



The ties that bind

WITH MARRIAGE TRADITIONALLY CREATING A WHOLE NEW LEGAL AND TAX STATUS, IT WAS ONLY A MATTER OF TIME BEFORE CIVIL PARTNERSHIPS GAINED A SIMILAR STATUS. PATRICIA MOCK, TAX DIRECTOR AT DELOITTE, EXPLAINS JUST WHAT BENEFITS AND PENALTIES TYING THE KNOT CAN BRING?

Marriage has always been a trigger point for reviewing tax and financial planning matters, given the issues the change of status creates. The same now applies for civil partnerships in the UK, although there are small variations within the different UK member countries. The UK can be seen as an indicator of similar situations on a more international front.

The Civil Partnerships Act 2004 (CPA) will introduce a new dimension to the treatment of relationships for tax and legal purposes. The CPA creates a new legal status for same sex couples who register their relationship as a civil partnership in the UK from 5 December 2005. The status will confer rights and obligations that will reflect many of the provisions that apply to married couples.

It is important to note that cohabiting couples, of whatever nature, who are either unmarried or have not entered into a civil partnership will continue to be treated as single persons for tax and legal purposes. The main exception to this is in respect of state benefits and tax credits, where entitlements can be calculated per couple.

Highlighted below are some key issues that need to be considered by couples whatever form their relationship takes.

Taxed alike

Civil partners will be treated in exactly the same way as a married couple for tax purposes. Some specific examples of this treatment include:

- Transfers of assets between civil partners will be free of capital gains tax and inheritance tax in the same way as married couples.
- Jointly owned assets of married couples and civil partners will be considered beneficially owned in equal proportions unless the couple elect for a different specific proportion. Such an election would then be used to determine the allocation of income tax and capital gains tax liabilities between the couple.

These provisions afford married couples and civil partners the opportunity to allocate the ownership of assets between them, on a tax-free basis, in order to achieve maximum tax efficiency. More importantly, under the CPA, the estate of a

deceased civil partner left to the survivor, will be inherited tax free in the same way as for married couples. These tax advantages remain unavailable for couples who cohabit without marrying or registering their civil partnership.

Marriage also carries certain tax penalties, mainly in the context of the application of anti-avoidance provisions. These will also apply to civil partnerships. Specific examples of these provisions are:

- A married couple, and now civil partners, are treated as connected persons for tax purposes. This can have a particular impact when considering issues relating to the control of companies.
- There are rules which treat income and capital gains arising from a settlement as the settlor's, where either the settlor or their spouse can benefit. The definition of spouse will be extended to include civil partners.
- Spouses are treated as associated persons for the purposes of anti-avoidance provisions relating to offshore arrangements, which means that one spouse can be taxed because of action by the other spouse. These rules will be extended to civil partners. None of these provisions apply or will apply to cohabiting couples.

Main residence gains exemption

Each individual's main residence is exempt from capital gains tax, providing certain conditions are satisfied. A married couple can only have one main residence between them. This rule will now be extended to civil partners.

With ever-wider property ownership, couples frequently own their own properties before marrying or entering relationships. They may or may not retain both properties after marriage.

It is important to note that when a couple owning one or more properties between them marry or enter into a civil partnership, they must jointly elect within two years of marriage or registration of the civil partnership to treat one property as their main residence for the purposes of the capital gains tax exemption. In the absence of an election, the main residence is determined based upon all relevant facts of actual use of the properties. The benefit of the election is that it allows the couple to apply the exemption to the property which is likely to attract the highest tax charge on disposal. In addition, once made, the election can be varied between the properties in the future, if this increases the total amount of relief available.

These provisions do not affect the application of the exemption to the properties during the period before marriage/civil partnership. Furthermore, a property which has been a main residence before marriage/civil partnership and which then ceases to be the main residence will continue to attract exemption for the last 36 months of ownership, so that any sale of the second property in that time frame would still attract full exemption, subject to any earlier periods of use other than as the main residence.

Cohabiting couples can, in theory, each have a separate main residence. In practice however, for example if one of the properties is let, a main residence claim for it could not succeed, as the property would not be a residence of the owner.

Wills and estate planning

Property held by a couple as joint tenants passes to the survivor automatically, irrespective of the nature of their relationship, any provisions of the deceased's will or the intestacy laws (in the absence of a will). For all other property, and in the event that a couple has arranged ownership of their main home as tenants in common, the estate passes according to the deceased's will. Therefore, again, the nature of the relationship between the couple is irrelevant.

BOB MARLEY FLOATS OUT FROM A SIDE ALLEY – GONE BUT NOT FORGOTTEN

However, in the event of death without a will, the intestacy rules will grant automatic inheritance rights to the surviving spouse and also, under the CPA, to a surviving civil partner. The extent of these rights will depend on whether either individual has children.

For couples who are neither married nor civil partners, there are no inheritance rights whatsoever under the intestacy rules. Therefore, the only protection for the survivor of such relationships is through holding property as joint tenants or being the beneficiary of the deceased's will.

Pensions and life assurance

Upon marriage, or when individuals enter into a civil partnership, it is important to review the trust arrangements (and the attaching letter of wishes) relating to pension and life assurance arrangements, to ensure that potential beneficiaries and the way in which benefits are distributed are in line with latest wishes.

The principles are the same for non-married/civil partner couples and indeed, in this case, it is all the more important to ensure trust arrangements are up to date so trustees have sufficient guidance on paying benefits in the event of premature death. A non-married/civil partner may have more difficulty convincing trustees that he or she should be the principal beneficiary in situations where there are surviving parents or children.

It is also important to ensure pension provision is considered in the context of joint overall financial planning, upon marriage or entering into a civil partnership. Taking a holistic approach is important to ensure long-term joint financial objectives are achieved.

The break-up

A marriage can only be dissolved through the courts. Similarly, the dissolution of a civil partnership will be subject to exactly the same procedures the only difference being that adultery is omitted. Financial settlements and divisions of assets, including pension sharing, can be imposed between the parties, and provision also made for maintenance of and access to children of the relationship.

The courts will seek to value pension arrangements as part of the divorce settlement. Valuation can be complex in the case of final salary benefits, for which a fund value must be calculated and agreed between parties. Specialist advice is often required in these cases. Cohabiting couples have no formal process to end a relationship. One party has no entitlement to any assets or support from the other. □

Author

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