

FREQUENTLY ASKED QUESTIONS ABOUT GRANTMAKING

A Resource for Grantmaking Organizations

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This information is provided by Ask CMF, a technical assistance service of the Council of Michigan Foundations, for educational purposes only and does not constitute legal advice.

This resource provides guidance for foundations on making grants to a variety of institution types, informed by frequently asked questions submitted via Ask CMF.

While grantmakers are automatically allowed to make grants to public charities (501(c)(3) organizations), they may or may not have the infrastructure in place to make grants to other institutions, such as businesses, individuals or other non-501(c)(3) organizations. Some of the categories of grantmaking described in this resource are relatively rare or impermissible for certain types of grantmakers, as designated in the comparative chart and descriptive sections of this document.

Grantmakers seeking additional information about the grantmaking process and related due diligence should reference CMF's resource, "[The Basics of the Grantmaking Process and Due Diligence.](#)" Those needing additional information about creating applications and other grantmaking process documents should use CMF's resource, "[Grantmaking With Purpose: Sample Documents for Grantmakers.](#)"

Before using this resource, please note:

- All grants, regardless of the recipient organization's type, must be used for distinctly charitable purposes. The charitability of some grant categories, such as economic development, are construed narrowly by the IRS.
- Grantmakers should verify that they are permitted to make grants to organizations other than 501(c)(3) organizations within their incorporation documents (articles and bylaws). In some cases, grantmakers may be restricted to making grants to only 501(c)(3) organizations or under restricted circumstances, based on their founding documents or related policies.
- Please consult with qualified counsel prior to moving forward with one of these "unusual" grant categories, as the facts and circumstances of the grant may significantly impact whether it is considered allowable.

Disqualified Persons

This document will at times reference important considerations for grantmaking in regard to disqualified persons. For example, grants from private foundations can be used to support non-501(c)(3) organizations, but among the guidelines and restrictions in such grantmaking are clear rules that those grants cannot create a direct, tangible benefit back to a disqualified person. The definitions for disqualified persons differ for private foundations and public charities, as explained below.

Private foundations: [IRC Section 4946](#) provides a list of disqualified persons with respect to a private foundation:

1. Substantial contributors;
2. Foundation managers;
3. Owner of more than 20% interest of certain organizations that are substantial contributors;
4. Family members* of persons described above (in 1-3);
5. Corporations in which persons described above (in 1-4) hold more than a 35% voting power;
6. Partnerships in which persons described above (in 1-4) hold more than a 35% profit interest;
7. Trusts or estates in which persons described above (in 1-4) hold more than a 35% beneficial interest;
8. Certain private foundations which are effectively controlled by the person or persons in control of the foundation in question; and
9. Governmental officials.

Public charities: [IRC Section 4958](#) provides a list of disqualified persons with respect to transactions involving public charities:

1. Any person who was (within 5 years of a transaction) in a position to exercise substantial influence over the affairs of the organization;
2. A family member* of those described above (in 1);
3. A 35%-controlled entity;
4. Anyone described above (in 1-3) with respect to a 509(a)(3) supporting organization for a tax-exempt organization;
5. Regarding donor advised funds (as described in section [4966\(d\)\(2\)](#)), donors and donor advisors described in [IRC Section 4958\(f\)\(7\)](#); and
6. Regarding sponsoring organizations (described in section [4966\(d\)\(1\)](#)), investment advisors described in [IRC Section 4958\(f\)\(8\)](#).

*Note that the definition of who constitutes a “family member” differs between IRC sections 4946 and 4958. In the case of private foundations, family members are based on ancestry and lineal descendants, whereas public charities (for excess benefit transactions) also includes siblings.

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COMPARATIVE GRANTMAKING BY ORGANIZATION TYPE

This section provides a brief synopsis of the rules and regulations applicable to a variety of grantmakers and grant recipients. Here and throughout this resource, there are important distinctions highlighted among the four primary types of grantmaking structures:

- **Private Foundations:** (Notated within the text in GREY) This category includes family foundations, independent foundations, corporate foundations and other grantmaking entities that are required to follow private foundation requirements set by the IRS because they do not meet the public support test under Internal Revenue Code (IRC) 509(a).
- **Community Foundations and Other Public Charitable Entities:** (Notated in ORANGE) This category includes community foundations, university and community college foundations and other nonprofit organizations.
- **Corporate Giving Programs:** (Notated in DARK BLUE) This category includes internal philanthropy programs of corporations, banks, credit unions and other corporate entities. Corporations and related entities engaged in philanthropic activities should consult with legal counsel, as industry-specific rules and regulations may vary.
- **Donor Advised Funds (DAFs):** (Notated in TEAL) This category includes donor advised funds held by community foundations and other public charities. Advisors may recommend grants be made out of their fund, with the approval of the sponsoring organization. These funds have unique rules and regulations under the Internal Revenue Code.

For more detail about these categories of activity, see the section, “[Grantmaking to Recipient Types](#).” For information regarding [expenditure responsibility](#), [equivalency determination](#), and other key terms relevant to specific categories of grantmaking organizations, see the section, “[Grants Management](#).”

	Community Foundations and Other Public Charities	Private Foundations	Corporate Giving Programs	Donor Advised Funds
Grants to 501(c)(3) Public Charities	Allowable.	Allowable.	Allowable and deductible.	Allowable.

Grants to Private Foundations	Considered very unusual and not recommended.	Allowable only with expenditure responsibility (and mandatory spend through if grant is to “count” toward 5% minimum distribution). Considered relatively unusual in the field.	Allowable and deductible.	Allowable with expenditure responsibility and so long as there is no control by the donor, advisor or their family members, however this is considered generally inadvisable in the field. Many DAF sponsors refuse to make grants to private non-operating foundations.
Grants to Donor Advised Funds	Allowable, although rare.	Currently allowable, although regulation may require pay-through to count toward the 5% payout. Must list DAF grants in 990-PF.	Allowable and deductible	Currently allowable, although regulation may change.
Grants to Businesses	Allowable with expenditure responsibility and so long as it is for a charitable purpose.	Allowable with Expenditure Responsibility (IRC 4945) and so long as it is for a charitable purpose.	Allowable, but could be subject to gift tax.	Allowable with Expenditure Responsibility (IRC 4945) and so long as it is for a charitable purpose.
Grants to Non-501(c)(3) Exempt Organizations¹	Allowable with expenditure responsibility and so long as it is for a charitable purpose.	Allowable with Expenditure Responsibility and so long as it is for a charitable purpose.	Allowable but could be subject to gift tax.	Allowable with expenditure responsibility and so long as it is for a charitable purpose.
Grants to Cemeteries	Potentially allowable, but the process depends on organizational type. Depends upon whether owned by	Potentially allowable, but the process depends on organizational type. Depends upon whether owned by	Potentially allowable. May or may not be deductible or subject to gift tax. Depends upon whether owned by	Potentially Allowable. Depends upon whether owned by municipality, 501(c)(13) or if for

¹ This category includes 501(c)(4) and 501(c)(6) organizations, among others.

	municipality, 501(c)(13), or if for private interests (unacceptable).	municipality, 501(c)(13), or if for private interests (unacceptable).	municipality, 501(c)(13), or if for private interests (unacceptable).	private interests (unacceptable) including benefits to Donors/Advisors. Expenditure Responsibility may be required.
Grants to Supporting Organizations²	Allowable.	Allowable, but may require Expenditure Responsibility.	Allowable.	Allowable, but may require Expenditure Responsibility.
Grants to Fiscal Sponsorships	Allowable, the same as other grants to public charities.	Allowable, but may require additional due diligence to ensure sufficient fiscal sponsor discretion and control.	Allowable, but may require additional due diligence or expenditure responsibility to be considered deductible, especially if will be transmitted internationally.	Allowable, but may require additional due diligence to ensure sufficient fiscal sponsor discretion and control.
Grants to Individuals/Scholarships	Community foundations and other public charities that manage scholarships typically use private foundation rules as the basis for best practice, although they do not need pre-approval by the IRS (unless limited to employees and former employees of a particular employer and funded by corporate foundation).	Can make grants to individuals and scholarships, however the IRS must pre-approve the scholarship procedures or else the scholarships will be deemed taxable expenditures.	Not a deductible contribution by the company unless donated to a charity to conduct the program itself (outside of corporate control). If scholarships are exclusive to employees, former employees, and their families, additional rules must be followed.	Not allowed to make contributions to individuals. However, this grant would be permitted in another type of fund at a sponsoring organization (such as a community foundation) so long as exemptions to the DAF definition provided in Internal Revenue Code (IRC) 4966 are followed.

² Note that supporting organizations are ineligible to receive funding from qualified charitable deductions (QCDs).

<p>Disaster Relief and Emergency Hardship</p>	<p>May establish a disaster relief program for individuals or host an employee hardship fund on behalf of a corporation, subject to significant rules (or an employer-sponsored DAF, but only for federally qualified disasters).</p>	<p>Private foundations can implement a disaster grantmaking strategy or use a discretionary grant to address general needs within the community. Self-dealing rules still apply, including restrictions on the disaster program generating business for the company or benefitting a disqualified person.</p> <p>May operate an employee disaster relief fund that provides employee disaster assistance for victims of federally qualified disasters only.</p> <p>It is not known with certainty whether a private foundation may fund an employee hardship program at an independent charity.</p>	<p>Can assist organizations as an extension of its standard grantmaking. In a federally qualified disaster, corporations may provide direct support (cash or in-kind with products and materials) to assist in disaster relief. Can assist individual employees via an Employee Assistance Program maintained by an independent charitable entity. In a federally-declared disaster, the corporation can provide disaster relief support directly to employees, subject to significant rules.</p>	<p>General rules for DAFs apply, including the ability to make grants in the case of federally qualified disasters.</p> <p>Not otherwise allowed to make contributions to individuals.</p>
<p>Grants to International Efforts</p>	<p>Allowable with expenditure responsibility.</p>	<p>Allowable with expenditure responsibility or equivalency determination. Alternatively, this can be achieved through an intermediary or “friends of” organization.</p>	<p>Not typically deductible (unless there is an applicable tax treaty – Canada, Israel, Mexico – and in that case may only offset taxable income in the corresponding country).</p>	<p>Allowable with expenditure responsibility or equivalency determination. Some DAF sponsors refuse to make international grants.</p>

Grants to Government Agency	Allowable, but there must be a charitable purpose.	Allowable, but there must be a charitable purpose.	Allowable, but there must be a charitable purpose.	Allowable, but there must be a charitable purpose.
Grants to Support Advocacy	Unlimited advocacy allowable. Lobbying is allowable as an “insubstantial part” of activities (or for expenditures, if made the 501(h) election).	Unlimited advocacy allowable. Private foundations may not earmark funds for lobbying, however private foundations may support other advocacy activities and support charities that lobby (either by general operations grants with an agreement that does not prohibit lobbying or as part of a project for the non-lobbying portion of the budget).	Contributions for purposes of lobbying are not charitable nor eligible for a charitable deduction.	DAF holders may not earmark funds for lobbying, however they may support other advocacy activities and support charities that lobby.
Grants to Federally Recognized Tribe	Allowable, if it is for a charitable purpose.	Allowable, if it is for a charitable purpose.	Allowable and deductible, if it is for a charitable purpose. Other situations may be explored on a case-by-case basis.	Allowable, if it is for a charitable purpose.
Event Sponsorships	Allowable.	Allowable. However, caution should be taken to avoid self-dealing. Donors should not receive a benefit for the foundation’s support of the event, although name recognition is permissible. Use of tickets only by Foundation directors, officers, and staff with no non-foundation guests.	Allowable and deductible for the company within the existing corporate sponsorship regulations. Quid Pro Quo portion of donation that is not deductible should be listed on the ticket/charitable acknowledgement. Potentially could choose to deduct as business expense.	There is a strict prohibition on DAF grants providing any benefit back to the donor or any advisor. The DAF sponsoring organization may prohibit payment of sponsorships where tickets are involved or may prohibit acceptance of tickets.

GRANTMAKING TO RECIPIENT TYPES

Can grants be made to support 501(c)(3) public charities?

Organizations may be created under a state's nonprofit legal structure (as opposed to being established as a for-profit business). However, these new organizations must apply to the Internal Revenue Service to receive an "exemption," which classifies them as a 501(c)(3) organization or else they will be nonprofit corporations that are subject to income tax as if they were regular corporations. These organizations will receive a letter of determination from the IRS and can be further researched via the [IRS Tax Exempt Organization Search Tool](#) and their completed Form 990 documents.

- **Private Foundations:** Private foundations are designed to use their grantmaking to support 501(c)(3) public charities, whether through programmatic, capital or operating support grants. The foundation's incorporation documents, bylaws and policy documents may include 501(c)(3) public charities as the default type of organization able to receive grants from the foundation. Grantmakers seeking to make grants to other types of organizations will need to check their documentation to determine if those grant expenditures are allowable.
- **Community Foundations and Other Public Charities:** See above explanation for private foundations.
- **Corporate Giving Programs:** See above explanation for private foundations. Grants to 501(c)(3) public charities are considered to be deductible.
- **Donor Advised Funds:** See above explanation for private foundations.

Can grants be made to support churches and other religious organizations?

Churches that meet certain criteria set by the IRS are automatically considered to be tax-exempt organizations, meaning they do not necessarily have their own IRS determination letter and are not required to file annual returns to the IRS (Form 990, etc.). They are also not required to secure a charitable solicitation license and therefore are exempt from the related rules for reviewed or audited financial statements. If a church or other religious organization does not have an IRS determination letter, a foundation would need to conduct additional due diligence prior to making a grant to this organization. For churches that are part of a known denomination, the foundation may be able to reference the denomination's letter of determination and a directory that lists all of the congregations affiliated with it. However, not all denominations have a letter of determination or directory.

- **Private Foundations:** Generally, a foundation can make grants to support churches and other religious organizations (synagogues, mosques, etc.). In some cases, a foundation may outline certain restrictions on providing grants to faith-based organizations.
- **Community Foundations and Other Public Charities:** Restrictions are program-specific or limit the use of publicly-raised gifts to make grants for non-sectarian activities of religious organizations, rather than supporting their primarily-religious functions.
- **Corporate Giving Programs:** This category of grants is generally uncommon; legal counsel should be sought prior to making this type of grant.

- **Donor Advised Funds:** The foundation can make grants for either religious or non-sectarian purposes, as long as there are no such restrictions within the foundation’s existing policies.

Can grants be made to support private foundations?

- **Private Foundations:** Private foundations can make grants to other non-operating, operating and exempt operating private foundations. However, this can only be achieved through the use of expenditure responsibility (see “[What is expenditure responsibility?](#)”) and requires a mandatory spend-through for the grant to “count” toward the foundation’s 5% minimum distribution, along with special tax elections made by the recipient private foundation. A private foundation making a grant to another private foundation is considered to be relatively unusual in the field and is a somewhat risky endeavor: If more than one private foundation grantmaker is involved, they may bear joint and several risk for failure to follow the rules to the letter.
- **Community Foundations and Other Public Charities:** Private foundations are not a typical grant recipient. While it may be possible that policy allows these grants under limited circumstances (i.e., grants to a private operating foundation), these grants are nonetheless unusual.

The Council on Foundations recommends against making grants to private, non-operating foundations because of the potential for a donor to utilize the community foundation to illegally circumvent private foundation rules. Also, as private foundations are typically more closely controlled, they are unlikely to be an optimal grant partner compared to other community-based organizations.

Typically, private foundations are not designed to accept contributions or grants from external parties. If they are interested in accepting external contributions, the organization would likely need to have a charitable solicitation license from the state of Michigan. Additionally, charitable deduction rules and related issues may differ from a public charity, resulting in less benefit for most individuals to make a contribution to a private foundation.

- **Corporate Giving Programs:** A grant to a (non-operating or operating) private foundation is allowable and deductible, although private foundation grants carry less generous deductibility limitations.
- **Donor Advised Funds:** A grant to a non-operating or operating private foundation is allowable. However, it requires expenditure responsibility (see “[What is expenditure responsibility?](#)”). Additionally, there can be no control by the donor, advisor or their family members. Generally, this type of grant is considered inadvisable in the field, and many DAF sponsoring organizations refuse to make grants to private, non-operating foundations.

Can grants be made to donor advised funds?

- **Private Foundations:** Private foundations are currently allowed to make grants to DAFs. However, forthcoming regulation may impact the allowable timing and grantmaking requirements for this type of activity. At the current time, DAF grants must be listed on the 990-

PF tax return. It is good practice to have them further advised by the end of the following year to avoid claims that the private foundation is using DAFs to avoid the 5% payout.

- **Community Foundations and Other Public Charities:** See above explanation for private foundations.
- **Corporate Giving Programs:** See above explanation for private foundations.
- **Donor Advised Funds:** Recent regulatory discussions have called attention to the phenomenon known as “DAF-to-DAF transfers.” These transfers take place between two DAF accounts held by the same or different DAF sponsoring organizations. See the box below for additional information.

DAF-to-DAF Transfers

DAF-to-DAF transfers are currently allowable, however forthcoming regulation may impact this practice in the future. As such, DAF-to-DAF transfers can be a questionable practice, especially as public scrutiny focuses on rare, anecdotal cases where a DAF grant ultimately returned to the account of the original donor or advisors, rather than benefiting charitable entities.

It is important to highlight that DAF-to-DAF transfers can and do serve important logistical and/or legal purposes within the field. The following are examples of such DAF-to-DAF transfers:

- If a local community foundation does not have the ability to accept a donor’s contribution of property (real estate, artwork, etc.), they may identify a separate DAF provider that does. A DAF-to-DAF transfer would be used, with one provider accepting the gift and then transferring it to the other provider in the form of a DAF, with the original donor serving as the primary advisor on the account. This structure permits the donor to utilize one organization’s infrastructure to accept gifts of property, while maintaining their DAF within their local community foundation.
- If a donor opens a DAF account within their local community foundation, but then relocates, they may request that their DAF account be transferred to a different community foundation within their new region. With the permission of the board of the sponsoring organization, the DAF account is transitioned from one DAF sponsoring organization to another.

In the case of transfers between two separate DAF sponsoring organizations, a grant between DAFs would be included in the overall DAF activity on the Form 990. However, in the case of internal transfers (which happen within the same organization), these grants are generally not documented on the Form 990 of the sponsoring organizations.

Can grants be made to support businesses?

Generally, making a grant to a business is not considered to be charitable, unless the business is carrying out a charitable activity.

Low-Profit Limited Liability Companies (or L3C) organizations are businesses with an intentional charitable component. While this designation was intended to make it easier for these businesses to receive philanthropic support, grants to L3C organizations require the same form of due diligence (expenditure responsibility) as any other business requesting philanthropic support because the states that permit formation of these entities do not vet whether their primary purpose is charitable, as does the IRS with public charities.

Grants for downtown development efforts and related economic development activities may need to be explored on a case-by-case basis. The organizational structure of downtown development groups can take many forms, whether as a unit of government, business, 501(c)(3), or 501(c)(6). Grantmakers should seek the assistance of qualified legal counsel to properly navigate these situations and ensure that the activity being funded is considered “charitable activity” that can be supported, depending on the grantmaker’s form (see below).

Grants intended to support child care facilities may also need to be explored on a case-by-case basis. While some child care organizations are established as 501(c)(3)s, others are created as for-profit businesses. Any grant made to a for-profit business would need to follow the appropriate procedures described below. On a related note, grants to individuals designed to support their child care expenses are not automatically considered to be a charitable activity, unless there is a basis of financial need.

- **Private Foundations:** Grants can be used to support non-501(c)(3) organizations, but only for particular charitable purposes (no general operating support grants) and within the guidelines of the foundation itself (i.e., incorporation documents, bylaws, grantmaking policies). However, they must exercise expenditure responsibility in compliance with the Internal Revenue Code (see “[What is expenditure responsibility?](#)”). In these cases, there can be absolutely no tangible benefit back to any donor, advisor, family members or certain other related parties.
- **Community Foundations and Other Public Charities:** Grants can be made to certain non-501(c)(3) organizations, depending on the specific fund types. This type of activity is most commonly carried out via a field of interest fund or fiscal sponsorship.

Prior to considering such a grant, the community foundation would first need to check its articles of incorporation, bylaws and any grant procedure/policy documents to ensure that it can make grants to a non-501(c)(3) organization or institutions that are not considered to be “public charities.” It is common for grantmaking foundations to have their incorporation documents or grantmaking policies clearly limit their grantmaking to 501(c)(3) organizations, so it is important to verify this information.

Grants to non-501(c)(3) organizations from funds other than DAFs require a slightly less formal version of expenditure responsibility than required by the IRS for private foundations (see “[What is expenditure responsibility?](#)”).

- **Corporate Giving Programs:** Corporate giving programs that are not operated through a charitable entity (typically a related private foundation, but sometimes these are also public charities) may only take a charitable deduction for grants to U.S. public charities. Therefore, they typically limit their grants to these charitable entities, or in some cases they may make grants through a fund at the community foundation or a fiscal sponsorship.

- **Donor Advised Funds:** Grants can be used to support non-501(c)(3) organizations, but only for particular charitable purposes (no general operating support grants) and within the guidelines of the DAF sponsoring organization. However, they must exercise expenditure responsibility in compliance with the Internal Revenue Code, comparable to the process required for private foundations (see “[What is expenditure responsibility?](#)”). In these cases, there can be absolutely no tangible benefit back to any donor, advisor, family members or certain other related parties.

Can grants be made to support non-501(c)(3) exempt organizations?

Examples of non-501(c)(3) exempt organizations may include chambers of commerce, local Rotary clubs, mutual aid groups, veterans’ organizations, social clubs and other organizations that fall under other subsections of Section 501(c). Unlike a 501(c)(3) organization, these organizations are exempt from federal taxes under the 501(c) section, but typically donations made to them are not considered tax deductible as a charitable donation, but may be eligible as a business expense. However, gifts to 501(c)(4) and 501(c)(6) organizations are not subject to gift tax. For a full listing of other tax-exempt organization categories, visit the IRS website (<https://www.irs.gov/charities-non-profits/other-tax-exempt-organizations>).

Grants made to non-501(c)(3) organizations are only possible when they are intended for a charitable purpose and oftentimes must serve a public purpose, rather than private interests (i.e., members or those directly connected with the organization). Grants to these organizations – including 501(c)(4) and 501(c)(6) organizations – cannot be used for general operations.

501(c)(4) social welfare organizations have become a more popular organizational form in recent years, with donors and partners being led to believe this is an equivalent alternative to a 501(c)(3) public charity or private foundation. However, this is a functionally different type of organization. Grants to 501(c)(4) organizations still follow the same procedures as those made to any other form of non-501(c)(3) organization. Any grant by a charitable organization must be restricted to charitable purposes only and cannot be used for lobbying, general operations or other purposes explicitly restricted, based on the grantmaker’s type (see below and “[Can a grant be made to support advocacy efforts?](#)”).

- **Private Foundations:** Grants from private foundations can be used to support non-501(c)(3) organizations, but only for particular charitable purposes (no general operating support grants) and within the guidelines of the foundation itself (i.e., incorporation documents, bylaws, grantmaking policies). However, they must exercise expenditure responsibility in compliance with the Internal Revenue Code, comparable to the process required for private foundations (see “[What is expenditure responsibility?](#)”). In these cases, there can be absolutely no tangible benefit back to any Disqualified Persons. (See “Disqualified Persons” description on page 2 for details regarding who constitutes a Disqualified Person, as definitions differ between public charities and private foundations.)
- **Community Foundations and Other Public Charities:** Grants can be made to certain non-501(c)(3) organizations, depending on the specific fund types. This type of activity is most commonly carried out via a field of interest fund or a fiscal sponsorship.

Prior to considering such a grant, the community foundation would first need to check its articles of incorporation, bylaws and any grant procedure/policy documents to ensure that it can make grants to a non-501(c)(3) organization or institutions that are not considered to be "public charities." It is common for grantmaking foundations to have their incorporation documents or grantmaking policies clearly limit their grantmaking to 501(c)(3) organizations, so it is important to verify this information.

Grants to non-501(c)(3) organizations from funds other than DAFs require a slightly less formal version of expenditure responsibility than required by the IRS for private foundations (see ["What is expenditure responsibility?"](#)).

- **Corporate Giving Programs:** In most cases, these grants will not be eligible for a charitable deduction. However, a corporate giving program may sponsor activities of an exempt (but not charitable) organization that comes with certain naming or sponsorship rights and deduct that amount as a business expense. This grant may be eligible for a business deduction and should not be subject to gift tax.
- **Donor Advised Funds:** Grants from DAFs can be used to support non-501(c)(3) organizations, but only for particular charitable purposes (no general operating support grants) and within the guidelines of the DAF sponsoring organization. However, they must exercise expenditure responsibility in compliance with the Internal Revenue Code, comparable to the process required for private foundations (see ["What is expenditure responsibility?"](#)). In these cases, there can be absolutely no tangible benefit back to any donor, advisor, family members or certain other related parties.

Can grants be made to cemeteries?

- **Private Foundations:** Private foundations should first determine the cemetery's organizational type, which is likely either a local government unit or 501(c)(13) organization. Grants made to a local government unit can follow the process as a standard 501(c)(3) organization, whereas grants to a 501(c)(13) organization may require expenditure responsibility (see ["What is expenditure responsibility?"](#)). One key consideration is whether the cemetery benefits a small group of members (or a family) or the general public. A religious order may be acceptable as charitable.
- **Community Foundations and Other Public Charities:** Community foundations are periodically approached with requests to support nonprofit cemeteries, which may be categorized as 501(c)(13) organizations or as local government units. Grants may be appropriate for charitable purposes, such as supporting the maintenance of the cemetery as a whole or for certain significant historical or artistic portions of the property. Additionally, restoring a war memorial or notable local resident's grave site may also qualify. Foundations should first determine the cemetery's organizational type, which is likely either a local government unit or 501(c)(13) organization. Grants made to a local government unit can follow the process as a standard 501(c)(3) organization, whereas grants to a 501(c)(13) organization may require expenditure responsibility (see ["What is expenditure responsibility?"](#)).

Community foundations approached to take on a new cemetery fund should be aware that cemeteries can vary significantly in their structure (i.e., local government unit, 501(c)(13)) and are overseen by the state. Additionally, cemeteries are subject to audit and reserve requirements. Foundations should work with qualified legal counsel to review the situation in advance before establishing a cemetery fund and related agreements.

- **Corporate Giving Programs:** Given that most cemeteries are not charitable, it is unlikely that a corporate giving program would support this endeavor as it would likely not lead to any type of tax deduction.
- **Donor Advised Funds:** This activity may be supported if there is a charitable purpose and if Expenditure Responsibility is exercised. However, the sponsoring organization would want to be certain that there is no tangible benefit to any donor, advisor or other Disqualified Person (as discussed above).

Can grants be made to supporting organizations?

The Pension Protection Act added new requirements for supporting organizations, including the addition of two sub-types of Type III supporting organizations that affect grants by both private foundations and DAFs. Non-compliance with these rules may result in excise taxes and penalties. If the supporting organization's type is not listed on its IRS Determination Letter, then a grantmaker, acting in good faith, may rely on a written representation from a grantee and a review of specified documents in determining whether the grantee is a Type I, Type II, Type III supporting organization (and which sub-type of Type III). Legal counsel should be sought when contemplating any grant to a 509(a)(3) supporting organization (as opposed to a charity exempt under IRC 509(a)(1) or 509(a)(2), as noted on grantee's IRS Determination Letter). An organization will fail to qualify for type I status (and will be converted to private foundation status) if it accepts a gift from a person who directly or indirectly controls the supported organization.

- **Private Foundations:** Private foundations can make grants to supporting organizations that are classified as Type I, Type II or Type III functionally integrated. However, expenditure responsibility is required for grants to Type III "non-functionally integrated" supporting organizations, and the grant will not count as a qualifying distribution for the foundation (toward the 5% payout requirement), unless it has operating foundation status. Also, with a grant to any type of supporting organization, if the proposed grantee or the organization(s) it supports is controlled, directly or indirectly, by one or more Disqualified Persons to the private foundation, expenditure responsibility will be required and private, non-operating foundations may not count the grant as a qualified distribution.
- **Community Foundations and Other Public Charities:** These public charities may make grants to supporting organizations (but see DAF instructions below).
- **Corporate Giving Programs:** Supporting organizations are public charities and should be eligible for a charitable contribution deduction as allowed by law.
- **Donor Advised Funds:** DAFs making grants to type III supporting organizations that are not "functionally integrated" must use expenditure responsibility (see "[What is expenditure](#)

[responsibility?](#)). Also, if the DAF is making a grant to a supporting organization (regardless of type), it would require expenditure responsibility if there is direct or indirect control by a donor, advisor, or related party.

Can grants be made to support fiscal sponsorships?

Fiscal sponsorships can vary significantly and may follow several highly-distinct models.

If an organization has been recently created within the state and is still in the process of seeking its 501(c)(3) status or is only registered within the state and has no intention of obtaining its 501(c)(3) status, then using a fiscal sponsorship model is the organization's only means of obtaining grant funding. A fiscal sponsorship means that the "organization" or project relies on the charitable status (501(c)(3) status) of an existing nonprofit to obtain external contributions and grant funding. Without a fiscal sponsorship, these projects/organizations may not otherwise be eligible for funding via a foundation.

The Model A Comprehensive Fiscal Sponsorship has the following attributes:

- At the most basic level, the Model A structure is one where the sponsor (in this case, a community foundation) takes in a project as an internal program.
- In this case, the project would not have a separate legal existence from the sponsoring organization (the community foundation), even if it has a project committee or entity otherwise responsible for its direction.
- If the project has "employees," those individuals are staff hired by the sponsoring organization. Likewise, the sponsor pays all expenses to vendors and all contracts on behalf of the project are signed/engaged by the sponsor. All contributions come in through the sponsoring organization.
- This arrangement provides the least operational independence for the project and the greatest liability and workload for the sponsoring organization.

In comparison, the Model C Preapproved Grant Fiscal Sponsorship has the following attributes:

- At the most basic level, the Model C structure is one where the sponsor and project representatives have a grantor-grantee type of relationship.
- The project is a legally-separate entity from the sponsoring organization (i.e., community foundation).
- It is not uncommon for the Model C project to be commonly represented by, and operated within, an outside entity or another nonprofit, particularly one that has been recently formed and is seeking exemption.
- The sponsor accepts contributions intended for the project's charitable purposes.
- This fiscal sponsorship model has the least liability for the sponsor and the greatest independence for the project. This is also the easiest fiscal sponsorship model to transfer or terminate (in theory), in the case that the project wants to become independent or shift to a different sponsor.

These models are the most common in the field, but there are several other models of fiscal sponsorship that can be used to accept donations on behalf of a project, using an established nonprofit's tax-exempt status and/or reputation to provide funders reassurances while a charitable project is in its earliest stages.

- **Private Foundations:** Expenditure responsibility does not need to be followed for a grant made to a fiscal sponsor (i.e., to a 501(c)(3) organization). However, the fiscal sponsor must exercise a proper amount of discretion and control, otherwise the IRS could treat this grant as one made directly to a business or other non-charitable entity, which would lead to a taxable expenditure that does not count toward the foundation’s 5 percent payout. Foundation personnel should review the fiscal sponsorship agreement between the grantee and the fiscal sponsor. They should also carefully craft a grant agreement between the foundation and fiscal sponsor that includes certain terms from the tax regulations, underscoring the importance of discretion and control.
- **Community Foundations and Other Public Charities:** These public charities are permitted to support other public charities, such as the fiscal sponsor, which has discretion and authority of the gifts. The grantor should include in the grant agreement that the fiscal sponsor will exercise expenditure responsibility over the grant funds, to ensure that they are used for charitable purposes. That takes the burden off the grantor to do so, although the fiscal sponsor will charge a fee, so the grantor will want to inquire as to how much of the grant will go toward that.
- **Corporate Giving Programs:** The gift to the fiscal sponsor should be treated as a gift to a public charity, and therefore a charitable tax deduction is permitted. However, if the ultimate recipient of the gift is not a public charity, and the fiscal sponsor does not exert appropriate discretion and control over the gift, the IRS may “collapse” the transaction and deem the gift to be to a non-charity and therefore not eligible for a charitable deduction.
- **Donor Advised Funds:** This is permissible as a gift to a public charity. However, if the ultimate recipient of the gift is not a public charity, and the fiscal sponsor does not exert appropriate discretion and control over the gift, the IRS may “collapse” the transaction and deem the gift to be to a non-charity, therefore resulting in potential fines and penalties to the sponsoring organization.

Can grants be made to support individuals?

Grants made to support individuals typically requires standardized grantmaking procedures and a sufficient broad charitable class. In limited circumstances, select individuals may be eligible for grants without following this process.

Grants should be used for charitable purposes, such as education. Grants to individuals for non-charitable purposes (i.e., child care, travel) must be restricted to those with financial need in order to be considered charitable or must be contained within a grant that supports a broadly charitable activity.

For more information on scholarships beyond what is further outlined below, see “Navigating Scholarships and Grants to Individuals” (<https://www.michiganfoundations.org/resources/navigating-scholarships-and-grants-individuals>).

- **Private Foundations:** Private foundations can make grants to individuals, including in the form of scholarships. However, the IRS must pre-approve the scholarship/grantmaking procedures in advance, otherwise they may be considered taxable expenditures.

- **Community Foundations and Other Public Charities:** Public charities may manage scholarships and other grants to individuals by using the private foundation rules as the basis for best practice. Grantmaking procedures for grants to individuals by public charities do not need to be pre-approved by the IRS (unless in a scholarship program limited to employees or former employees of a corporation and funded by a private foundation).
- **Corporate Giving Programs:** Grants to individuals, including scholarships, are not considered to be a deductible contribution unless it is donated to a charity to conduct the program. If scholarships are open to employees and their families, additional rules must be followed.
- **Donor Advised Funds:** DAFs may not be used to make grants directly to individuals, including scholarships. Therefore, a donor wishing to establish a scholarship fund in which they may participate in the decision making must make sure that it complies with the noted exception for DAFs. DAFs may make grants to other organizations, such as schools, universities or community foundations for the purpose of a scholarship program controlled by the charitable institution. However, the DAF cannot make a gift to a university for the benefit of a particular individual, and DAFs cannot be used to satisfy binding pledges. (Note that under the currently proposed DAF regulations, DAF grants would require the recipient to agree not to distribute the DAF funds to individuals).

Depending on a community foundation's policies and procedures, a DAF donor may be allowed to sit on a scholarship fund selection committee. However, the donor, DAF advisors and their respective family members would not be allowed to constitute a majority of those deciding on scholarship recipients for a fund that they support. This means that the donor (and their DAF advisors/family members) cannot have control over advice from the fund, regardless of whether the funds originate from a DAF or not.

Can grants be made to support disaster relief and emergency hardship?

For more information on disaster grantmaking beyond what is featured below, see CMF's "[Frequently Asked Questions About Disasters](#)" resource.

- **Private Foundations:** Private foundations can implement a disaster grantmaking strategy or use a discretionary grant to address general needs within a community. Self-dealing rules still apply, including restrictions on the disaster program generating business for a related company or benefitting a disqualified person. A private foundation may operate an employee disaster relief fund that provides employee disaster assistance for victims of federally qualified disasters only.
- **Community Foundations and Other Public Charities:** Public charities may establish a disaster relief program for individuals or host an employee hardship program fund on behalf of a corporation (or an employee-sponsored DAF, but only for federally qualified disasters).
- **Corporate Giving Programs:** A company can assist organizations as an extension of its standard grantmaking program. In a federally qualified disaster, corporations may provide direct support (cash or in-kind with products and materials) to assist in disaster relief. A company can also assist individuals via an Employee Assistance Program maintained by an independent charitable

entity. During a federally-declared disaster, the corporation can provide disaster relief support directly to employees.

- **Donor Advised Funds:** Donor advised funds can be used to support disaster response in a federally qualified disaster.

Generally, DAFs must follow many standard rules and restrictions even during a disaster, especially when used to provide support through domestic public charities. In many cases, DAF grants to public charities are the easiest option to support urgent action for disaster relief, as they have the fewest rules in comparison to other categories of recipient organizations. Expenditure responsibility may be required for grants to supporting organizations and is required for grants to non-501(c)(3) organizations. Grants to organizations outside of the U.S. may have additional requirements.

Further, there is an exception to the DAF prohibitions for certain employer-related funds established to benefit employees and their family members who are victims of a federally qualified disaster. In the event of a federally qualified disaster (as defined in IRC Section 139), a DAF may make grants to employees and their family members in the following circumstances:

- (i) The fund serves the single identified purpose of providing relief from one or more qualified disasters;
- (ii) The fund serves a charitable class that is large enough so as to be “indefinite”;
- (iii) Grants are selected based upon an objective determination of need;
- (iv) The selection of recipients of grants is made using either an independent selection committee or adequate substitute procedures to ensure that any benefit to the employer is incidental and tenuous (meaning that a majority of its members must consist of persons who are not in a position to exercise substantial influence over the employer’s affairs);
- (v) No payment is made from the fund to or for the benefit of any director, officer, or trustee of the sponsoring organization or any member of the selection committee; and
- (vi) The fund maintains adequate records to demonstrate the recipients’ need for the disaster assistance provided.

Can grants be made to support international efforts?

- **Private Foundations:** Private foundations making international grants must either exercise expenditure responsibility (see “[What is expenditure responsibility?](#)”) make an equivalency determination (see “[What is equivalency determination?](#)”), or utilize a charitable intermediary or “US Friends of” organization, ensuring that funds are used for the IRS’s definition of charitable purposes. Foundations must follow procedures to comply with OFAC, Patriot Act and similar laws aimed at preventing the funding of terrorism, and they must determine whether withholding of a portion of grant funds is required for tax purposes.

Specific questions regarding the foundation’s international grantmaking should be directed to qualified legal counsel. Note that even in countries with which the U.S. has tax treaties – Canada, Mexico, Israel – expenditure responsibility may be required.

- **Community Foundations and Other Public Charities:** Generally, legal requirements for community foundations and other public charities conducting international grantmaking are less restrictive than those for private foundations. However, community foundations can use existing rules for private foundations as a guide for best practice in making these types of grants (see above).

Each foundation may have an established policy or procedure regarding whether international grants can be made by certain fund types or may outline a minimum gift amount. DAFs do have extra requirements for international grants, including either expenditure responsibility (see [“What is expenditure responsibility?”](#)) or equivalency determination (see [“What is equivalency determination?”](#)).

The Council on Foundations recommends that public charities making international grants use the following approach:

- Acquire copies of the grantee’s organizational documents (in English), as well as a description of its activities and programs.
- Develop a written agreement that outlines the grantee organization’s commitments and the use of the grant dollars for a charitable purpose.
- Procure yearly records that account for the use of the grant dollars for each year included in the grant (through the time that the last dollar is expended by the organization).

Although not defined by the Internal Revenue Code, public charities must also ensure that funds granted internationally are used for charitable purposes and may want to follow the private foundation rules as best practice. Grantmakers must follow procedures to comply with OFAC, Patriot Act and similar laws aimed at preventing the funding of terrorism, and they must determine whether withholding of a portion of grant funds is required for tax purposes.

Specific questions regarding the foundation’s international grantmaking should be directed to qualified legal counsel.

- **Corporate Giving Programs:** Corporations may not take a charitable deduction for a gift that is to be used outside of the United States, unless there is a U.S. public charity intermediary that will exercise appropriate discretion and control over the grant.
- **Donor Advised Funds:** DAF accounts interested in making international grants must either exercise expenditure responsibility (see [“What is expenditure responsibility?”](#)) or make an equivalency determination (see [“What is equivalency determination?”](#)), ensuring that funds are used for the IRS’s definition of charitable purposes. DAF sponsoring organizations must follow procedures to comply with OFAC, Patriot Act and similar laws aimed at preventing the funding of terrorism, and they must determine whether withholding of a portion of grant funds is required for tax purposes.

Some DAF sponsors have internal policies that prohibit grants to international organizations or require the use of an intermediary organization with specialization in making international grants.

Specific questions regarding international grantmaking should be directed to qualified legal counsel.

Can a grant be made to support a local, state or national government agency?

Government agencies, school districts and public libraries are all permissible charitable grantees, equivalent to public charities. This also includes government units and colleges/universities that are affiliated with a government unit (i.e. public universities). These organizations/agencies do not require a letter of determination from the IRS to receive grants from foundations. However, legal counsel may be helpful in identifying the status of a potential government grantee, supplying an opinion letter or submitting a private letter ruling request to the IRS.

In some cases, school districts may prefer that grants or scholarships be managed via an external nonprofit (i.e., educational foundation) due to internal procedures or accounting rules.

Private schools/colleges/universities typically have their own 501(c)(3) letter of determination or proof of their status (i.e., nonprofit, for-profit). The grantmaker should follow the necessary procedures, depending on the category of the organization. In Michigan, charter schools are deemed to be the equivalent of public schools and do not require separate tax-exempt status, although many have a supporting foundation that do have tax-exempt status.

- **Private Foundations:** Private foundations are allowed to make grants to governmental units, as long as the grant is for charitable purposes. Expenditure responsibility is not required in this instance. A grant should provide no more than an incidental private benefit to the grantmaker or a related disqualified person. Appropriate records and grant agreements should be maintained for reference, especially due to high rates of turnover in government positions.
- **Community Foundations and Other Public Charities:** Grants may be made to governmental entities so long as they are for charitable purposes.

The Michigan Community Foundation Act (Act 38 of 2017) clarified that municipalities, school boards, intermediate school boards and public libraries may establish funds at community foundations for their own benefit. As governmental entities are generally prohibited from making charitable grants, the Act is important as these entities often are not as qualified to manage longer-term funds. Community foundations accepting gifts from these entities will want to consult the Act, however, as there are a number of requirements.

- **Corporate Giving Programs:** Charitable contributions to governmental units are tax-deductible under section 170(c)(1) of the Internal Revenue Code if made for a public purpose.
- **Donor Advised Funds:** See above explanation for private foundations.

Can a grant be made to support advocacy efforts?

Organizations of all types (i.e., public charities, private foundations) may engage in an unlimited amount of advocacy-related activity, so long as it does not cross the line into lobbying or political campaign

intervention. Much more on the distinctions between advocacy and lobbying are outlined below, along with further guidance on related permissible and impermissible activities.

Examples of advocacy include sharing organizational updates and information with policymakers, inviting policymakers to events and tours of facilities (although private foundations must be careful in paying for travel and other expenses of governmental officials), and visiting policymakers to share information about the organization's activities. It is sometimes acceptable to recognize policymakers at events or as part of the organization's communications efforts, although these activities must be undertaken with care, especially during an election season.

Other examples of permitted advocacy activity include:

- Educating legislators about your foundation's work (such as during the national event Foundations on the Hill).
- Educating the public about public policy issues (e.g. climate change) without including a call to action or discussing specific legislation.
- Nonpartisan analysis or research that is widely distributed (even to a segment of the population) and is independent or objective.
- Attempting to influence legislation that impacts a foundation's existence, powers, duties, tax-exempt status, or deductibility of contributions to it.
- Nonprofit voter engagement, although there are specific rules for private foundations undertaking this activity.

Lobbying under the IRS is defined as any communication with a legislator (or legislative staff) that expresses a view about specific legislation ("direct lobbying") which includes referenda and ballot initiatives upon which the public votes), or a communication to the public that expresses a view about specific legislation and includes a call to action ("grassroots lobbying").

Public charities (including community foundations) may engage in an "insubstantial amount" of lobbying; private foundations and DAFs may not. Charities may not use federal or state funds for lobbying.

501(c)(3) organizations are not permitted to engage in partisan political activity (also known as "electioneering" or "political campaign intervention"). Specifically, they are not allowed to favor a specific candidate or political party, including offering a candidate/party financial or in-kind support, rating candidates or endorsing candidates. Candidates and political parties are also not allowed to use the organization's office space, equipment or mailing lists without it being equally available to all groups at a fair market value. Due to the importance of specific facts in determining if an activity may be considered as a form of campaign intervention, CMF recommends that its members seek advice from external counsel before engaging in any activity that could potentially fall into this category. The IRS can impose excise taxes or revoke an organization's tax-exempt status for engaging in this type of activity.

- **Private Foundations:** Private foundations are prohibited from directly conducting lobbying activities and from earmarking grant funds for lobbying, which oftentimes result in internal policies on the types of grants allowed to support legislative activities.

Foundations may choose to develop an internal policy that specifically outlines what types of advocacy are permitted for staff, board members and other affiliated persons. Likewise, the organization’s grant agreements (or grantmaking policy) should provide clarification regarding the extent to which grants made from funds can be used for advocacy and related purposes. A social media policy that protects the first amendment rights of employees and others associated with the foundation yet avoids the inference that such persons are speaking on behalf of the foundation is also prudent.

- **Community Foundations and Other Public Charities:** Community foundations and public charities may only conduct an insubstantial amount of lobbying, which oftentimes result in internal policies on the types of grants allowed to support legislative activities.

Community foundation funds may be used for the purposes of advocacy (activities that inform or advance public policies). However, community foundations and other public charities can only be engaged in limited lobbying activities – those that directly influence legislation.

Community foundations may choose to develop an internal policy that specifically outlines what types of advocacy are permitted for staff, board members and other affiliated persons. Likewise, the organization’s template fund agreement language (or grantmaking policy) should provide clarification regarding the extent to which grants made from funds can be used for advocacy and related purposes.

- **Corporate Giving Programs:** Earmarking funding even to a charity for lobbying is not tax deductible. However, a deduction is allowable for grants to a charity that happens to lobby, so long as there is no earmarking by the funder.
- **Donor Advised Funds:** Funding advocacy activities of a charity is fine, but they may not be earmarked for lobbying as that is not a charitable purpose.

Can grants be made to support federally recognized tribes?

Similar to government agencies (i.e., state governments), federally recognized tribes are permissible charitable grantees. Federally recognized tribes may carry out activities that extend beyond what is considered charitable, so grantmakers need to verify that the funds are used for charitable purposes. As part of due diligence, the grantmaker should also confirm that the potential grantee is listed on the [federal register](#) by the United States Bureau of Indian Affairs.

For additional information regarding some of the most meaningful and appropriate ways to engage with Indigenous communities, please visit the [Native Americans in Philanthropy website](#).

- **Private Foundations:** Private foundations can support federally recognized tribes. However, a grant would need to be limited to charitable purposes, as the grant could not be made for non-charitable purposes.
- **Community Foundations and Other Public Charities:** Yes, community foundations and other public charities can make grants to federally recognized tribes. However, a grant would need to be limited to charitable purposes, as the grant could not be made for non-charitable purposes.

- **Corporate Giving Programs:** Corporate giving programs can make grants to federally recognized tribes. Tribes described in IRC Section 7871 (a federally recognized tribe and/or its political subdivision) is determined by the IRS to be an organization to which contributions may be tax deductible, as provided in IRC Section 170.

For corporate giving programs, only grants to a charity for charitable purposes are considered charitable deductible. However, corporate giving programs may deduct some grants as expenses for marketing or employee expenses. These cases are fact-dependent and may require legal counsel to determine the appropriateness and/or deductibility of these grants.

- **Donor Advised Funds:** Yes, DAFs can make grants to federally recognized tribes. However, a grant would need to be limited to charitable purposes; a grant could not be made for non-charitable purposes.

Can grants be made to support event sponsorships?

- **Private Foundations:** Private foundations can support events and other sponsorship opportunities. However, the foundation should be cautious about sending staff, board members or disqualified persons to attend the event. Staff of the foundation may attend an event if they are carrying out the work of the foundation itself. For example, the staff person or board member may attend to monitor the grantee's programming or use of funds. However, spouses should not attend unless they have an official position with the foundation. If a sponsorship is purchased by an individual donor or corporation (as opposed to a foundation), then there are not restrictions on who may use the tickets, although the fair market value of any benefits provided in exchange for the donation – such as meals and entertainment – will reduce the charitable deduction.
- **Community Foundations and Other Public Charities:** Community foundations and other public charities can support event sponsorships. While there are not legal limits on who can use tickets or attend events, grantmakers should check the organization's relevant conflict of interest policies and potential excess benefit transactions that may benefit individuals affiliated with the organization. As a general rule, charity staff should have a good and compelling professional reason for using the tickets.
- **Corporate Giving Programs:** If sponsorship is purchased from corporate funds (as opposed to foundation funds), there are no restrictions on who may use the tickets. The recipient charity is required to note the amount of "*quid pro quo*" received in exchange for the ticket price (such as a dinner, entertainment) that will not be deductible as a charitable contribution.
- **Donor Advised Funds:** Any tangible benefit provided to a donor, advisor or related party from a DAF grant is an automatic excess benefit transaction under Internal Revenue Code Section 4958. Therefore, most sponsoring organizations will not make a grant where tickets are available, or if they do, they require refusal of the tickets. (The IRS has opined in the private foundation context

that it is not enough to receive the tickets but not use them; they must be refused, or the grantee may gift them to another charity of their choice.)

Are pass-through grants allowable?

Generally, foundations should not fund a grant that is designed to pass-through to another organization, especially one that would not normally be allowed to be funded directly. For example, a foundation should not make a grant made to a 501(c)(3) organization that is pre-designated (based on the application or grant agreement) to solely support the general operations of a 501(c)(4) organization. That situation is distinguishable from a fiscal sponsorship in which an intermediary organization is exercising the requisite discretion and control over the funds.

GRANTS MANAGEMENT

What is expenditure responsibility?

Expenditure responsibility is a process of additional due diligence, contractual obligations, and reporting required for private foundations and other grantmakers (under specific circumstances). It is commonly required for grants made to private foundations and certain categories of supporting organizations. It may also be used as an option for foreign charities (as an alternative to equivalency determination). It is not typically required for grants to public charities or units of government.

Foundations may require qualified external counsel in order to determine whether a supporting organization requires expenditure responsibility and/or counts toward a private foundation's qualifying distribution. The Council on Foundations has a useful [flow-chart](#) to help organizations determine if expenditure responsibility is necessary.

In the case of grants being considered to international organizations, grantmakers may choose between using expenditure responsibility or equivalency determination (see "[What is equivalency determination?](#)"). If the potential grantee is found to not be a charitable organization or equivalent to a U.S. public charity, then expenditure responsibility is required.

- **Private Foundations:** Private foundations are required to follow a full version of expenditure responsibility, as defined by the Internal Revenue Code.

Expenditure responsibility includes the following five steps:

- **Conduct a pre-grant inquiry:** This should include a reasonable amount of due diligence of the potential grantee to ensure that the activity is considered to be charitable and that the grantee has the ability to carry out the proposed activity.
- **Execute a written agreement:** This document should specify the charitable purpose of the grant, include language that prohibits the use of the grant funds for lobbying activities, and requires the return of funds not used for the designated purposes outlined in the grant agreement.
- **Funds maintained in a separate fund:** The grantee organization (unless it is a private foundation) must maintain the grant funds in a distinct fund, in order to ensure that the charitable funds are kept separate from non-charitable funds used for its other programs and operations.

- **Obtaining reports:** The grantee must provide regular reports to the funder regarding the use of the funds and the charitable activities supported by the foundation's grant.
- **Form 990-PF Reporting:** The foundation itself must report on the grant on its Form 990-PF, including a brief description, the amount, its charitable purpose, and the status of the grant.

Without following expenditure responsibility, foundations can face additional taxes on both the organization and its managers who approved the transaction. In some cases, using expenditure responsibility (as opposed to supporting a project via a fiscal sponsorship) has resulted in instances of increased audit risk.

- **Community Foundations and Other Public Charities:** Grants to organizations that require expenditure responsibility (i.e., grants to non-501(c)(3) organizations) require a slightly less formal version of expenditure responsibility than is required by the IRS for private foundations. These grants would need to be narrowly defined and directed exclusively to the organization's charitable activities (not general operations). The community foundation has a duty to oversee that the funds are used for charitable purposes. Since the Internal Revenue Code (IRC) does not specify how to carry out this duty, it is advisable to look toward the expenditure responsibility rules as they apply to private foundations, listed above.
- **Corporate Giving Programs:** Grants to other than U.S. public charities will not be eligible for charitable tax deduction.
- **Donor Advised Funds:** See above explanation for private foundations.

What is equivalency determination?

In the case that a grantmaker wants to make a grant to an international organization located outside of the United States, it can either use expenditure responsibility (described in "[What is expenditure responsibility?](#)") or use what is called "equivalency determination." The process of equivalency determination allows a grantmaker to determine whether or not a non-U.S. grantee organization is the "equivalent" of a U.S.-based public charity. If an international organization does not meet the requirements of equivalency determination, then the grantmaker can instead use expenditure responsibility as an alternative process to consider the potential grantee for funding.

This process involves acquiring documentation from the potential grantee, in order to make a good faith determination that the organization is the equivalent of a U.S. public charity. This documentation requires an affidavit from the potential grantee or an opinion of legal counsel of either party (the grantmaker or grantee) regarding the status/equivalency of the grantee. The following documents should be collected from the potential grantee in English (or translated into English):

- Founding documents of the organization.
- Detailed description of the organization's purpose, including its past and proposed activities.
- Dissolution provisions, either based on applicable law or as contained within the organization's founding documents.
- Legal or founding documents that describe restrictions on private benefit, noncharitable activities, lobbying, and participation in political campaigns.
- Detailed financial records (excluding religious institution or medical education organizations).

Grantmakers interested in making international grants should seek qualified legal counsel, especially in situations where international grants are not a standard part of the organization's grantmaking portfolio. In some cases, grantmakers work with external firms to conduct the equivalency determination, especially in situations where other funders may have supported the potential grantee already (or may consider supporting it in the future).

- **Private Foundations:** Private foundations are required to either use equivalency determination or expenditure responsibility for grants made to charitable organizations/programs located outside of the U.S. They may also utilize an intermediary or U.S. public charity "friends of" organization.
- **Community Foundations and Other Public Charities:** Charities may conduct activities outside of the U.S. so long as they are able to ensure that the funds are used for charitable purposes and that they are obeying all U.S. laws regarding avoiding funding terrorism (OFAC compliance).
- **Corporate Giving Programs:** Grants to non-U.S. public charities will not be tax deductible in most cases. Tax treaties with Canada, Israel, and Mexico do permit taxpayers with income in such countries to deduct grants to charities in such countries to a certain extent.
- **Donor Advised Funds:** See above explanation for private foundations.

What documents should be maintained within a grant file and for how long?

Foundations should save records of all grants (digital and/or paper) to maintain appropriate records and documents. These records should be kept for at least three years beyond the annual IRS Form 990 or 990-PF filing covered by the last grant payment. Records for each grant should include:

- Information related to the grant program, including records related to complying with the required grantmaking procedures.
- All records and information used to evaluate grant applicants, both potential recipients and successful grant recipients.
- Information related to the purpose and amount of each grant.
- Identification information for grant recipients.
- Information related to grant applicants with relationships to selection committee members (and their family members) and disqualified persons to the foundation.

The National Standards for Community Foundations recommends maintaining signed fund agreements and fund correspondence related to the terms for the fund on a permanent basis, in addition to gift acknowledgements and solicitations for at least 7 years.³ Approved grants and related documentation should be maintained for 7 years after completion of the funded program or the date of the grant, in the case of general operating support. These files may be able to be maintained in a physical or digital format, with appropriately backed-up electronic copies.

Documentation for donor interactions (gift acknowledgements, evaluations, scholarship letters, annual distribution statements, etc.) may be kept with these files or maintained separately.

³ See National Standards Form entitled, "Policy on Records Retention and Destruction"

Why would a grant agreement reference a 509(a) organization, rather than a 501(c)(3) organization?

Depending on the foundation's grant agreement template language, this document may reference a 509(a) organization, a 501(c)(3) organization, or both. This leads to the frequent question of whether these are the same designations or not.

A 501(c)(3) organization is either a public charity or private foundation, both designated as charitable organizations within the Internal Revenue Code (IRC). Each organization with a 501(c)(3) tax-exempt status also has a 509(a) designation, which describes the origins of its funding and is listed within the organization's IRS determination letter. Most nonprofit grant recipients have either a 509(a)(1) or 509(a)(2) designation, while supporting organizations may have a 509(a)(3) designation. These differences are most relevant when making a grant from a DAF or private foundation to a 509(a)(3) supporting organization because expenditure responsibility is required in some limited circumstances (see "[What is expenditure responsibility?](#)").

What is "tipping" in the context of philanthropy, and should grantmakers be concerned about the consequences of "tipping?"

Tipping is an industry term that describes what occurs when a corporation, private foundation or major donor makes a sufficiently large gift/grant that threatens a nonprofit's public charity status.

501(c)(3) organizations are private foundations by default, unless they can prove that they have a sufficient amount of public support. If a public charity receives too much support from any one person or small group, then that could threaten their balance of public support, potentially turning them into a private foundation. The public charity status is preferable over private foundation status, especially in situations where the organization seeks external funding from donor's tax deductible gifts and intends to carry out charitable programs, rather than expending its funds through legally-mandated levels of grantmaking.

Nonprofit organizations that are defined as public charities must be compliant with the public support test, otherwise they default to private foundation status.

Grants made from a publicly supported charity (exempt under Section 509(a)(1), including most community foundations), or a unit of government does not negatively impact the public support test for a nonprofit organization (although government contracts for services might). Any such grant counts as public support. Grants from donor advised funds can only be made to public charities (not private foundations), so it is particularly important that DAF sponsoring organizations are aware of the current status of a nonprofit that may have been "tipped" by it or another funder. [IRS Publication 557](#) provides more guidance on calculating the public support test.

Legally, foundations are generally not held responsible for the impact of their grants on the status of their grantees. However, as good partners, grantmakers should help nonprofits be aware of the impact of large gifts and grants on their status.

Rev. Proc. 89-23 provides that a foundation cannot be penalized for tipping a grantee so long as (1) the grantee has a valid IRS determination letter at the time the grant is made; (2) the IRS has not revoked

the letter, and the foundation is not aware of imminent action by the IRS to do so; and (3) the foundation does not control the grantee. Corporate giving programs should be concerned, however, as tipping might result in a loss of the charitable deduction for their gift.

In some cases, a multi-year grant (or an arrangement involving several years of installments) may prevent a “tipping” problem. Similarly, collaborating with other funders (grantmakers and/or donors), providing a “matching grant,” or helping to identify other forms of income may help diversify the organization’s revenue. When other options do not work, the foundation may need to provide a smaller grant than it originally intended to preserve the public charity status of the nonprofit.

RECOMMENDED RESOURCES

- Council of Michigan Foundations. “An Operations Checklist for Foundation Compliance: Legal Requirements and Operational Best Practices for Private Foundations and Public Charities.” 2022. <https://www.michiganfoundations.org/resources/operations-checklist-foundation-compliance>.
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This document was authored by Brittany Kienker, Ph.D., Knowledge Insights Expert in Residence for the Council of Michigan Foundations (CMF). Legal aspects of this document were reviewed by Jennifer Oertel, outside legal counsel to CMF. CMF members can find answers to their most pressing questions through CMF's Knowledge Insights division, including Ask CMF, the Knowledge Center and the Sample Documents Hub. Ask CMF is a free service to CMF members, available through the "Ask CMF" link on the CMF homepage or by visiting <https://www.michiganfoundations.org/practice/ask-cmf>.

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