the discount method to calculate her net capital gain of \$67,500.

**Note:** The 3rd and 4th elements costs are not included in this example.

### Example: renting out part of a home

Thomas purchased a house 1 July 1999 and sold it on 30 June 2020. The house was his main residence for the entire time.

Throughout the period Thomas owned the home, a tenant rented one bedroom (20% of the home). Both Thomas and the tenant used the living room, bathroom, laundry and kitchen (30% of the home). Thomas used the rest of the home.

Thomas is entitled to a 35% (20% + half of 30%) deduction for interest on money borrowed to acquire his home.

Thomas made a capital gain of \$120,000 when he sold the home. Of this total gain, the following proportion is not exempt:

Capital gain x percentage of floor area  
= taxable portion

$$\text{\$120,000} \times 35\% = \text{\$42,000}$$

Thomas can use either the indexation or the discount method to calculate his capital gain.

As this is a complex topic, it may not meet your individual circumstances.

If you are uncertain, you should get appropriate professional advice relevant to your circumstances.



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