

The Former Matrimonial Home & Divorce – do we still need to consider tax?



The Former Matrimonial Home ("the FMH") can often be the most valuable asset listed in the financial settlement of any divorce. However, it is commonly understood that in most cases, Private Residence Relief ("PRR") will mitigate any capital gains tax ("CGT") arising on sale of the home. Furthermore, Finance Act (No. 2) 2023 improved the position on divorce, which previously left the leaving party exposed to Capital Gains Tax ("CGT") when they moved out. Surely, we don't need to consider CGT and the FMH anymore?

These recent changes have perhaps led us into a false sense of security. Where an interest in the FMH is transferred from one party to the other pursuant to a Court Order, there is now no immediate tax on divorce for the transferring spouse, as the property transfers at "no gain, no loss". However, to assume the recipient spouse will not have any tax liability either, is an oversight and potentially undermines the value of their settlement. Furthermore, if the FMH is not transferred, but instead is to be sold on order of the Court, both parties risk exposure to CGT if tax advice is not sought.

In this article, we will look to highlight some of the main areas where CGT exposure can arise on the sale of the FMH. It is important to remember, that full PRR is only available where all of the property is used as the only or main home of the owners and that they have occupied it as their only or main home throughout their period of ownership.





Claiming the correct elections

- If one party moves out of the FMH on separation, the FMH will most likely no longer be their only or main for the purpose of PRR. A gap in occupation of more than nine months could expose the party to CGT if the property is to be sold as part of the financial settlement.
- To prevent this tax exposure, it is possible for the leaving spouse to elect to treat this period of absence as "deemed occupation". This can ensure the whole period of ownership is covered by PRR and no tax liability arises.
- However, the election is not automatic and must be made in writing to HMRC within two years of disposal, or via the self-assessment tax return for the year of disposal. Failure to do so could expose the leaving party to an unwanted tax bill.



Large properties

- PRR is automatically applied for plots up to 5,000m² (0.5 hectares). Where the plot is larger than this, consideration must be made to whether the plot size is "necessary for the reasonable enjoyment of the property", bearing in mind its size and character.
- Typically, land within the plot used for purposes other than enjoyment of the property (such as grazing land for hobby farm animals, equestrian land or certain separate guest accommodation) may prevent full PRR from applying to any arising gain on sale.



Absences from the home

- Certain periods of absence from the home can be treated as "deemed occupation" in order to maintain maximum PRR. However, these can easily be lost or limited for example:
 - Deemed occupation may be restricted if there is a gap of more than two years before moving into a home due to building or renovation works
 - Deemed occupation may be lost if the parties move into a new home on return from a period of absence for any reason, unless prevented from doing so by employment.
 - Deemed occupation may be restricted if the period of absence is caused by an overseas assignment with work but the duties are not wholly performed outside the UK (even if only incidental duties are performed in the UK).





Business Use

- PRR can also be restricted if part of the property is used wholly and exclusively for business purposes.
- A home office that is also used for personal matters is generally not a concern, but where, for example, a garden room is used exclusively for a beauty business, part of any gain relating to that part of total sales proceeds will be excluded from PRR.



More than one home

- A person can only have one main home at a time to which PRR is applied. A married couple can only have one main home between them. This continues only up until the date of separation, thereafter they can apply PRR separately.
- Where a person or couple has more than one property (such as a city centre flat and a larger home in the country) , HMRC will determine which is the "main home" based on factual use of the properties. This can include a rented home as well as an owned property.
- Alternatively, an election can be made as to which property is to be treated as the main home for tax purposes, generally within two years of any change in occupation pattern.
- Elections can be varied, so careful planning can ensure the property with the largest gain, receives the greatest amount of relief.

These are just some of the areas where assuming there is no tax to pay on the sale of the FMH could cause unforeseen issues for the divorcing parties. The solution is to seek advice at the earliest opportunity from a qualified Tax Advisor, specialising in personal taxes. Please contact Jackie Hockney at HockneyGrey Consulting LLP at JackieH@hockneygrey.co.uk if you have any queries.

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