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Investment Expenses and Deductibility: Segregated Funds

Questions frequently come up regarding how expenses associated with an investment fund are treated for deduction purposes on income tax returns. There are four general categories of expenses we can consider for non-registered investments. Any amounts that are paid for services in connection with a registered retirement savings plan (RRSP) or registered retirement income fund (RRIF) are expressly non-deductible under the Income Tax Act (Canada).

Acquisition fees for segregated funds include any portion of the "premium" or deposit that is not invested in the fund. That definition, found under ss 138.1(6) of the Income Tax Act (Canada), extends to what some refer to as insurance fees, used to provide some death and/or maturity benefit. It also includes commissions and surrender charges.

These portions of the deposit are not deductible when the customer sets up the policy. They do not add to the adjusted cost base of the policy. These monies are treated as a capital loss when the policyholder surrenders the policy, reducing the capital gain or increasing the capital loss on disposition.

Annual investment management fees are charged to segregated funds and are generally not deductible by the investor. The insurance company handling the investments treat these fees as fund expenses. The fees are deducted from the income earned in the fund before that income is allocated to investors. The end result is the same as if the investor had been able to deduct a pro rata portion of these fees with the benefit that the insurance company has done all the calculations, simplifying reporting by the investor.

Fees paid for investment advice and services may be deductible provided they do not include commissions. The advice may cover the relative merits of buying or selling an investment and services provided to administer or manage the investments. The advisor providing these services must do so as a principal business. General planning and counselling are normally not deductible by the investor.

Deducting interest on money borrowed to invest in segregated funds is possible through the application of ss 20(2.2) of the Income Tax Act (Canada). The usual rules applying to interest deductibility will govern money borrowed to invest in segregated funds, i.e. expenses incurred for the purpose of earning income from a business or property.

Our Tax, Retirement & Estate Planning support covers seminar education, workshops advanced concept illustrations & technical support including articles and reference material.

Peter A. Wouters focuses on tax & estate planning, retirement, and guidance for related investment product strategies.

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