TD 95/60 - Income tax: are fees paid for obtaining investment advice an allowable deduction under subsection 51(1) of the Income Tax Assessment Act 1936 ('the Act')for taxpayers who are not carrying on an investment business?

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Australian Taxation Office

Taxation Determination TD 95/60

Taxation Determination

Income tax: are fees paid for obtaining investment advice an allowable deduction under subsection 51(1) of the *Income Tax Assessment Act 1936* ('the Act')for taxpayers who are not carrying on an investment business?

1. When a taxpayer seeks advice in relation to the most appropriate investment or investments to make, the taxpayer may participate with an investment adviser in developing an investment plan. In many cases there will be a continuing relationship with the investment adviser. A fee is payable for drawing up a plan. A 'management fee' or 'annual retainer' is payable if advice is provided over the period of the investment(s), usually upon an annual or semi-annual review of the performance of the investment(s).

2. In discussing what makes expenditure deductible under subsection 51(1), Lockhart J said in *F C of T v. Cooper* 91 ATC 4396; 21 ATR 1616 (at ATC 4399, ATR 1620):

> 'The phrase "incurred in gaining or producing assessable income" in the first limb of s. 51(1) has been construed to mean incurred in the course of gaining or producing assessable income...
>
> 'For expenditure to be an allowable deduction as an outgoing incurred in gaining or producing the assessable income, it must be incidental and relevant to that end; ... This test of deductibility has been explained in subsequent judgments of the High Court, so that to be deductible the expenditure must be incidental and relevant in the sense of having the essential character of expenditure incurred in the course of gaining or producing assessable income ... The essential character test is also applied to determine if the expenditure is of a capital, private or domestic nature...'

3. In view of the above, we do not think that the fee for drawing up the plan is deductible for income tax purposes. This is because it is not expenditure incurred in the course of gaining or producing the assessable income from the investment(s). It is too early in time to be an expense that is part of the income producing process. It is an expense that is associated with putting the income earning investment(s) in place, in the same way as certain kinds of investments attract entry fees, and has, therefore, an insufficient connection with earning income from the investment(s). See *F C of T v. Maddalena* 71 ATC 4161; (1971) 2 ATR 541 and the discussion of that case by Hill J in *Cooper*, (supra) at ATC 4412, ATR 1635.

4. Expenditure on drawing up the plan is incidental and relevant to **outlaying the price of acquiring the investment(s)**, and is so associated with the making of the investment(s) as to warrant the conclusion that it is capital or capital in nature: see *Sun Newspapers v. Federal Commissioner of Taxation* 5 ATD 87 per Dixon J especially at ATD 95. The expenditure may qualify as an incidental cost to the taxpayer of the acquisition of the assets(s) [i.e., the investment(s)] for capital gains tax purposes. See subsections 160ZH(1) and 160ZH(5) of the Act.

5. On-going management fees or retainers are deductible under subsection 51(1). In Taxation Ruling IT 39 we discussed expenditure incurred in 'servicing' an investment portfolio. The Ruling discussed the decision in *F C of T v. Green* (1950) 81 CLR 313 which allowed a taxpayer a deduction in relation to the management of the income producing enterprises of the taxpayer. The Ruling concluded that expenditure in 'servicing' the portfolio should be regarded as incurred in relation to the management of income producing investments and thus as having an intrinsically revenue character. However, to be wholly deductible, all of a management fee must relate to gaining or producing assessable income. If the advice covers other matters or relates in part to investments that do not produce assessable income, only a proportion of the fee is deductible.

6. Over the period of an investment plan advice may be received suggesting changes be made to the mix of investments held. This would normally be part and parcel of managing the investments in accordance with the plan. This advice may be from the original investment adviser or from a new adviser. Provided the advice is not in relation to drawing up an investment plan it will be an allowable deduction as set out in paragraph 5 above.

7. We have been asked what is the position where a taxpayer has existing investments and goes to an investment adviser to draw up an investment plan. For example, a taxpayer nearing retirement may have a number of small investments, is expecting a superannuation payment (eligible termination payment (ETP)) and decides to put in place a long term financial strategy incorporating the investments arising from the ETP. In our view, a fee paid to an investment adviser to draw up an investment plan in these circumstances would be a capital outlay even if some or all of the pre-existing investments were maintained as part of the plan. This is because the fee is for advice that relates to drawing up an investment plan. The character of the outgoing is not altered because the existing investments fit in with the plan. It is still an outgoing of capital for the same reasons as set out in paragraphs 3 and 4 above.

Commissioner of Taxation
06/12/95

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