Rev. Rul. 75-410, 1975-2 C.B. 446

Private foundation; audit fees. Audit fees paid by an exempt private foundation must be apportioned between its investment and exempt activities and only that portion of the fees attributable to the investment activities is deductible in computing the foundation's net investment income under section 4940(c) of the Code.

Advice has been requested whether, under the circumstances described below, audit fees paid by a private foundation exempt from Federal income tax under section 501(c)(3) of the Internal Revenue Code of 1954 are deductible in full in computing the foundation's net investment income under section 4940(c).

The private foundation's income is derived from investments and is distributed exclusively for charitable purposes. The foundation retains an accounting firm to perform an annual audit of its financial records.

Section 4940(a) of the Code imposes on each private foundation exempt from taxation under section 501(a) a tax equal to 4 percent of the net investment income of such foundation for the taxable year.

Section 4940(c)(3) of the Code provides that in the computation of allowed as a deduction from gross allowed as a deduction from gross investment income all the ordinary and necessary expenses paid or incurred for the production or collection of gross investment income or for the management, conservation, or maintenance of property held for the production of such income.

Section 53.4940-1(e)(1) of the Foundation Excise Tax Regulations indicates that expenses paid or incurred for exempt activities are not deductible in computing net investment income.

The annual audit of the foundation's financial records involves an examination of both the income and expenses attributable to investment activities and distributions in furtherance of exempt purposes. Only that part of the audit fee attributable to examination of investment income and expenses is deductible under section 4940(c)(3) of the Code as an amount paid or incurred for the production or collection of gross investment income or for the management, conservation, or maintenance of property held for the production of such income. Accordingly, the audit fees paid by the foundation must be apportioned between the investment activity and the exempt activity, and, therefore, are not deductible in full in computing its net investment income under section 4940(c) of the Code.