

Example (3). Assume the facts as stated in Example (1), except that Y removes \$2,000 of the investment from jeopardy within the taxable period, with X refusing to agree to the removal from jeopardy of the remaining \$3,000 of such investment. Y will be liable for an additional tax of \$750, imposed upon the portion of the investment which has not been removed from jeopardy within the taxable period (i.e., $\$3,000 \times 25\%$). Further X will be liable for an additional tax of \$150, also imposed upon the same portion of the investment (i.e., $\$3,000 \times 5\%$).

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§ 53.4944-3 Exception for program-related investments.

(a) *In general.* (1) For purposes of section 4944 and §§ 53.4944-1 through 53.4944-6, a “program-related investment” shall not be classified as an investment which jeopardizes the carrying out of the exempt purposes of a private foundation. A *program-related investment* is an investment which possesses the following characteristics:

(i) The primary purpose of the investment is to accomplish one or more of the purposes described in section 170(c)(2)(B);

(ii) No significant purpose of the investment is the production of income or the appreciation of property; and

(iii) No purpose of the investment is to accomplish one or more of the purposes described in section 170(c)(2)(D).

(2)(i) An investment shall be considered as made primarily to accomplish one or more of the purposes described in section 170(c)(2)(B) if it significantly furthers the accomplishment of the private foundation’s exempt activities and if the investment would not have been made but for such relationship between the investment and the accomplishment of the foundation’s exempt activities. For purposes of section 4944 and §§ 53.4944-1 through 53.4944-6, the term *purposes described in section 170(c)(2)(B)* shall be treated as including purposes described in section 170(c)(2)(B) whether or not carried out by organizations described in section 170(c).

(ii) An investment in an activity described in section 4942(j)(5)(B) and the regulations thereunder shall be considered, for purposes of this paragraph, as made primarily to accomplish one or

more of the purposes described in section 170(c)(2)(B).

(iii) In determining whether a significant purpose of an investment is the production of income or the appreciation of property, it shall be relevant whether investors solely engaged in the investment for profit would be likely to make the investment on the same terms as the private foundation. However, the fact that an investment produces significant income or capital appreciation shall not, in the absence of other factors, be conclusive evidence of a significant purpose involving the production of income or the appreciation of property.

(iv) An investment shall not be considered as made to accomplish one or more of the purposes described in section 170(c)(2)(D) if the recipient of the investment appears before, or communicates to, any legislative body with respect to legislation or proposed legislation of direct interest to such recipient, provided that the expense of engaging in such activities would qualify as a deduction under section 162.

(3)(i) Once it has been determined that an investment is “program-related” it shall not cease to qualify as a “program-related investment” provided that changes, if any, in the form or terms of the investment are made primarily for exempt purposes and not for any significant purpose involving the production of income or the appreciation of property. A change made in the form or terms of a program-related investment for the prudent protection of the foundation’s investment shall not ordinarily cause the investment to cease to qualify as program-related. Under certain conditions, a program-related investment may cease to be program-related because of a critical change in circumstances, as, for example, where it is serving an illegal purpose or the private purpose of the foundation or its managers. For purposes of the preceding sentence, an investment which ceases to be program-related because of a critical change in circumstances shall in no event subject the foundation making the investment to the tax imposed by section 4944(a)(1) before the 30th day after the date on which such foundation (or any of its

managers) has actual knowledge of such critical change in circumstances.

(ii) If a private foundation changes the form or terms of an investment, and if, as a result of the application of subdivision (i) of this subparagraph, such investment no longer qualifies as program-related, the determination whether the investment jeopardizes the carrying out of exempt purposes shall be made pursuant to the provisions of § 53.4944-1(a)(2).

(b) *Examples.* The provisions of this section may be illustrated by the following examples:

Example (1). X is a small business enterprise located in a deteriorated urban area and owned by members of an economically disadvantaged minority group. Conventional sources of funds are unwilling or unable to provide funds to X on terms it considers economically feasible. Y, a private foundation, makes a loan to X bearing interest below the market rate for commercial loans of comparable risk. Y's primary purpose for making the loan is to encourage the economic development of such minority groups. The loan has no significant purpose involving the production of income or the appreciation of property. The loan significantly furthers the accomplishment of Y's exempt activities and would not have been made but for such relationship between the loan and Y's exempt activities. Accordingly, the loan is a program-related investment even though Y may earn income from the investment in an amount comparable to or higher than earnings from conventional portfolio investments.

Example (2). Assume the facts as stated in Example (1), except that after the date of execution of the loan Y extends the due date of the loan. The extension is granted in order to permit X to achieve greater financial stability before it is required to repay the loan. Since the change in the terms of the loan is made primarily for exempt purposes and not for any significant purpose involving the production of income or the appreciation of property, the loan shall continue to qualify as a program-related investment.

Example (3). X is a small business enterprise located in a deteriorated urban area and owned by members of an economically disadvantaged minority group. Conventional sources of funds are unwilling to provide funds to X at reasonable interest rates unless it increases the amount of its equity capital. Consequently, Y, a private foundation, purchases shares of X's common stock. Y's primary purpose in purchasing the stock is to encourage the economic development of such minority group, and no significant purpose involves the production of income or the appreciation of property. The investment

significantly furthers the accomplishment of Y's exempt activities and would not have been made but for such relationship between the investment and Y's exempt activities. Accordingly, the purchase of the common stock is a program-related investment, even though Y may realize a profit if X is successful and the common stock appreciates in value.

Example (4). X is a business enterprise which is not owned by low-income persons or minority group members, but the continued operation of X is important to the economic well-being of a deteriorated urban area because X employs a substantial number of low-income persons from such area. Conventional sources of funds are unwilling or unable to provide funds to X at reasonable interest rates. Y, a private foundation, makes a loan to X at an interest rate below the market rate for commercial loans of comparable risk. The loan is made pursuant to a program run by Y to assist low-income persons by providing increased economic opportunities and to prevent community deterioration. No significant purpose of the loan involves the production of income or the appreciation of property. The investment significantly furthers the accomplishment of Y's exempt activities and would not have been made but for such relationship between the loan and Y's exempt activities. Accordingly, the loan is a program-related investment.

Example (5). X is a business enterprise which is financially secure and the stock of which is listed and traded on a national exchange. Y, a private foundation, makes a loan to X at an interest rate below the market rate in order to induce X to establish a new plant in a deteriorated urban area which, because of the high risks involved, X would be unwilling to establish absent such inducement. The loan is made pursuant to a program run by Y to enhance the economic development of the area by, for example, providing employment opportunities for low-income persons at the new plant, and no significant purpose involves the production of income or the appreciation of property. The loan significantly furthers the accomplishment of Y's exempt activities and would not have been made but for such relationship between the loan and Y's exempt activities. Accordingly, even though X is large and established, the investment is program-related.

Example (6). X is a business enterprise which is owned by a nonprofit community development corporation. When fully operational, X will market agricultural products, thereby providing a marketing outlet for low-income farmers in a depressed rural area. Y, a private foundation, makes a loan to X bearing interest at a rate less than the rate charged by financial institutions which have agreed to lend funds to X if Y makes

the loan. The loan is made pursuant to a program run by Y to encourage economic redevelopment of depressed areas, and no significant purpose involves the production of income or the appreciation of property. The loan significantly furthers the accomplishment of Y's exempt activities and would not have been made but for such relationship between the loan and Y's exempt activities. Accordingly, the loan is a program-related investment.

Example (7). X, a private foundation, invests \$100,000 in the common stock of corporation M. The dividends received from such investment are later applied by X in furtherance of its exempt purposes. Although there is a relationship between the return on the investment and the accomplishment of X's exempt activities, there is no relationship between the investment per se and such accomplishment. Therefore, the investment cannot be considered as made primarily to accomplish one or more of the purposes described in section 170(c)(2)(B) and cannot qualify as program-related.

Example (8). S, a private foundation, makes an investment in T, a business corporation, which qualifies as a program-related investment under section 4944(c) at the time that it is made. All of T's voting stock is owned by S. T experiences financial and management problems which, in the judgment of the foundation, require changes in management, in financial structure or in the form of the investment. The following three methods of resolving the problems appear feasible to S, but each of the three methods would result in reduction of the exempt purposes for which the program-related investment was initially made:

(a) *Sale of stock or assets.* The foundation sells its stock to an unrelated person. Payment is made in part at the time of sale; the balance is payable over an extended term of years with interest on the amount outstanding. The foundation receives a purchase-money mortgage.

(b) *Lease.* The corporation leases its assets for a term of years to an unrelated person, with an option in the lessee to buy the assets. If the option is exercised, the terms of payment are to be similar to those described in (a) of this example.

(c) *Management contract.* The corporation enters into a management contract which gives broad operating authority to one or more unrelated persons for a term of years. The foundation and the unrelated persons are obligated to contribute toward working capital requirements. The unrelated persons will be compensated by a fixed fee or a share of profits, and they will receive an option to buy the stock held by S or the assets of the corporation. If the option is exercised, the terms of payment are to be similar to those described in (a) of this example.

Each of the three methods involves a change in the form or terms of a program-related investment for the prudent protection of the foundation's investment. Thus, under § 53.4944-3(a)(3)(i), none of the three transactions (nor any debt instruments or other obligations held by S as a result of engaging in one of these transactions) would cause the investment to cease to qualify as program-related.

Example (9). X is a socially and economically disadvantaged individual. Y, a private foundation, makes an interest-free loan to X for the primary purpose of enabling X to attend college. The loan has no significant purpose involving the production of income or the appreciation of property. The loan significantly furthers the accomplishment of Y's exempt activities and would not have been made but for such relationship between the loan and Y's exempt activities. Accordingly, the loan is a program-related investment.

Example (10). Y, a private foundation, makes a high-risk investment in low-income housing, the indebtedness with respect to which is insured by the Federal Housing Administration. Y's primary purpose in making the investment is to finance the purchase, rehabilitation, and construction of housing for low-income persons. The investment has no significant purpose involving the production of income or the appreciation of property. The investment significantly furthers the accomplishment of Y's exempt activities and would not have been made but for such relationship between the investment and Y's exempt activities. Accordingly, the investment is program-related.

§ 53.4944-4 Special rules.

(a) *Joint and several liability.* In any case where more than one foundation manager is liable for the tax imposed under section 4944 (a)(2) or (b)(2) with respect to any one jeopardizing investment, all such foundation managers shall be jointly and severally liable for the tax imposed under each such paragraph with respect to such investment.

(b) *Limits on liability for management.* With respect to anyone jeopardizing investment, the maximum aggregate amount of tax collectible under section 4944(a)(2) from all foundation managers shall not exceed \$5,000, and the maximum aggregate amount of tax collectible under section 4944(b)(2) from all foundation managers shall not exceed \$10,000.

(c) *Examples.* The provisions of this section may be illustrated by the following examples: