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Succession and Taxation Considerations

for the Family Lawyer

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When considering the division of assets for a spouse, civil partner or cohabitant on the break up of a relationship, often the focus for the client is on immediate living expenses and lump sums for him/herself and/or the children. The purpose of this lecture is to focus on succession, pension and taxation issues to be accounted for now in negotiations and which should also be considered for later second relationships.

1 Succession Considerations

It is interesting to outline what differences there are now between spouses and civil partners and the differences between such spouse and civil partners as against cohabitants. The Civil Partnership and Certain Rights and Obligations of Cohabitants Act 2010 ("CPCROCA") introduced changes that many believe equated the rights of spouses and civil partners completely, but that is not entirely correct. The rights of cohabitants are known to be relatively limited, yet they can impact significantly on an estate. The time limits in relation to the right of a cohabitant to claim need to be monitored carefully and careful consideration is required to decide if litigation is required even in non contentious cases.

1.1 Spouses –v- civil partners – Rights on Death

1.1.1 Legal Right Share

Part 9 of the Succession Act 1965 provides for the rights of spouses and children where a person dies testate or partly testate. The significant succession right of the surviving spouse, known as the legal right share, is set out in Section 111 of that Act. This right has been extended to civil partners amending the Succession Act to provide that the "legal right" in Section 3 of the 1965 Act will now mean :

a) the right of a spouse under Section 111 to a share in the estate of a deceased person, and

b) the right of a civil partner under Section 111A to share in the estate of a deceased person; and inserting

Section 111A to provide as follows :

a) If the testator leaves a civil partner and no children, the civil partner shall have a right to one-half of the estate.

b) Subject to section 117(3A), if the testator leaves a civil partner and children, the civil partner shall have a right to one-third of the estate.

However, while the legal right share of the surviving spouse cannot be affected by a Section 117 application (so that in a Section 117 claim taken by a step child of a surviving spouse, the Court can never award that stepchild an amount that would reduce the surviving spouse's legal right share), this is watered down in the case of a civil partner. The legal right share of a civil partner where there are children of a deceased person is now subject to Section 117(3A) Succession Act 1965 which provides as follows:

"An order under this section shall not affect the legal right of a surviving civil partner unless the court, after consideration of all the circumstances, including the testator's financial circumstances and his or her obligations to the surviving civil partner, is of the opinion that it would be unjust not to make the order."

Therefore:

A civil partner is now entitled to a legal right share of one half of the estate where there are no children (of the deceased). This is the same position for a spouse.

A civil partner is now entitled to a legal right share of one third of the estate where there are children of the deceased, but, unlike the legal right share of a spouse, the legal right share of a civil partner is vulnerable under Section 117(3A) to a possible claim being brought by a child of the deceased.

So prior to CPCROCA a step-parent's legal right share was always secure from the children of a testator. However if the step parent is a civil partner, the civil partner is not as protected – s/he is not in the equivalent position as a step-parent spouse. This has left uncertainty for the civil partner in a death situation where there are children of the other civil partner.

This legislation is surprisingly written in the double negative which might further appear to be an invitation to litigation. The Court has to be of the opinion that it would be unjust not to make an order affecting the legal right share under Section 117(3A) rather than being of the opinion that it be just to make the order under Section 117(3A).

The existing case law available to litigants in considering the merits of taking a section 117 claim will be available to litigants in connection with seeking attack of the Legal Right Share of a Civil Partner under section 117A.

1.1.2 Intestate Succession

Similarly in the case of intestate succession, while the civil partner is in a very similar position to the surviving spouse of the deceased, it is not an identical position due to the insertion of Sections 67A(3) to (7) Succession Act 1965 .

With language borrowed heavily from the more familiar Section 117, these subsections provide that the rights of a civil partner on intestacy are vulnerable to an application being brought by a child in a manner similar to a Section 117 application in the case of a Will. Once again the Court is entitled to make provision out of the intestate's share due to the civil partner if the Court is of the opinion that it would be unjust not to make the order (once again the double negative wording) after considering all of the circumstances including for instance the intestate's "obligation" to the civil partner. While the right to vary a provisional intestacy under Section 67A is more limited than the more heavily litigated Section 117, it does seem that this section is destined to give rise to considerable litigation. It also is open to criticism as imposing less certainty on intestacy which has always previously operated on a fixed basis of shares .

While in both cases this refers to the Court intervening if it was unjust not to intervene by making an order in favour of a child, the criteria for the Court to apply appears different under Section 67A from that of a claim taken by a child under Section 117 where Section 117 (3A) is to apply. Under Section 117 there is a requirement to show need and prove a failure in the moral duty of a parent. Section 67A refers to the court considering all the circumstances including a non

exhaustive list of four instances namely:
a) The extent to which the intestate has made provision for that child during the intestate's lifetime;

b) The age and reasonable financial requirements of that child;
c) The intestate's financial situation; and
d) The intestate's obligation to the civil partner.

This at first glance appears different from the criteria used in the Section 117 cases which refer to the court considering the means rather than the financial situation of the intestate. The needs of the claimant are critical in a Section 117 claim while under Section 67A age and reasonable financial requirements of the claimant are to be accounted for. Under Section 67A the intestate's obligation to the civil partner are specifically considered but under Section 117 the court generally considers the testator's moral duty to other people also. The four listed circumstances however are not exhaustive and therefore there is nothing to stop the court from taking other matters into consideration. No doubt there will be greater jurisprudence on this as this matter becomes more litigated in the future.

The effect of Section 67A is that the civil partner’s intestate share is again vulnerable to attack by a step child unlike the intestate share of a surviving spouse.

1.1.3 Foreign Aspects

The Irish succession system applies both fixed and discretionary forced heirship provisions to a deceased's estate. The fixed element is that of the legal right share (one half or one third of the estate depending on whether the deceased had children) and the discretionary element is in relation to the Section 117/117A Succession Act 1965 right of a child to claim against the estate, as outlined above.

Where assets of a deceased are held in other jurisdictions, forced heirship provisions providing for different succession rights may apply in relation to such assets under the jurisdiction local to where each asset is situate. To the extent an agreement is made between divorcing spouses/separating spouses for the division of assets it is important to consider who will be entitled ultimately on death to foreign assets, particularly in the case of separation which in itself may not have a recognised status abroad and where the jurisdiction may or may not recognise a civil partnership. Where a blocking order against rights under the Succession Act is sought under the divorce legislation , similar blocking orders if available should be sought in relation to foreign assets otherwise a surviving divorcee may be able to make a claim under the forced heirship provisions for provision out of the foreign assets despite a blocking order being in place for the Irish situate assets.

The organisation Notaries in Europe with the support of the European Commission launched the website Couples in Europe **www.coupleseurope.eu** which is a useful first point of call for practitioners where European aspects are involved. There is a similar website for succession law in Europe **www.successions-europe.eu**.

1.1.4 Revocation of Will

A Will is revoked by the subsequent marriage or civil partnership registration of a testator.
A Will is not revoked by a divorce of the testator / dissolution of a civil partnership entered in to by the testator.
There is a perception that a divorce, similar to the marriage, automatically revokes the Will however the Succession Act is silent on divorce in the case of revocation of Wills. While the automatic rights of inheritance for a spouse/civil partner do cease and are extinguished on the divorce/dissolution, what is voluntarily being left under the Will does not change even if it would seem clear that a Will made many years before the divorce is not likely to be the testator’s intended last wishes.

Therefore while the family lawyer is usually careful to ensure that a blocking order is obtained if possible under Section 18(10) Family Law (Divorce) Act 1996 , it is also very advisable that s/he informs the client of the importance of updating his/her Will so that there is no longer provision made for their divorced spouse, presuming that is the client's wish.
It is also advisable for the divorcee to consider in the event of remarriage whether there should be a prenuptial agreement to cover off among other issues the succession rights of the surviving second spouse/civil partner. If prior to the marriage a Will is made providing separately for the spouse to be, the Will should be made in contemplation of the marriage to avoid automatic revocation on marriage. Where a testator wishes to provide for his/her children of the first marriage after death, while a 'full blown' prenuptial agreement might be resisted, a simple declaration renouncing the legal right share might be easier to organise . This would not mean that the second spouse would not be provided for; the testator's will could provide for the full estate to pass to the second spouse, but it would mean that the automatic right to one third of the estate (in the case of children of the testator surviving) would not be available. Indeed to protect the children's inheritance after the second spouse's death, the provision for the spouse could be made in the form of a life interest, allowing the spouse the use and the income of the assets for his/her lifetime and protecting the capital for the children. This may reduce the potential of a Section 117 Succession Act claim .

1.1.5 Testamentary Guardians

Where there are minor children it is sensible to provide that a testamentary guardian is appointed under the Will by your client in the event there is a concern to ensure that there is still representation for the child from one 'side' of the family as opposed to the other . The testamentary guardian can then act jointly with the surviving parent as the other guardian where so appointed.

1.2 Spouses/civil partners –v- Cohabitants – Rights on Death

Unlike spouses and civil partners, a cohabitant within the meaning of CPCROCA is not automatically entitled to a share in the estate of the deceased cohabitant, whether testate or intestate. Instead a qualified cohabitant as defined has the right to apply to court for provision out of the net estate of his or her deceased's cohabitant where inadequate or no provision has been made for them by the deceased cohabitant by Will or otherwise.

The relevant time limits are as follows:

To be a qualified cohabitant the couple should have been in a relationship with each other for either 2 or 5 years immediately before the time the relationship ended whether by death or otherwise. This excludes time of cohabitation where one or other of the couple was married to someone else (note time in a civil partnership with someone else is not excluded surprisingly even though a cohabitant can be of a same sex or opposite sex relationship) and the couple of the marriage had not yet lived apart for at least 4 out of 5 years, i.e. the 'clock' does not start until 4 years after the marriage is over even if there are children of the cohabitant relationship.
If the cohabitants' relationship had ended more than 2 years prior to death, there are different criteria for qualifying for a claim – financial dependency must be proven in such a case.
If the cohabitants' relationship had ended prior to death and the claimant had since married/ entered a recognised civil partnership with another person, no claim for provision can be made.
The claim for provision must be made by the claiming cohabitant within 6 months of the date of the grant of representation to the estate of the deceased (similar to the claim by a child under section 117 Succession Act 1965).

Section 194(3) CPCROCA provides:

"The court may by order make the provision for the applicant that the court considers appropriate having regard to the rights of any other person having an interest in the matter, if the court is satisfied that proper provision in the

circumstances was not made for the applicant during the lifetime of the deceased for any reason other than conduct by the applicant that, in the opinion of the court, it would in all the circumstances be unjust to disregard."
The court in deciding to make an order for provision for the cohabitant must have regard to the rights of any other person having an interest in the matter (including legal rights of any surviving spouse, civil partner and children) and decide if proper provision was made. It should take into account orders already made for maintenance, pension and property adjustment orders, any provision under the will of the deceased, the interests of the beneficiaries of the estate and the factors the court takes into account when deciding if a maintenance order should be made .

1.3 Recent case law

1.3.1 Blocking orders

In a case reported in the Irish Times last August the High Court has indicated that it will no longer be routine for the court to issue a blocking order preventing an application to be made for financial provision out of the estate of the deceased spouse. Instead the court will need to satisfy itself that there is sufficient protection for maintenance payments to continue after the death of the paying spouse.

The practice to date had been that provision would be made for continuing lifetime maintenance of a dependent spouse through the payment of a lump sum or property adjustment order, through the setting-up of a life insurance scheme to provide for continuing maintenance or through a pension adjustment order. In such instances a blocking order would be appropriate so that the divorcee would not get a 'second bite' of a distribution at death. However because more and more families have limited resources, increasingly such clean break arrangements are more difficult to make, particularly where there is no pension or life assurance to guarantee a maintenance payment. Because of this the court is now recognising that there should be opportunity to ensure adequate maintenance continues post death for the divorcee.

The case that came before the High Court reported last August involved a couple who were legally separated and the man later sought a divorce in the Circuit Court. The court made the divorce decree, giving the wife a lump sum of €50,000 and €200 a week in maintenance. The husband had no pension so a Pension Adjustment Order could not be made. The Circuit Court judge also made a blocking order that neither could apply for provision out of the estate of the other.
The wife appealed the issuance of the blocking order because of her concern that there was no security for the maintenance payment. She sought the right to make a claim against her husband's estate if he died.
"It is reasonable for the wife to have fears around what is to happen to her in the event of the applicant's death, whenever that should occur," Mr Justice Peart said.
He ordered the husband to give a month's notice to the wife of any intention to retire, sell or otherwise dispose of his business, so that she could take legal advice about how to secure maintenance. Regarding the blocking order, Mr Justice Peart said: "It seems appropriate that the court should not make a blocking order under section 18(10) of the Act of 1996 unless the court can be satisfied that proper provision has been made for her maintenance after her husband's death." This would allow her to make an application for provision out of his estate, if her circumstances justified it. It would be a matter for the judge hearing the application to consider the case history, he said.
The implications of this are that because of the lack of finances available there is now likely to be less of a 'clean break' than financial circumstances had previously permitted. While it would seem unlikely that there would be an opportunity given to a spouse to revisit a decision to block made some time ago, practitioners will need to be aware of the importance of negotiating maintenance payments without assuming the court would automatically grant a blocking order.

1.3.2 Second Bite cases and inheritances

The decision in G v G set out general principles to apply where there has been a prior separation agreement followed by a subsequent application to court. Included in that were, from a succession perspective, welcome principles as follows that:

the requirement to make proper provision is not a requirement for the redistribution of wealth; and

if a spouse acquires wealth after a separation and the wealth is unconnected to any joint project by spouses during their married life, then that is not a factor of itself to vest in the other spouse a right to further monies or assets.

This has reassured parents of children who have divorced that whatever their child might inherit from the parents later will not automatically be open for a claim by the child's spouse. While there is still no absolute certainty that the inheritance is fully protected, the judgement in the G v G case goes far in indicating that there would need to be extenuating circumstances to assume that that later inheritance is open for redistribution.

2 Taxation on Succession

2.1 Spouses & civil partners and tax

The spouse and the civil partner are for tax purposes in an equal position . CPCROCA itself did not contain any taxation provisions relating to civil partners but instead Finance (No. 3) Act 2011 provided sweeping changes to taxation legislation across all the tax heads. On foot of this generally where there was a reference to a spouse there is now a reference to a spouse or a civil partner and relations extending from that spouse now also generally extend from the civil partner. For example, in establishing for tax if a person is connected or related to another person, already the child of a person includes a step child and now there is specific provision for the child of the civil partner and all relations off this in the relevant cases. This is very welcome i.e. the child of the civil partner is being treated in the same way as a step child so there is no difference in tax between spouses and civil partners. However this did lead to very complicated drafting of the relevant tax legislation.

Therefore the reliefs such as principal private residence relief for CGT, exemption for gifts and inheritances apply to civil partners in the same way (and with the same conditions) as apply to spouses. See paragraph 4 below for further consideration of the effect of this on transfers on divorce.

A few interesting points arise from the fact that not all the tax legislation was merely a replacement of the word 'spouse' with 'spouse or civil partner'. For instance the legislation does not redefine relatives so that the restrictions / anti avoidance that pertains to relatives and the extended relations of relatives applies to civil partners and their children but not to the extended relationships of the civil partner/child.

2.2 Cohabitants and tax

CPCROCA did not contain any taxation provisions relating to cohabitants either; again instead Finance (No. 3) Act 2011 provided for the taxation position for this relationship.

Payments made on foot of a court order for redress under ss.173 or 194 are treated in the relevant charging provisions under the various tax heads in the same manner as payments made to a spouse/civil partner in a separation/divorce. Thus maintenance paid under a court order under section 175 CPCROCA can be deducted for income tax purposes from the payer's tax return and paid gross to the payee who in turn should return the tax, similar to separated spouses or civil partners ; property transferred to a qualified cohabitant under a property adjustment order is taxable in the same manner as property transferred to a spouse under a separation agreement so that the disposal is treated as not giving rise to CGT and the original base cost and acquisition date passes to the acquiring cohabitant with the asset . In addition an order for the deceased's estate to pass property of the estate to a surviving cohabitant is exempt from CAT .

The principal limitation in relation to the tax position for cohabitants is that, unless there is an order made under the redress provisions of CPCROCA, there is no tax relief for the cohabitant, even if the cohabitants had agreed the arrangements under a Cohabitants Agreement in accordance with section 202 CPCROCA. The effect of this is that a

cohabitant is treated as a stranger for tax purposes. For instance for CAT purposes any transfer other than for full value is deemed to be a gift with a group threshold of €15,075 after which tax at 33% of the value passing arises. Submissions have been made seeking to increase this threshold to provide that a qualified cohabitant should stand in the same threshold for CAT as a child i.e. with a group threshold of €225,000.
The dwellinghouse exemption from inheritance tax (CAT) should be considered when drafting Wills in the event that the deceased cohabitant leaves the house in which the cohabitants both lived to the surviving cohabitant. Provided the surviving cohabitant fulfils the conditions of that exemption, there may be no CAT arising on that inheritance. If however the surviving cohabitant has an interest in another dwellinghouse or has not the requisite number of years of living in the house, s/he may not qualify. The changes brought in from February 2007 to gifts where the time that both the cohabitants live together is disregarded means that the relief is unlikely to be relevant for gifts for cohabitants and so an agreement to transfer property pre death will unlikely be exempt.

Given that CPCROCA appears to encourage the agreement between cohabitants to provide for financial matters during the relationship or when the relationship ends under section 202 CPCROCA (the 'prenuptial for cohabitants'), it is somewhat surprising that there is not a taxation relief for transfers made on foot of such agreements.
The difficulty with this aspect is that under the current taxation provisions for cohabitants they are obliged to litigate to obtain tax relief. Even if a cohabitating couple are happy to regularise and agree their finances, they cannot do so tax efficiently without formal litigation and the requirement for the court to assess the position. The relief is then confined to what the court orders by way of redress. There is then a possibility that if a deceased cohabitant was in the court's opinion over generous in his bequest – the relief would only be against what the court would order. It is not known if a court order confirming an existing bequest to a cohabitant means that the bequest in itself is the subject of the order and therefore tax free. Is that an order for proper provision and so the bequest is free of inheritance tax or is it a dismissal of the application for proper provision under s194 CPCROCA and confirmation that the bequest should stand and therefore the bequest is taxable? Similarly a contractual agreement to pass assets on death that is confirmed by the court could be either a court order making provision (tax exempt) or a dismissal of the application for proper provision under s194 CPCROCA (taxable).
The practitioner will therefore need to carefully advise the cohabitant in relation to any cohabitant agreement or Will whether litigation may still be required to reduce tax that might otherwise arise on any transfer by agreement or Will. Structures such as discretionary will trusts, although causing a tax charge in themselves, may be the best solution to protect the surviving cohabitant's bequest bearing in mind the interests and expectations of the deceased cohabitant's other beneficiaries that a court may need to otherwise consider.
See also in the Appendix the Frequently Asked Questions on Taxation and the Redress Scheme for Cohabiting Couples September 2012.

3 Pensions

3.1 Case law

3.1.1 Receivers and ARFs

In 2010 there was considerable disturbance in the pension advisory industry concerning the vulnerability of pensions to creditor attack. Previously it had always been the view that a pension was protected from a creditor but then in 2010 a receiver was appointed over the Brendan Murtagh Approved Retirement Fund (ARF).
The case at the time however was distinguished by advisors because that appointment of the receiver over the ARF was not contested at the time so there was no analysis given as to whether in fact the receiver would have the right to take over an ARF. In addition, generally pension funds prior to retirement that were not yet converted into an ARF were held in a different trust structure, leaving some room for doubt as to whether those pensions could be attacked.

The outcome of the case did however highlight for the industry the distinction between pre retirement pension structures (usually set up in a trust form) and the ARF structure where the ARF does not need to be held under a trust but is deemed to be held by the Qualifying Fund Manager as nominee for the beneficial owner, yet where there are contingent beneficiaries, such as a spouse or children.

3.1.2 Receivers and pensions

The High Court in October 2012 issued judgment in a significant case on individual self-administered pension schemes.

A bank sought to appoint a receiver over individual borrowers' self-administered schemes. The Court held that the characteristics of the pension scheme precluded the appointment of a receiver.

As mentioned above the prevailing view in the pensions industry had been that pre-retirement benefits were not vulnerable to attack by creditors. However, there was no clear Irish legal authority on the point so the matter was not absolutely free from doubt, particularly because of the Murtagh case, until this judgment.

It is important to note that, whilst most Irish pension schemes have the same characteristics as the pension schemes in the case, all scheme documents must be reviewed to ensure that appropriate protections are in place.

3.2 Practical issues for pensions

3.2.1 Communication & Mechanism of Pensions Adjustment Order (PAO)

Practitioners should contact the trustee of the self administered scheme both prior to agreeing any settlement for the Court to rule on; and after the order is made to ensure the pensioneer trustee is aware of the order. Enquiries must first be made of the trustees of the pension scheme or contract provider (insurance company) in the case of PRSAs, ARFs and Personal Pension Plan type structures as to:

Trustee details (name and address)

Copy of the Trust Deed and Rules.

Type of pension scheme - Defined Contribution or Defined Benefit (for occupational schemes), retired annuity contracts (for self employed), PRSA, buy out bonds, paid up pensions, preserved benefits from previous employments or Civil Service Superannuation schemes.

Most recent Benefit Statement and Statement of Projections of Pension Fund to normal retirement age.

Details of investment asset mix

Up to date transfer valuation

Contingent benefits in place (Death in service payments)

Confirmation as to whether scheme is suitably funded (Defined Benefit schemes)

Confirmation of the benefits and how they are calculated (members pension, lump sums payable in commutation and spouse's/dependant children death in retirement pension)

Eligibility conditions for the member to enter the scheme (e.g. to determine if there a pension preservation order is required)

Details of additional voluntary contributions

Details of any transferred benefits from previous employments/schemes

What options are available regarding transfer in lieu of retaining the designated benefit (this can be requested later)

Section 54 Pensions Act 1990 provides for the trustees duty to disclose this information and the Court can direct disclosure under Section 12 Family Law Act 1995 and Section 17 Family Law (Divorce) Act 1996. Indeed the Court usually requires confirmation from the pension scheme or provider in the event of agreement by the parties where the Court is asked to rule on such agreement.
Where the Court decides to make a PAO in relation to retirement benefits, part of the member spouse's benefits (called the Designated Benefit) is designated for payment to the other spouse (or to a person representing a dependant child). A separate PAO is required for contingent benefits (death in service payments).

The Court will then rule on the two key factors which will determine the amount of the Designated Benefit. These are the Relevant Period and the Relevant Percentage. The Relevant Period is the period of service that should be taken into account in determining the benefit. The order cannot extend beyond this date. It typically relates to the period of the marriage. The Relevant Percentage is the percentage of the benefit that is to be taken into account. If it is agreed by both parties to disregard the pension or ensure that neither party has an interest in the other party's pension, a nominal Pension Adjustment Order (also known as a Nil Adjustment Order) will be made for 0.001%.

The trustees are responsible for calculating the Designated Benefit following the procedure set out in legislation and in detailed guidance notes issued to them by the Pensions Board. The calculation depends on whether the retirement benefits are determined on a defined benefit or a defined contribution basis. The transfer amount is calculated and applied to provide independent benefits within same scheme;

in another occupational scheme of which the dependent spouse is a member (provided the trustee of the other scheme accept it);

into a buy out bond

into a PRSA

The Court usually sends the PAO to the trustees however it has been known that the trustees do not always receive these orders, therefore it is important for family law practitioners to contact the trustees themselves direct with a copy of the order once issued.
Once a PAO has been made the trustees on receipt of the order should notify the person(s) in whose favour the order is made of the amount and nature of retirement benefits and/or contingent benefits which have been designated under the order(s). The trustees should also advise the person of the options available regarding any transfer amount that may be available in lieu of retaining the designated benefit.

As there will be decisions for a member to take in relation to the pension at retirement, if the non member spouse wishes to be independent of those decisions, it would be better to seek to separate the Designated Benefit from the main pension. Otherwise decisions such as early or late retirement taken by the member spouse could affect the payment of the Designated Benefit. In a Defined Benefit scheme that may mean the non member spouse would seek to establish an independent benefit in lieu of retaining the benefit in its original form.

Therefore once an order has been granted to the dependent spouse, the dependant non member spouse should consider how they would like this benefit managed going forward. Options typically available are:

Default position - retention of designated benefit within the scheme
Independent benefit be established (Defined Contribution Type Scheme or when a Member elects transfer on leaving service).

However this option is only available if member spouse has not commenced receiving retirement benefits.
3.2.2 Death and Pension Adjustment Orders. Bearing in mind the level of complexity generally surrounding pensions, the added tier of a PAO can leave a spouse very confused as to what that means in real terms for them into the future. Various provisions apply to dealing with the benefit taken by a spouse after the PAO has been made depending on what circumstances arise in the future. It is useful for practitioners to make their client aware of what the effect of the PAO will be in real terms in the event of retirement or death in scenarios such as follows:

If, while a member spouse is alive and he has not yet reached retirement, the dependant spouse dies, then the Designated Benefit passes to the personal representative of the dependant spouse.

If, while a member spouse is alive and he has reached retirement, the dependant spouse dies, then the Designated Benefit passes to the personal representative of the dependant spouse based on a calculation of the Designated Benefit at that time calculated on an actuarial basis.

If, while the member spouse is alive whether retired or not, his dependant child who holds a Designated Benefit dies, then the benefit ceases – no further payments can be made.

If the member spouse dies pre retirement in service and the dependant spouse is alive, the Designated Benefit passing to the spouse is treated as a notional benefit as if payable the day prior to death and the benefit to a dependant child is the actuarial value on date of death of the Designated Benefit. [Note there may also be a PAO in relation to the contingent benefit and therefore a pay out of the death in service lump sum benefit.]

If the member spouse leaves the scheme pre retirement (moves job) and the dependant spouse is alive, then the benefit to spouse passes in accordance with the rules of scheme, where the proportion of overall retirement benefit is passed to the spouse.

3.2.3 Approved Retirement Funds
The structure of an Approved Retirement Fund (ARF) is unusual. It is not a trust as would be typical in a pension scheme. Its legal status is not specified in legislation. On that basis a pension adjustment order is in fact not the order to seek to adjust an ARF. Instead a Property Adjustment Order should be sought.

The ARF is held by the Qualifying Fund Manager as to its legal title, apparently as nominee for the individual. Yet the ARF arises from the pension contributions made by the individual to a scheme that provides for not just for the individual, but also, albeit on a contingent basis, for his spouse and dependants. So it is arguable that the individual does not own the ARF himself beneficially absolutely. This is an argument proffered by those seeking to protect an ARF from attack by creditors of the individual, not helped by the Murtagh case where the ARF was given to the creditors in a settlement, but assisted by the recent ESB case, discussed above. If the Property Adjustment Order has been made in advance of a creditor claim against the ARF, this would seem to allow protection against the Designated Benefit awarded to the spouse.

3.2.4 Taxation and Pensions
Where payment from a pension is made to a spouse under a PAO, then the income is treated as that of the recipient and taxed accordingly. If the payments on retirement under an ARF are not yet being made and the member spouse dies, no income tax charge will arise on death of member spouse where a PAO is in place or indeed the spouse inheriting the ARF under the Will/intestacy of the deceased member spouse. However the surviving spouse is taxed in

normal way on withdrawals from the ARF.
Children age 21 or older who inherit an ARF are not subject to CAT on the value of the ARF received but instead pay income tax at the standard rate (not CAT, albeit the 'section 60' insurance policies can be used to pay that tax as if it is CAT). The child in each case must be 21 or older at the date of death of the owner of the ARF - it is not sufficient to postpone the taking of the ARF into a trust until that age is reached.

This income tax charge does not aggregate with any benefits taken under the Will or on intestacy, unlike for those children under age 21 who are subject to CAT (inheritance tax) on taking the benefit of the ARF on their parent's death and not income tax but who would have the group threshold available to them in calculatiing the CAT payable. Note the ARF although a lump sum may be seen to be in the category of the exemption for minor (under 18) children in respect of the provision of support, maintenance and education when both parents have died where the provision of that support etc. is part of the normal expenditure of someone such as the disponer.

This capital taxation position for ARFs is to be extended to PRSAs under Finance Bill 2013, which has not yet been enacted at time of printing.

4 Divorce

4.1 Taxation issues in negotiations

4.1.1 Maintenance and court orders

For income tax purposes if the husband and wife are not living together (separated under Court Order or by Deed of Separation or separated in such circumstance that the separation is likely to be permanent) then they are treated as separate persons and taxed as single persons unless they elect to be treated as jointly assessed . This right to elect to be jointly assessed is extended to a divorced couple under section 5 Family Law (Divorce) Act 1996. Both spouses must be Irish resident and not have remarried for this election to be permitted. The election is available to civil partners also.

If the election is made by the couple to be jointly assessed even though they are separated, the couple is assessed to income tax without regard to the maintenance payments and their married person's tax credit is available to them. If the couple has their own separate income apart from the maintenance payments, the income tax is calculated using the separate assessment procedure but ignoring the payer's income as undiminished by the maintenance payments. Such cooperation can be financially sensible to ensure that the lower rate bands and credits are not lost in the context of the individualization provisions of the income tax code.
If the couple does not elect to be treated as jointly assessed then they are taxed as single persons. In such a case the tax of the payee on a maintenance payment that is legally enforceable should not be deducted at source; instead the payment is deducted from the income of the payer and treated as Schedule D Case IV income in the hands of the payee. For the year of separation, the married person's tax credit is available to the payer in addition to the deduction of the payment. It is important that the recipient spouse is aware that the maintenance payment received is taxable in that spouse's hands.

If the payment is made without a formal separation agreement, then the deduction cannot be made from the income of the payer unless in limited circumstances. While the married person tax credit is available, the standard rate band of the payee is not available. It is therefore important that a client is made aware of the taxation implications of making or receiving legally enforceable maintenance payments. If later top ups for maintenance might be made, the client should be made aware of the distinction for tax purposes of those top ups (if not legally enforceable then not deductible) against the original payments (if legally enforceable then deductible). Either way the couple need to be aware that there is no tax saving achieved by virtue of making or not making maintenance payments other than in the case of electing for joint assessment to use up any shared credits available as the payment merely shifts the tax burden to the recipient.

This treatment for deductions is applicable to periodic type payments and not lump sum payments.
Payments for dependant children are ignored for tax purposes – neither deducted nor taxed. Irrespective of where the child is living the person who pays his/her maintenance is entitled where appropriate to the incapacitated child tax credit.

See also appendix

IT2 Taxation of Married Persons and Civil Partners July 2011;

IT3 What to do about tax on the breakdown of a marriage, civil partnership or cohabiting relationship;

Frequently Asked Questions on Taxation and the Redress Scheme for Cohabiting couples September 2012.

4.1.2 CGT traps
4.1.2.1 Transfers without a court order/deed of separation

Any transfer of chargeable assets for CGT purposes are generally treated as if exempt in effect where the transfer is between a couple living together as husband and wife or as partners to a civil partnership .
A transfer after separation/divorce/dissolution is not treated as if exempt unless it is a transfer made under Deed of Separation, court order on separation, divorce order or dissolution order .
Any other transfer after separation where the couple are not living together as husband and wife, i.e. voluntarily without a court order or by deed of separation will be treated as a disposal for CGT purposes in the usual way even if the couple are still married to each other.

4.1.2.2 Unrealised gains

As mentioned while the initial effect of the transfer is that it appears to be exempt, in fact the transfer is not strictly an exempt transfer but instead is one in which there is deemed to be a no gain/no loss so that the acquiring spouse will take the base cost of the disposing spouse and the date of acquisition for ownership purposes. This means that there is not a rebasing of the value of the asset on transfer. This can be significant for negotiation purposes if the asset has increased or decreased in value since the original acquisition.

For example if the couple agree that land purchased by the husband in 1980 for €20,000 should now be transferred to the wife at its current value of €100,000, the wife is deemed to take the land at the value of €20,000 in 1980 for tax purposes. If she later sells it for €100,000, she will have made a chargeable capital gain calculated as follows:

Disposal price 100,000
Less Acquisition cost 20,000
Indexation factor to 2004 3.240
Indexed acquisition cost (64,800)
Capital Gain 35,200
Tax at 33% (ignoring personal exemption) 11,616

Therefore the wife should ensure that the agreement to transfer €100,000 in value of land to her is treated in division terms at a value of €100,000 less the accrued unrealized indexed gain at the current rate of CGT. In the case of a loss on shares instead of transferring the shares, if more convenient, the shares could be sold by one and repurchased by the other spouse so that the loss relief restrictions would not apply as the spouses are no longer living together .

4.1.2.3 Principal Private Residence Relief (PPR)

Where a transfer is made by a couple of a property in which they lived, no CGT will arise by virtue of the principal private residence relief.
Couples with more than 2 residences available to them (whether they own them or not) must elect which one will qualify for the relief within 2 years of acquiring or occupying the second residence or else leave themselves open to the Inspector of Taxes chosing for them.
While this may not impact on a spouse transferring the house to the other spouse on foot of a court order, it might be relevant if there is agreement that the family house is to be sold at a later stage and the couple are no longer living in it together but one (the non owner) lives there and the other, as owner disposing of the house, is living in another house that s/he also owns.

Appendix

1. Frequently Asked Questions on Taxation and the Redress Scheme for Cohabiting couples September 2012- attached

2. IT2 Taxation of Married Persons and Civil Partners July 2011 – attached

3. IT3 What to do about tax on the breakdown of a marriage, civil partnership or cohabiting relationship - attached

4. Frequently Asked Questions on Taxation and Civil Partners September 2012

5. Taxation of Cohabitants

Extracts from Taxes Consolidation Act 1997 (TCA97) and Capital Acquisitions Tax Consolidation Act 2003 (CATCA03)
Section 1031P TCA97 Interpretation (Chapter 1)
(1)In this Part— "cohabitant" has the same meaning as in section 172 of the Civil Partnership and Certain Rights and Obligations of Cohabitants Act 2010; "inspector", in relation to a notice, means any inspector who might reasonably be considered by the individual giving notice to be likely to be concerned with the subject matter of the notice or who declares himself or herself ready to accept the notice; "qualified cohabitant" has the same meaning as in section 172 of the Civil Partnership and Certain Rights and Obligations of Cohabitants Act 2010.

Section 1031Q TCA97 Maintenance where relationship between cohabitants ends

(1)In this section— "maintenance arrangement" means an order of a court under section 175 of the Civil Partnership and Certain Rights and Obligations of Cohabitants Act 2010 giving rise to a legally enforceable obligation; "payment" means a payment or part of a payment, as the case may be. (2)(a)This section applies to payments made directly or indirectly by a qualified cohabitant under or pursuant to a maintenance arrangement. (b)For the purposes of this section a payment, whether conditional or not, which is made directly or indirectly by a qualified cohabitant under or pursuant to a maintenance arrangement shall be deemed to be made for the benefit of the other qualified cohabitant.
(3)Notwithstanding anything in the Income Tax Acts, as respects any payment to which this section applies made directly or indirectly by an individual under or pursuant to a maintenance arrangement for the benefit of a qualified

cohabitant— (a)the individual making the payment— (i) shall not be entitled on making the payment to deduct and retain out of the payment any sum representing any amount of income tax on the payment, and (ii)shall, if he or she makes a claim in that behalf in the manner prescribed by the Income Tax Acts, be entitled, for the purposes of those Acts, to deduct the payment in computing his or her total income for the year of assessment in which the payment is made, and (b)the payment shall be deemed for the purposes of the Income Tax Acts to be profits or gains arising to the qualified cohabitant, and income tax shall be charged on that qualified cohabitant under Case IV of Schedule D in respect of those profits or gains. (4)(a)Subsections (1) and (2) of section 459 and section 460 shall apply to a deduction under subsection (3)(a)(ii) as they apply to any allowance, deduction, relief or reduction under the provisions specified in the Table to section 458 . (b)Subsections (3) and (4) of section 459 and paragraph 8 of Schedule 28 shall, with any necessary modifications, apply in relation to a deduction under subsection (3)(a)(ii).

Section 1031R TCA97 Transfers of assets where relationship between cohabitants ends
(1)Notwithstanding any other provision of the Capital Gains Tax Acts, where by virtue or in consequence of an order made under section 174 of the Civil Partnership and Certain Rights and Obligations of Cohabitants Act 2010, on or following the ending of a relationship between cohabitants, either of the cohabitants concerned disposes of an asset to the other cohabitant, then, subject to subsections (2) and (3), both cohabitants shall be treated for the purposes of the Capital Gains Tax Acts as if the asset was acquired from the cohabitant making the disposal for a consideration of such amount as would secure that on the disposal neither a gain nor a loss would accrue to the cohabitant making the disposal. (2)Subsection (1) shall not apply where the cohabitant who acquired the asset could not be taxed in the State for the year of assessment in which the acquisition took place, in respect of a gain on a subsequent disposal in that year by that cohabitant of the asset, if that cohabitant had made such a disposal and a gain accrued on the disposal. (3)Subsection (1) shall not apply if until the disposal the asset formed part of the trading stock of a trade carried on by the cohabitant making the disposal or if the asset is acquired as trading stock for the purposes of a trade carried on by the cohabitant acquiring the asset. (4)Where subsection (1) applies in relation to a disposal of an asset by a cohabitant to the other cohabitant, then, in relation to a subsequent disposal of the asset (not being a disposal to which subsection (1) applies), the cohabitant making the disposal shall be treated for the purposes of the Capital Gains Tax Acts as if the other cohabitant's acquisition or provision of the asset had been the acquisition or provision of the asset by the cohabitant who made the disposal.

Section 88A CATCA03 Certain transfers by qualified cohabitants.
Notwithstanding any other provision of this Act, a gift or inheritance taken by virtue or in consequence of an order made under Part 15 of the Civil Partnership and Certain Rights and Obligations of Cohabitants Act 2010 by a qualified cohabitant, within the meaning of that Act, is exempt from tax and is not taken into account in computing tax.