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## Section 41: separated spouses and civil partners

### Background

Until the Finance (No. 2) Act 2023 (F(No.2)A 2023), capital gains tax (CGT) was generally the most problematic tax for couples on separation and divorce. No CGT is payable on transfers between spouses/civil partners in the tax year in which they are married and still living together: such disposals are treated as having been made on a no gain/no loss basis.<sup>1</sup> This is the case even if the recipient is non-UK resident or the disposal is by way of sale. This treatment continues for disposals made in the tax year of separation. However, until April 2023 if the date of disposal was after the tax year of separation (that is, at a time when spouses or civil partners were no

<sup>1</sup>Taxation of Chargeable Gains Act 1992 (TCGA) s.58.

longer living together), section 58 of the Taxation of Chargeable Gains Act 1992 (TCGA) did not apply and such disposal was treated as taking place at market value.<sup>2</sup>

The date of disposal is not straightforward in divorce. It is usually the date of agreement<sup>3</sup> but if the transfer takes place pursuant to a court order then it is the date of the court order, unless the order precedes the decree absolute, in which case it is the date of decree absolute.<sup>4</sup> However, if the actual transfer of property takes place immediately without waiting for either decree absolute or the order to take effect then it is the date of the actual transfer. This is based on case law. HMRC comment as follows<sup>5</sup>:

“CG22420 - It is sometimes suggested that the agreement between the parties, which precedes a consent order, is a binding contract and so the date of any such agreement is the date of disposal of the assets. However you should not accept this view; it is a view that was rejected by the Privy Council in the non-tax case of *de Lasala v de Lasala* 1980 AC546 in which Lord Diplock stated,

‘Financial arrangements that are agreed upon between the parties *for the purpose of receiving the approval and being made the subject of a consent order* by the Court once they have been made the subject of the Court Order no longer depend upon the agreement of the parties as the source from which their legal effect is derived. Their legal effect is derived from the Court Order.’

This principle has subsequently been applied in tax cases, for example in *Aspden v Hildesley* (55TC609) and in *Harvey v Sivyver* (58TC569). In the latter case, Nourse J commented that it is

‘now well established that the legal effect of the provisions embodied in this kind of consent order is derived from the order itself and does not depend on any anterior agreement between the parties.’”

### Example 1

- 1) H and W separate in May 2020. Provided that any disposals between H and W took place before 6 April 2021 such disposals would be treated as taking place on a no gain/no loss basis. After 5 April 2021 the transfers are at market value.
- 2) H and W obtain a court order in year 1 requiring a transfer of property to W on decree absolute (year 2). The date of disposal is year 2. If the parties want the disposal to take place in year 1 they must accelerate the transfer into year 1.

<sup>2</sup> TCGA s.288(3): the provisions of the Income Tax Act 2007 (ITA 2007) s.1011 apply to the test of “living with”. See *Gubay v Kington (Inspector of Taxes)* [1984] S.T.C. 99 (HL). It is not always clear whether a couple have ceased living together: what of a couple who led entirely separate lives in different parts of a large property? They are still under the same roof so are they living together? Husband and wife remain connected persons until decree absolute or the final dissolution order of a civil partnership: see TCGA s.286 and *Aspden (Inspector of Taxes) v Hildesley* [1982] S.T.C. 206 DC.

<sup>3</sup> TCGA s.28.

<sup>4</sup> See HMRC, Internal Manual, *Capital Gains Manual* (published 12 March 2016; updated 7 September 2023), CGTM22410–22423.

<sup>5</sup> HMRC, Internal Manual, *Capital Gains Manual* (published 2016; updated 2023), CG22420, “Transfer of assets: between spouses or between civil partners: separation, divorce or dissolution: Court Orders”, emphasis added.

- 3) H and W have a court order after decree absolute requiring transfer of property. The date of transfer for CGT purposes is the date of the court order not decree absolute.
- 4) H and W agree to exchange chattels which is not dealt with by consent order or ratified by consent order and H also agrees to transfer to W some shares as part of the same agreement; the date of disposal is the date of agreement.

Following decree absolute a former husband and wife are no longer connected persons by virtue of their former marital relationship and the subsequent disposal of an asset by one to the other is normally a transaction at arm's length. Prior to decree absolute they remain connected persons even if permanently separated.

Until December 2019 HMRC accepted that a hold over relief claim could be made on transfers of business assets and this could alleviate CGT on transfers of shares in family companies that were done as part of a divorce settlement. In the light of *Haines v Hill*<sup>6</sup> HMRC had to change their view.<sup>7</sup> The spouse giving up the right to the business asset is in fact receiving consideration equal to the value of the assets being transferred. The CGT position became even worse and the Office of Tax Simplification recommended reform in its CGT report.<sup>8</sup> The government has broadly adopted the recommendations although the drafting is somewhat obscure.

### Disposals from 6 April 2023

Section 41(2) F(No.2)A 2023 amends section 58 TCGA by inserting new sections 1A, 1B, 1C and 1D to provide that from 6 April 2023 the no gain/no loss rule will continue to apply for three tax years after the tax year of separation or if earlier until a court order or decree absolute is granted. This is the case even if the transfer is not made pursuant to any court order. This allows spouses to make voluntary disposals to each other on an informal basis without having to worry about CGT after separation but before decree absolute.

Furthermore no gain/no loss treatment continues to be available without time limit if the assets are transferred in accordance with a formal consent order, a court order or an annulment.

Section (1D) is rather impenetrable as it uses a section on principal private residence relief (section 225B(2)(a) or (b) TCGA) to amend the CGT treatment of disposals of assets that may not be houses at all!

The provisions of section 58(1A)–(1D) only apply to disposals that occur on or after 6 April 2023.<sup>9</sup> Hence if the legal transfer occurs after 5 April but takes place pursuant to a court order issued before 6 April 2023 and decree absolute has occurred before 6 April 2023, the disposal takes place at the date of the later of court order or decree absolute and therefore the disposal is at market value, that is, the pre-6 April 2023 position operates.

The CGT change has been generally welcomed although in unusual cases some spouses may lose out.

<sup>6</sup> *Haines v Hill* [2007] EWCA Civ 1284; [2008] Ch. 412.

<sup>7</sup> HMRC, Internal Manual, *Capital Gains Manual* (published 2016; updated 2023), CG66886, "Relief for Gifts of Business Assets: Restrictions on Relief".

<sup>8</sup> Office of Tax Simplification, *Capital Gains Tax review – first report: Simplifying by design* (HMSO, November 2020).

<sup>9</sup> F(No.2)A 2023 s.41(6).

*Example 2*

Robin is foreign domiciled and a remittance basis user. It was agreed between Robin and Alf, Robin's separated civil partner, informally in December 2022 that Robin would transfer the foreign shares showing the most gain to Alf who would acquire them at market value. Robin would realise a gain but it would not be chargeable provided Alf did not sell and remit the proceeds before decree absolute when Alf ceases to be a relevant person. If the disposal takes place on or after 6 April 2023 then Robin will realise no gain but Alf will acquire them at the original cost for Robin. On a later sale by Alf his chargeable gain will be higher.

As noted above there are three possible dates to consider for CGT purposes: the date of the court order, the date of the decree absolute, and the date of the actual transfer of the asset.<sup>10</sup> If the court order was before decree absolute and this was before 6 April 2023 then the disposal is treated as taking place at decree absolute even if the transfer occurs on or after 6 April. If the court order occurred after decree absolute then that later date is the date of disposal so if the court order applying to Robin and Alf was after 5 April 2023 then the disposal occurs then and takes place on a no gain/no loss basis.

**The matrimonial home***CGT issues—the pre-6 April 2023 position*

For many divorcing couples the matrimonial home is their most significant asset. As part of the divorce settlement, it is usual for it to be sold and the proceeds split or for one spouse to transfer his interest in it to the other. Since 6 April 2020, full main residence relief is available only if the disposal takes place within nine months of the property ceasing to be the main residence of the transferor (18 months for disposals between 6 April 2014 and 5 April 2020).

Section 225B TCGA provided further limited relief.<sup>11</sup> The transferred property could continue to be treated as the departing spouse's only or main residence until the date of actual disposal if all the following conditions were met:

- 1) the disposal of the interest was to the other spouse and was pursuant to an agreement made in connection with the separation or dissolution of the marriage or under a court order;
- 2) in the period between the date when the donor left and the disposal occurred, the other spouse occupied the house as his or her main residence;
- 3) the transferor had not elected to treat another dwelling as his or her main residence for any part of the period concerned. The transferor could acquire another house but could not claim any main residence relief on it for the period before the sale of the former matrimonial home.

<sup>10</sup> HMRC, Internal Manual, *Capital Gains Manual* (published 2016; updated 2023), CG22423, "Transfer of assets: between spouses or between civil partners: separation, divorce or dissolution: date of disposal where asset is transferred under a Court Order".

<sup>11</sup> Formerly Extra Statutory Concession D6.

Until 6 April 2023 no relief was available under section 225B TCGA if the property was sold to a third party and the proceeds split between the couple. Until then the house had to be transferred to the other spouse for this relief to apply. This was a significant limitation.

Fortunately section 41(4) F(No.2)A 2023 improves the position greatly by amending section 225B TCGA and inserting new section 225BA.

*The CGT position from 6 April 2023*

A spouse or civil partner who retains an interest in the former matrimonial home will be given an option to claim private residence relief when it is sold even if the sale is to someone other than the other party to the marriage. Otherwise all the above conditions apply.

For disposals from 6 April 2023 new section 225BA TCGA deals with deferred payments under deferred sale agreements. Individuals who have transferred their interest in the former matrimonial home (or any house in which they have lived together which was their main residence) to their ex-spouse or civil partner in accordance with a court order and are entitled to receive a percentage of the proceeds when that home is eventually sold, will be able to claim main residence relief on those sale proceeds when received as if the gain is attributable to the initial disposal of the house when they transferred it to the spouse but accruing to the transferor at the time received provided it was their main residence immediately before they separated. The transferor is not prevented from claiming main residence relief on another house after the transfer of the former matrimonial home.

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