

Corporation tax: restriction of relief for losses in farming or market gardening

Part 23 Chapter 1

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Contents

1. Introduction.....	2
2. Commercial activity.....	2
3. Expectation of profit.....	2
4. Potential for making profit.....	3
5. Ancillary to a larger trade.....	4
6. Commenced within three years.....	4
7. Anti-avoidance.....	5
8. Losses.....	6



1. Introduction

This manual outlines how the provisions of section 663 operate to deny relief from corporation tax to companies operated by "hobby" farmers and market gardeners, in the same way as relief from income tax is denied to individuals by section 662.

2. Commercial activity

Section 663 provides that relief under section 396(2) (see par. 9 of Tax Instruction 12.3.1) is not to be given for any loss incurred by a Company in carrying on in the State a trade of farming or market gardening -

- (a) unless it is shown that, for the accounting period of the loss, the trade was being carried on a commercial basis and with a view to the realisation of profits (see par. 2),

Or

- (b) if a loss, computed without regard to capital allowances (see below), was incurred in carrying on that trade in -
 - (I) the accounting period, and
 - (II) each of the accounting periods wholly or partly comprised in the three years prior to the accounting period (see par. 3).

For the purposes of the test at sub-head (b) above, losses are to be computed on Case I principles, and without regard to capital allowances and charges (notwithstanding section 307). Hence, the normal relief will not be prohibited merely because, either in the accounting period of claim or in any of the other relevant accounting periods, a profit has been converted into a loss for corporation tax purposes by the deduction of capital allowances; and, conversely, the relief will be prohibited even though the loss is converted into a profit by the addition of a balancing charge.

N.B. The factual test at sub-head (b) above is an alternative to, and to be applied independently of, the test at (a) above.

3. Expectation of profit

The object of section 663 is to deny relief from corporation tax to companies operated by "hobby" farmers and market gardeners, in the same way as relief from income tax is denied to individuals by section 662. It is not aimed at companies which are genuinely trading. Accordingly, section 663(2)(c) provides that the fact that the trade was being carried on so as to afford a reasonable expectation of profit is to be conclusive evidence that it was being carried on with a view to the realisation of profits.

4. Potential for making profit

The strict application of section 663, is further modified by subsection (2) (d) to meet the genuine case of a Company carrying on farming, etc., which engages in a special kind of undertaking which is potentially profit-making but cannot be expected to show a profit before the end of the accounting period of claim. For instance, it might take three years (or more) to regenerate marginal land, or to build up a stud farm.

Section 663(2)(d), provides that the relief is not to be denied if the company can show that -

- (a) the whole of its farming or market-gardening activities in the accounting period of claim are -

- (I) of such a nature, and

- (II) carried on in such a way

- as would have justified a reasonable expectation of the realisation of profits in the future if they had been undertaken by a competent farmer or market gardener, but that

- (b) if that competent farmer or market gardener had undertaken those activities at the beginning of the "prior period of loss", he could not reasonably have expected the activities to become profitable until after the end of the year following the prior period of loss.

(Subsection (1) defines the "prior period of loss" as, in effect, the last three years before the beginning of the accounting period of claim plus any earlier periods which together with those three years make up a consecutive sequence of loss-making accounting periods.)

Where a claimant company relies on section 663(2)(d), the whole of its farming or market gardening activities are to be taken into consideration. Thus, where a genuine long-term activity, e.g. the breeding of pedigree cattle, is combined with loss-making general farming, the relief is to be denied.



The onus of proof is laid entirely on the company which must show that the nature of its activities is such as to provide a reasonable expectation of profit in the future, i.e., any activities which, however efficiently carried on, could never show a profit do not qualify. In addition, the company must show that the activities are carried on in the way which would be expected of a competent farmer or market gardener working his land commercially and with a reasonable expectation of profit. To satisfy the condition set out in sub-head (b) above, the company should produce evidence as to the normal period of years during which a competent farmer or market gardener, engaged in the same type of long-term farming or gardening activity as itself, would be expected to show initial losses before his operations reached a profit-making level.

Any case in which relief is claimed under section 663(2)(d) will need to be considered on its merits. Where there is a substantial doubt, or where difficulty arises, and, in any case, before a claim is listed for hearing by the Appeal Commissioners, a report should be made to Head Office.

5. Ancillary to a larger trade

Section 663(2)(e), provides that relief is not to be denied under the section, where the loss-making farm or market garden is part of, and ancillary to, a larger trading undertaking. This provision is designed to meet cases such as that of a company which makes a practice of fattening bullocks for its butcher business, or a manufacturing company which grows its own raw materials or a seed merchanting or chemical manufacturing company which runs a farm for testing or improving its products.

6. Commenced within three years

Section 663, will not operate to deny relief under section 396(2) where the company's trade of farming or market gardening was set up and commenced within the period of three years before the beginning of the accounting period for which relief is claimed. Where, however, the company succeeded to the trade and, by virtue of section 400(6) (company reconstructions without change of ownership - see Tax Instruction 12.3.4), the predecessor's trade has not been treated as discontinued for the purposes of capital allowances and charges, the trade is to be regarded as a continuous trade: the restriction of relief for losses under section 663(2), will not then be prevented.

7. Anti-avoidance

Section 663(5), is an anti-avoidance provision designed to prevent the securing of more than one run of three years by transfers of farms between connected persons. Where there has been a change in the persons carrying on a trade of farming or market gardening, the application of the section is not to be affected by the change in relation to any person who was engaged in carrying on the trade immediately before and immediately after the change; and for this purpose persons "connected" with each other within the meaning of section 10, are to be treated as if they were the same person.

Thus, for example, if a company is under the control (see below) of an individual and -

(a) his (or her) spouse, or

(b) a relative (see below) of either, or

(c) the spouse of such a relative,

or of any or all of these "connected persons", and if

(a) the company's trade of farming or market gardening is transferred to any or all of them or

(b) such a trade is transferred by any or all of them to the company,

the trade will be regarded, for the purposes of section 663, as continuous and subsection (3) will not apply.

In this connection -

(I) "control" has by virtue of section 10(1) the meaning given by section 432, in the case of a "close" company (see par. 13 et seq. of Tax Instruction 13.1.1).

(II) "relative" means brother, sister, ancestor or lineal descendant.

Where a trade of farming or market gardening is, or falls to be treated as being carried on for part only of an accounting period (because the trade was commenced or discontinued or both within that period), section 663(2) will operate in relation to the trade for that part of the accounting period.

8. Losses

The carry-forward of losses incurred in farming or market gardening is not restricted by section 663. A company which has carried on farming unsuccessfully for a number of years is still entitled to carry forward all unused Case I farming losses for use against farming profits of subsequent periods.