BUSINESS TAX

155. CHANGES TO FARMERS' AVERAGING

With effect from the 2016/17 tax year, farmers now have the choice as to whether they average their profits over five years, two years or not at all, instead of averaging either over two years or none under the old rules. Following the uncertainty within the farming industry created by Brexit, this can be seen as a positive.

When averaging was first introduced in 1978, it was seen as providing relief for fluctuating profits. At the time, farmers and their advisers were quite conscious of the effects of the very hot summer of 1976, which was a joy for many in the UK but an expensive drought for the farming industry.

The changes to the averaging legislation made by clause 255, Finance Bill 2016 are being incorporated into ss221-225, Income Tax (Trading and Other Income) Act 2005, with most of the rules for the additional five-year option included in a new s222A ('Circumstances in which claim for five-year averaging may be made'). For individuals who have been in business for fewer than five years, only the option of two-year averaging is available until they have established a five-year trading history, excluding the tax year of commencement.

An averaging claim cannot be made in the year of commencement or of cessation of a trade. It is important to note that this includes individual partners joining or leaving an existing partnership. Tax losses in a year are treated as nil profits for the averaging calculation, with the loss available to offset in the normal way.

In theory, averaging what are in many cases miserly farming profits of recent years with what were possibly far more prosperous previous years has the potential to create some worthwhile tax advantage. However, for some farmers who have to pay for the necessary work in order to make the decision, the whole process may seem a potentially long and tedious journey for little tax reward.

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