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Private Foundations Bulletin

Program-Related Investments: An Opportunity to Leverage Philanthropic Dollars

Traditionally, private foundations have been associated with grant-making; however, foundations may utilize other alternatives to carry out their charitable mission and meet distribution requirements. Program-Related Investments (PRIs) are one such alternative. The primary purpose of a PRI is to accomplish one or more of the foundation's exempt purpose as defined by the Internal Revenue Service (IRS).

PRIs can take the form of alternative methods of financing (i.e., unsecured loans, bonds, mortgages, etc.), equity investments (private equity), etc. Through their use, the recipient gains access to capital at lower rates or cost potentially at an amount greater than a typical grant. The foundation can expect a nominal return of equity or repayment of capital which can be reinvested or granted for another future charitable purpose.

Examples of PRIs

The following are a few typical examples of program-related investments as provided by the IRS:

- Low-interest or interest-free loans to needy students,
- High-risk investments in nonprofit low-income housing projects,
- Low-interest loans to small businesses owned by members of economically disadvantaged groups, where commercial funds at reasonable interest rates are not readily available,
- Investments in businesses in low-income areas (both domestic and foreign) under a plan to improve the economy of the area by providing employment or training for unemployed residents, and
- Investments in nonprofit organizations combating community deterioration.

Historically, many foundations have shied away from PRIs because either they seem too complex or they are unfamiliar with the tax reporting requirements. However, PRIs are garnering attention in the foundation community, as they provide the opportunity to leverage philanthropic dollars for greater social impact. While PRIs need not be a sole strategy – when used to complement effective grant-making – a foundation may be able to more efficiently advance their charitable purpose and have a long-term impact.

Tax Considerations

The following presents some of the considerations that should be taken into account in regard to PRIs:

- When a foundation enters in a PRI, the amount is deemed a qualifying distribution when expended. In the year the PRI is repaid to the foundation, the repayment is calculated as a reduction of the foundation’s qualified distributions. Therefore, the timing of when PRIs are expended and repaid should be monitored to ensure that the foundation remains in compliance with minimum distribution requirements.
- PRIs typically require a higher level of due diligence than a simple grant-making program and some require the exercise of expenditure responsibility (i.e., PRIs that are commercial ventures).
- PRIs require additional disclosures on the Form 990-PF.
- PRIs are considered a charitable-use asset and, therefore, are not included in the mandatory distribution calculation.
- PRIs cannot be used to fund political activities or influence legislation as part of its charitable purpose.
- PRIs are exempt from the excess business holdings tax which is generally imposed for investments

that comprise more than 20 percent interest in for-profit ventures as well the investment tax which is generally imposed for investments that financially endanger the charitable work of the foundation.

In Conclusion

While PRIs may not be ideal for all foundations, they may be worth considering in connection with a foundation's grant-making program to further its purpose and mission.

Contact Us

We welcome the opportunity to answer any questions you may have related to this topic or any other accounting, audit, tax or advisory matters relative to private foundations. Please call 212.286.2600 or email any of the Private Foundation Services team members below:

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