



## Capital Gains Tax

Share exchanges involving non-UK incorporated close companies  
– clause 36

Separated spouses and civil partners – clause 41

### Executive Summary

**Clause 36:** The proposed anti-avoidance changes to the share for share rules raise some questions as to whom they should apply to and how they might work in practice.

**Clause 41:** Changes to the no-gains/no-loss window and principal private residence rules for divorcing couples are to be welcomed. These changes were a recommendation of the soon-to-be-defunct Office for Tax Simplification, showing the value of its work.

We also make a wider point around the government's reductions to the CGT allowance, highlighting the need for awareness-raising and the implications for HMRC's resources.

### 1 Clause 36: Share exchanges involving non-UK incorporated close companies

- 1.1 Clause 36 will deem shares or securities received by certain taxpayers in 'share for share' exchanges or schemes of reconstruction as being located in the UK for future capital gains tax (CGT) and distribution income tax purposes, even if they are in fact shares or securities in foreign holding companies. This anti-avoidance measure was originally announced in the Autumn Statement in 2022 and will apply to transactions taking place on or after 17 November 2022. It is intended to prevent non-domiciled taxpayers using the 'remittance basis' from inserting foreign holding companies into the holding structure for currently UK assets tax-free and then emerging from the transaction holding 'offshore assets' subject to the remittance basis for future income and gains.
- 1.2 The existing rules surrounding 'share for share' exchanges and similar transactions treat the new shares or securities as 'standing in the shoes' of the old shares or securities for CGT purposes when swapped (i.e. it is a tax-neutral event in the qualifying circumstances). Those new shares/securities inherit the base cost of the old ones to be used in calculating the gain in any subsequent disposal, but the exchange itself is not chargeable for CGT. However, these proposals include that taxpayers potentially affected by the new provision can opt out of this treatment altogether and pay the tax on the disposal of the old shares or securities based on their current market value, instead of the latent CGT liability being transferred into the new ones: in this case, the new assets they receive would not after all be deemed to be located in the UK.
- 1.3 The taxpayers affected by the Clause 36 proposals are company shareholders with a material interest in a UK-incorporated company, that is broadly speaking a 5% interest,

either on their own or together with associated persons (i.e. in most instances, their spouse and/or immediate relatives).

## **2 CIOT comments**

- 2.1 While supportive of what the government are trying to do with clause 36, in terms of closing down an avoidance opportunity, we do have three concerns about whether the legislation, as written, is tight and definitive enough to be fully effective.
- 2.2 The first issue is that, by just applying to individuals in no other guise (for example, when they are acting as trustees), we are concerned that this measure leaves gaps that could be exploited. We consider there may be a potentially straightforward, avoidance opportunity here by having shares held by trustees just before the share-for-share exchange, which could be resolved by extending the measure to trustees. Likewise, it appears partnerships (including limited liability partnerships - LLPs) also escape these provisions if they were holding shares which were subsequently exchanged. We suggest that individuals acting as trustees and partners/members of partnerships/LLPs be included within the definition of those affected by this change, to ensure that artificial intermediaries are not put in place prior to any exchange.
- 2.3 If the rules were changed so as to apply this measure to trustees, consideration would need to be given to the question of how offshore trustees should make an election to disregard the tax neutral share-for-share treatment under s.138ZC. Furthermore, offshore trustees may not themselves have a UK CGT liability, but a UK-resident beneficiary would have the trust's capital gains attributed to them by virtue of s.87 of the Taxation of Chargeable Gains Act 1992 (TCGA) upon receipt of capital payments from the trust.
- 2.4 Second, we think the wording of the legislation with respect to ownership of the shares may also leave an avoidance opportunity. Section 138ZA(1)(d) TCGA 1992 (which would be introduced by Clause 36) refers to the person to whom the shares are issued – that is, the legal owner as opposed to the beneficial owner (the person who ultimately owns them once you look through any trusts, corporate vehicles, etc.). It is well recognised throughout almost the whole of tax law that the beneficial owner is the real owner for tax purposes, so this legislation should also apply, or not, by reference to beneficial ownership. The person to whom the shares are issued (e.g. a corporate nominee) may not be the beneficial owner.
- 2.5 We wish to avoid any potential confusion between legal and beneficial ownership - failure to clarify that beneficial rather than legal ownership is meant, would appear to leave a possible avoidance opportunity open; for example, with the use of a bare/nominee trust with a corporate nominee legal owner who does not meet the material interest/participator criteria in s.138ZA(2) for these new rules to apply.
- 2.6 Third, there might be a practical issue as regards those who are non-resident at the time of the share-for-share exchange, but who might later become UK resident before the ultimate disposal of their shares. If, while they were non-resident, there was a share-for-share exchange, it is unlikely that they will know that they have the opportunity to make an election to disapply the rule (and how to make it even if they do know). Careful thought needs to be given as to how this would work in practice, and also how it would interact with the five-year temporary non-residence rule. The temporary non-residence rule applies when someone leaves the UK and a subsequent chargeable disposal of a pre-owned asset takes place during that absence - if they return within five years of their departure then they are treated as having made the disposal upon their return.

- 2.7 We suggest that it might be simpler just to disapply the new sections altogether for those who are non-resident at the point of the share-for-share exchange on the basis that there is no downside to such a person electing out of tax neutral share swap treatment, as they are outside the scope of UK CGT anyway.

### **3 Clause 41 - Separated spouses and civil partners**

- 3.1 Clause 41 changes the rules that apply to transfers of assets between spouses and civil partners in the process of separating. It proposes that separating spouses or civil partners be given up to three years after the year they cease living together, to make ‘no-gain/no-loss’ transfers of assets; and unlimited time when the assets are the subject of a formal divorce agreement.
- 3.2 The ‘no-gain/no-loss’ rule relates to transfers of assets between spouses and civil partners who are living together. It means that for CGT purposes any gains or losses from the transfer are deferred until the asset is disposed of by the receiving spouse or civil partner, who will be treated as having acquired the asset at the same original cost as the transferring spouse or civil partner.
- 3.3 The current rules with respect to divorcing couples are that the ‘no-gain/no-loss’ rules apply to transfers between the parties in the tax year of permanent separation. Thereafter, the parties are merely connected prior to the insolvency of the marriage, meaning this could result in (dry) CGT charges on the transfer of assets.
- 3.4 Additionally, the legislation gives a departing spouse the benefit of Principal Private Residence relief (PPR) when the marital property is sold to a third party under a deferred sale arrangement/order.
- 3.5 Whilst the departing spouse disposed of their share of the property to the remaining spouse, it may be that the house cannot be sold immediately because of an agreement/court order (to provide, for example, continuity and a stable home for the children). Under such an agreement/order, the departing spouse retains an interest in the proceeds upon eventual sale. Monies that the departing spouse subsequently receives upon that third-party sale will be treated having been received when they initially vacated the property.
- 3.6 The proposed changes will apply to all transfers made on or after 6 April 2023.
- 3.7 The change to extend both the no-gain/no-loss treatment, and to afford the departing spouse PPR relief on a deferred sale were recommendations made by the Office of Tax Simplification (OTS) in [Capital Gains Tax Review: Simplifying practical, technical and administrative issues \(May 2021\)](#).

### **4 CIOT comments**

- 4.1 We welcome these changes. Extending the ‘no-gain/no-loss’ rule to separating married couples and civil partners is a sensible reform, which CIOT has been calling for. Allowing relief for the departing spouse on sales to third parties is likely to be more useful, and fairer, than merely transferring their share to the remaining spouse as the legislation does now.
- 4.2 The current rules state that when a couple cease to live together as a married couple (in circumstances likely to be permanent), they only have the rest of the tax year to transfer assets to each other without incurring an immediate CGT bill. A couple separating on 31 March have less than a week to do this before the tax year expires. Reducing the time

pressure to agree a fair division of assets should help make divorce a little less stressful in such circumstances.

- 4.3 In practice those with professional advice are more likely to be able to navigate the current rules and avoid the CGT charge while those without professional advisers frequently fall foul of it.
- 4.4 The new rule applies to inter-spousal transfers made after 6 April 2023. CIOT has suggested that it might have been better had the transfer date come into effect immediately or been backdated to allow those currently separated for more than a year to benefit immediately from the change too. As it is, couples who are already separated will only be able to benefit from this provision if they have been prepared to defer their transfer of assets until after 6 April 2023 – which may not be appropriate for their circumstances, or even possible.
- 4.5 We identified a potential issue with the draft legislation within section 1C where, by reading ‘before... the last day of the third tax year’ it appeared to close the three-year no-gain/no-loss transfer window on 4 April (the penultimate day of the tax year) rather than the more logical 5 April (the last day of the tax year). We drew this to HMRC’s attention and welcome the government’s tabling of amendment 6 to remedy this.
- 4.6 As noted above, these changes are being made as a result of an OTS report. This is the third recommendation from the report to be implemented, following the increase in the notification period for the disposal of residential properties from 30 to 60 days, and the incorporation of CGT into a Single Customer Account (facilitating taxpayers’ ability to report and pay CGT).
- 4.7 These are all significant practical improvements to the operation of CGT rules, and show the value of the OTS. The CIOT, along with other professional bodies, have made clear our disappointment about the abolition of the OTS. We see this as another opportunity to highlight the positive changes which have materialised as a result of the OTS, and the significant loss we believe it will be to tax policy-making.
- 4.8 We also draw the committee’s attention to OTS recommendations not implemented by the government. In particular, in the May 2021 CGT report which contained this change, other recommendations which would have had a positive effect included: the creation of a ‘real time’ CGT reporting service, an option to revoke the exempt status of Qualifying Corporate Bonds (removing the need for confusing and complex clauses to be included in loan documentation, purely for tax purposes), and reforms to share pool rules when considering multiple portfolios/investment managers (reducing compliance burdens for those affected and helping to facilitate better use of third-party data).

## **5 Additional point regarding CGT allowance**

- 5.1 Finally, we draw the committee’s attention to a wider point relating to CGT, which we hope can be raised briefly during the debate on clause 41. From the 2023-24 tax year, the CGT allowance (also known as the annual exempt amount) is being reduced from £12,300 to £6,000. In April 2024 it falls even further to £3,000. As a consequence hundreds of thousands more people each year will be brought into the net of paying CGT.
- 5.2 CIOT has two concerns about these changes. The first is around awareness. The lowered allowances will see many more people required to fill out a Self-Assessment tax return, and possibly pay more tax as a result, but many of these people may not be aware they need to do so until it is too late. We are calling on the government to launch a publicity campaign highlighting the changes, aimed at those who may be affected. These include people with small holdings of shares, non-UK residents selling investments in UK real estate and those

selling a second home, including foreign holiday homes, who may not have access to advisers or investment managers to inform them of the changes and their new responsibilities.

- 5.3 Our second concern is around pressure on HMRC. As well as being an additional burden on taxpayers, these changes – combined with a similar lowering of the income tax dividend allowance – mean HMRC will have many more tax returns to process and will increase their administrative burden significantly at a time when they are already struggling with demands on them. We are already deeply concerned about the difficulties both advisers and taxpayers face getting timely responses and action from HMRC. If the Chancellor is going to ask them to do more he needs to resource them adequately for this, or we fear service levels will fall further.
- 5.4 While we cannot be sure of the numbers affected, figures published by the OTS based on HMRC estimates suggest a £6,000 allowance in 2021-22 would have seen an extra 235,000 people paying CGT over the year, while for £2,500 that figure would have been 360,000. (It did not estimate for a £3,000 allowance.) It estimated that 139,000 people would be required to complete tax returns for the first time if the allowance dropped to £6,000, or 240,000 if it decreased to £2,500. (These figures appear in paragraph 4.15 of the OTS’s [‘Capital Gains Tax review – first report’](#), published November 2020.)

## **6 The Chartered Institute of Taxation**

- 6.1 The CIOT is the leading professional body in the United Kingdom concerned solely with taxation. The CIOT is an educational charity, promoting education and study of the administration and practice of taxation. One of our key aims is to work for a better, more efficient, tax system for all affected by it – taxpayers, their advisers and the authorities. The CIOT’s work covers all aspects of taxation, including direct and indirect taxes and duties. Through our Low Incomes Tax Reform Group (LITRG), the CIOT has a particular focus on improving the tax system, including tax credits and benefits, for the unrepresented taxpayer.

The CIOT draws on our members’ experience in private practice, commerce and industry, government and academia to improve tax administration and propose and explain how tax policy objectives can most effectively be achieved. We also link to, and draw on, similar leading professional tax bodies in other countries. The CIOT’s comments and recommendations on tax issues are made in line with our charitable objectives: we are politically neutral in our work.

The CIOT’s 19,000 members have the practising title of ‘Chartered Tax Adviser’ and the designatory letters ‘CTA’, to represent the leading tax qualification.

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For further information, please contact:  
George Crozier, CIOT Head of External Relations  
[gcrozier@tax.org.uk](mailto:gcrozier@tax.org.uk) 020 7340 0569

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