

NAVIGATING SCHOLARSHIPS AND GRANTS TO INDIVIDUALS

A COMPARISON OF PHILANTHROPIC GIVING OPTIONS

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Community foundations, private foundations, companies and other grantmakers regularly reach out to CMF to learn how they can establish a scholarship program or other grantmaking programs that benefit individuals. Scholarships are one of the most common types of grants to individuals. This document is a reference tool for considering the variety of giving options available to philanthropy.

This resource is intended to provide an overview of important distinctions for establishing scholarships among the three primary institutions that house scholarship programs:

- **Community Foundations and Other Public Charitable Entities:** This category includes community foundations, university and community college foundations and other nonprofit organizations.
- **Private Foundations:** This category includes family foundations, corporate foundations and other grantmaking entities that are required to follow private foundation requirements set by the IRS.
- **Corporate Giving Programs:** 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.

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GENERAL CRITERIA OF SCHOLARSHIPS AND GRANTS TO INDIVIDUALS

The assets of 501(c)(3) organizations must be used to further charitable purposes (including education). If not, public charities threaten the loss of their charitable status and private foundations (and sponsoring organizations holding donor advised funds) may have these grants be considered taxable expenditures. Grants can be made to benefit individuals, as part of a scholarship program, disaster relief effort, or for other purposes to provide monetary awards.

Scholarships and other grants to individuals are typically managed by community foundations and other public charity grantmakers through the creation of unique fund agreements, which outline the primary contribution, criteria and procedures affiliated with the fund. Since the federal tax code does not give much insight into rules for public charities, many follow the rules applicable to private foundations, which are more restrictive, although charities usually do not secure IRS approval of scholarship criteria as is required by private foundations. For more information on fund agreements, see CMF's resource, "[Frequently Asked Questions About Fund Agreements](#)." For details regarding relevant rules for private foundations, see the section "[IRS Regulations](#)" below.

Although the rules for private foundations and public charities (including community foundations) differ, in this resource "foundation" will be used to refer to all such entities unless otherwise specified.

GOVERNING DOCUMENT REQUIREMENTS: While many foundations regularly engage in grantmaking intended for charitable organizations they may not necessarily have infrastructure in place to support grants to individuals. As an early step, foundations should check their governing documents (articles of incorporation and bylaws, or the trust agreement, as applicable) to ensure they are permitted to provide grants in the form of scholarships or other forms of support to individuals; some foundations are restricted to only provide relief to other 501(c)(3) organizations.

CHARITABLE CLASS: Grants to individuals, including scholarship programs, require the designation of a sufficiently large (indefinite) "charitable class" so that it is not possible to know the identity of the recipient in advance. The charitable class is comprised of potential recipients who meet the requirements of the program's criteria, while illustrating a benefit to the general community. Scholarships and similar programs cannot be established to benefit pre-selected individuals or a relatively small group of people, such as members of a family. Examples of charitable classes may include graduating seniors of a local high school or first-generation students of a local university. These charitable classes benefit from the fact that future classes are also eligible for these scholarships, making for an indefinite charitable class. (Additional information on selection criteria is included in the FAQ section.)

IRS REGULATIONS: Private foundations are not entitled to make grants to individuals for travel, study or other similar purposes, unless such grants satisfy the requirements of [Internal Revenue Code \(IRC\) Section 4945\(g\)](#). The section encompasses scholarships or fellowships that qualify under IRC 117(a) and are to be used for study at an educational organization described in IRC 170(b)(1)(A)(ii), certain grants

constituting a prize or award if the recipient is selected from the general public, or for grants whose purpose is to achieve a specific objective, produce a report or other similar product, or improve or enhance a literary, artistic, musical, scientific, teaching or other similar capacity, skill or talent of the grantee.

The focus of this resource is scholarships and fellowships. Private foundations desiring to conduct their own scholarship programs (as opposed to donating money to a community foundation or educational institution for such grantee to choose scholarship awardees) must have their “objective and non-discriminatory” scholarship guidelines approved in advance by the IRS. Changes to a private foundation’s scholarship programs must also be approved by the IRS. Further, Treasury Regulations require that any award to an individual for travel or study by a private foundation must meet the following requirements:

- The grant is awarded on an objective and nondiscriminatory basis;
- The grant is made pursuant to a procedure approved in advance by the IRS; and
- It demonstrated to the satisfaction of the IRS that:
 - The grant constitutes a scholarship or fellowship grant which is excluded from gross income and is to be utilized for study at an educational institution;
 - The grant constitutes a prize or award which is excluded from gross income under section 74(b), and the recipient of such prize or award is selected from the general public (within the meaning of section 4941(d)(2)(G)(i) and the regulations thereunder); or
 - The purpose of the grant is to achieve a specific objective, produce a report or other similar product, or improve or enhance a literary, artistic, musical, scientific, teaching or other similar capacity, skill or talent of the grantee.

The following rules apply to scholarship grants by any type of charitable funder:

- Grant recipients must be chosen from a sufficiently large charitable class. (See above.)
- The selection criteria for recipients must be reasonably related to the purposes of the scholarship or grant program.
- Neither selection committee members nor Disqualified Persons may derive direct or indirect private benefit from the selection of specific grant recipients. (See Disqualified Persons textbox below for more information.)
- Grant selection must be made based on a procedure that will reasonably result in grantees carrying out the activities intended by the grant dollars.
- If the grant is made to the educational institution and that institution agrees to use the grant funds to defray the recipient’s expenses or to pay the funds (or a portion thereof) to the recipient only if the recipient is enrolled at such educational institution and their standing at such educational institution is consistent with the purposes and conditions of the grant, then the grantor does not need to require recipient reporting (although may want to). However, if a private foundation provides funds directly to the individuals, they are required to receive a report of the grantee’s courses taken (if any) and grades received (if any) in each academic

period. Such a report must be verified by the educational institution attended by the grantee and must be obtained at least once a year. Although these rules do not apply to public charities, they also have a duty to ensure the use of their funds for charitable purposes, and so following these rules is a good practice. It is notably easier to provide grant funds directly to the educational institution.

- Grants and scholarships may be renewed if the foundation has received all required reports on time, any additional criteria and procedures for renewal are objective and non-discriminatory, and the grantor has not received information indicating the misuse of the original funds. The foundation must pursue recovery of funds that have been mis-spent and must suspend grants unless and until such misuse is rectified, in accordance with the Treasury Regulations (53.4945-4).

Private foundations may still make grants to individuals for purposes other than travel or study (as outlined in IRC 4945), such as grants to low-income individuals to assist them with basic needs, so long as the private foundation keeps sufficient records to demonstrate to the IRS that the payments were for proper charitable purposes.

Disqualified Persons

The definitions for disqualified persons differ for private foundations and public charities.

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.

SPECIAL RULES FOR CORPORATE PROGRAMS: Corporate-sponsored scholarship programs, including scholarship funds established at community foundations by corporations or corporate foundations for the benefit of a particular employer's employees (or their respective family members, including those of deceased or retired employees), have additional restrictions that stem from revenue procedures designed to ensure that these programs are not providing employer benefits such as additional compensation or employee retention and recruitment under the guise of charity. Accordingly, the main IRS guidance on this subject, IRS Rev. Proc. 76-47 (as clarified by Rev. Proc. 77-32, 81-217, 85-51, and 80-39, among others), requires that such scholarship program must meet the following factors:

1. The program is not used as a means of inducing employees to continue employment or follow a course of action (although advertising the program to employees has been deemed acceptable, so long as the foundation is clearly identified as the grantor of the funds).
2. The selection committee is independent of the employer.
3. The program identifies minimum requirements for grant eligibility.
4. Recipients are selected based on substantial objective standards unrelated to the employment of the recipients or their family members and to the employer's line of business.
5. The grant is not terminated because the recipient or his or her family member terminates employment.
6. The course of study for which grants are available are not limited to those that would be of a particular benefit to the employer.
7. The terms of the grant and the course of study for which grants are available must meet all other requirements of [Section 117](#) of the IRC and the regulations thereunder, and must be consistent with a disinterested purpose of enabling the recipients to obtain an education in their individual capacities solely for their personal benefit and must not include any commitments, understandings or obligations, conditional or unconditional, suggesting that the studies are undertaken by the recipients for the benefit of the employer (or the related foundation) or have as their objective the accomplishment of any purpose (even though consistent with exempt status) other than enabling the recipients to obtain an education in their individual capacities and solely for their personal benefit.

In addition, the foundation must limit the number of scholarships awarded to (a) 25% or fewer of the eligible applicants who were considered by the selection committee in selecting recipients of grants in that year, or (b) 10% or fewer of the employees' children who can be shown to be eligible for grants (whether or not they submitted an application) in that year. Use of the 10% test is very complicated, and while clarified in the rulings noted above, funders should proceed with caution before utilizing it.

The IRS has clarified that if a corporate foundation makes a grant to a public charity for purposes of carrying out a scholarship program that it is limited to a related employer's employees and their family members (including those of deceased or retired employees), then the requirements of Rev. Proc. 76-47 must be followed, including that scholarship criteria must be approved in advance by the IRS, just as private foundations are required to do, or else the grants may be considered a taxable expenditure of the private foundation.

For more information regarding corporate philanthropy restrictions, see “[Choosing a Corporate Philanthropy Approach](#).”

DONOR ADVISED FUNDS: DAFs are prohibited from making grants to individuals. IRC 4966, which defines Donor Advised Funds, includes an exception to the definition of a DAF when a DAF provides grants for travel, study or other similar purposes, if:

- (I) Such person’s advisory privileges are performed exclusively by such person in the person’s capacity as a member of a committee, all of the members of which are appointed by the sponsoring organization;
- (II) No combination of persons described in subparagraph (A)(iii) (or persons related to such persons) control, directly or indirectly, such committee; and
- (III) All grants from such fund or account are awarded on an objective and nondiscriminatory basis pursuant to a procedure approved in advance by the board of directors of the sponsoring organization, and such procedure is designed to ensure that all such grants meet the requirements of paragraph (1), (2), or (3) of section 4945(g).

Typically, if a DAF wants to fund scholarships, the community foundation will appoint members to a selection committee to vet potential recipients based on criteria approved by the community foundation’s board of directors. In such cases the donor and other DAF advisors and their family members, collectively, must compose less than a majority of such committee.

A COMPARATIVE CHART OF PHILANTHROPIC GIVING OPTIONS FOR SCHOLARSHIPS AND GRANTS TO INDIVIDUALS

	Community Foundations and Other Public Charities	Private Foundations	Corporate Giving Programs
Legal Structure of Scholarship/Grantmaking Program	Community foundation, college/university, or other public charity houses the scholarship fund.	Distinct private foundation. The foundation is responsible for all legal and tax requirements of a private foundation.	Based within the corporation itself. Not a separate entity.
Administrative Costs and Set-Up	Community foundations and other public charities that hold scholarship funds may have an administrative fee for managing the scholarship within the institution. These organizations frequently create scholarships and should have the infrastructure in place to manage the legal and best practices required of a scholarship program.	Private foundations must obtain IRS approval of its scholarship procedures, as well as those intended for grants to individuals for travel or study under IRC 4945. This can be done when the foundation is established or at a later date but must be completed prior to any scholarships or grants to individuals being awarded. Does not apply if the private foundation makes a grant to a charity for purposes of scholarship if the foundation does not control the recipient selection (except in the case of scholarships for employees of a particular corporation).	Minimal administrative costs. Philanthropic efforts are established internally and can be coordinated in conjunction with tax/finance staff responsible for corporate relations, or the corporate marketing team.
Eligible Recipients	<p>Eligible applicants/recipients should fit the criteria outlined by the grant program.</p> <p>For public charities, IRC 4958 restricts excess benefit transactions to disqualified persons, including board members, key staff, and their family members. Eligibility for these</p>	<p>Eligible applicants/recipients should fit the criteria outlined by the pre-approved grant program.</p> <p>Private foundations have a strict prohibition against providing private benefit to individuals, particularly any form of self-dealing to disqualified persons. Eligibility for grants to these individuals should be strictly</p>	<p>Eligible applicants/recipients should fit the criteria outlined by the pre-approved grant program. Note that corporate giving programs may not award scholarships directly, as they are not charitable (deductible).</p> <p>Corporate scholarship rules limit the number of scholarships awarded.</p>

	individuals may be restricted, based on institutional policy. ¹	prohibited, as noted in institutional policy. ²	See “ Special Rules for Corporate Programs. ”
Scholarships	Community foundations and other public charities that manage scholarships use private foundation rules as the basis for best practice, although they do not need pre-approval by the IRS (except in the case of scholarships for employees of a particular corporation).	Can make 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 open to employees and their families, additional rules must be followed.
Grants to Individuals (other than for travel or study)	Follows similar rules to scholarships. Some grants to individuals may be considered taxable to the recipient, depending on the purpose.	Allowable, with careful record keeping.	Not considered deductible unless generally supported through a public charity; individual recipients may not be known in advance.
Disaster Relief to Individuals	May establish a disaster relief program for individuals or host an employee hardship fund on behalf of a corporation (or an employer-sponsored DAF, but only for federally qualified disasters). (See “ Are there special rules for making grants to individuals involved in a disaster situation? ”)	May operate an employee disaster relief fund that provides employee disaster assistance for victims of federally qualified disasters only. (See “ Are there special rules for making grants to individuals involved in a disaster situation? ”)	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. (See “ Are there special rules for making grants to individuals involved in a disaster situation? ”)
Composition of Selection Committee	Selection committee members may be made up of community members, some of whom (less than a majority) may include the donor and/or family members.	Selection committee members may be made up of foundation board members or other community members with special knowledge	Note that corporate giving programs may not do scholarships directly, as they are not charitable (deductible). Corporations only receive a charitable tax deduction for grants

¹ For more information on disqualified persons and excess benefit transactions, see the CMF resource, “[What Boards and Executives Need to Know About Self-Dealing.](#)”

² For more information on disqualified persons and self-dealing, see the CMF resource, “[What Boards and Executives Need to Know About Self-Dealing.](#)”

	<p>Follow exception to DAF definition in IRC 4966 (noted above).</p> <p>Rules for donor involvement vary by institution. The donor or family members (employees of a corporation – but not if the scholarships are limited to employees of a corporation) may be involved in the selection of recipients. However, these individuals may not comprise a majority of these committees.</p>	<p>related to the scholarship or grant program.</p> <p>The primary donor or representatives of the funders may be included in the grantmaking process.</p>	<p>made to U.S. public charities. Grants to individuals could be managed via a separate charity (established by the company or a third party). Selection committees involving a program targeting employees of an employer/company must be comprised of individuals who are independent of the company.</p> <p>For employee hardship funds, selection of grantees cannot be made by a committee with a majority of members being corporate leaders, who could provide substantial influence over the company/employer, such as might be the case for a corporate foundation board making standard grants to charitable organizations. Employees who are not in leadership roles may participate on these committees, although care should be taken that the corporation is not exerting too much control over them, and thus the selection.</p>
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ESTABLISHING NEW SCHOLARSHIPS AND GRANTS TO INDIVIDUALS

Can a donor establish a scholarship via a Donor Advised Fund? Are there alternative options to direct scholarships?

Donor advised funds cannot be used for grantmaking to individuals (including scholarships). However, DAFs can be used to support scholarships and similar initiatives in a number of ways, including:

- Recommending a grant to support general scholarships via a specific educational institution.
- Providing a grant to a specific educational institution to establish a scholarship program with restrictions. The educational institution then manages the scholarship program, including the selection of recipients.
- Funding a grant at an established community foundation or public charity that operates a scholarship program, choosing a charitable organization that serves a specific population of students.
- Establishing a scholarship fund at a community foundation or public charity, with some criteria for the selection of recipients. However, the charitable organization manages the scholarship fund, including the selection of recipients, although there may be limited donor involvement.

Depending on the organization managing the scholarship, DAF donors may be allowed to sit on the selection committee. However, these donors, DAF advisors and their respective family members are not allowed to constitute a majority of those deciding on the scholarship recipients.

Can a donor establish a scholarship for students attending trade schools or for-profit educational institutions?

Scholarships can be established to benefit students attending educational institutions, including traditional preschool, K-12 schools and colleges/universities. In addition, scholarships may be granted to students attending trade schools and for-profit educational institutions, if the institution meets the following criteria:

- A regularly-scheduled curriculum.
- A regular faculty.
- An enrolled body of students attending the institution.

A foundation paying out a scholarship to a student attending a for-profit institution that fits this criteria would be considered a charitable activity. However, it would likely be prohibited private benefit to establish a scholarship fund specifically benefitting a particular for-profit educational institution.³

³ Charitable organizations and charitable activity cannot be organized to benefit private interests, including people with a personal or private interest in the activities. For example, in the case of a scholarship designed for a broad class of students attending a specific for-profit institution, such a scholarship could be created by owners or beneficiaries of the for-profit, providing personal benefit to the business owners, regardless of the intended “charitable” purpose of serving students attending the institution, and this would therefore likely be prohibited.

Can veterans organizations, business leagues or social clubs establish scholarships at a community foundation?

Community foundations are frequently approached by non-501(c)(3) organizations to establish scholarship funds that benefit their members and family members. The answer to this question is directly dependent on the size of the organization represented.

In the case of a relatively small membership organization: A scholarship fund limited to its members and their families would provide direct benefit to members of these groups and this would not be considered a charitable activity. However, if such an organization approached the foundation to establish a scholarship for students attending a local educational institution and/or program that is not restricted to members and their family members, that option may be considered if the potential charitable class is large enough.

In the case of a significantly large membership organization, such as a statewide or national membership organization, there is a distinct possibility that a scholarship program for members may be feasible. In the case of a large membership organization, such as a fraternity or sorority, there could be a sufficiently large charitable class for a scholarship program with appropriate criteria and procedures in place. This would require a limited number of scholarships be offered. Additionally, ensuring that the scholarship is open for the future, rather than being available for one year or a small set of years, would help ensure a sufficiently large, indefinite charitable class. In terms of the management of such a scholarship, the number of scholarships cannot be so large that most of the eligible students/applicants receive one. Additionally, selection committee members could not be related to recipients, per a conflict of interest policy. It may be prudent to follow the guidance applicable to corporate-sponsored scholarships. See the [Corporate Scholarships](#) section above.

Can a donor establish a scholarship specifically for students who are people of color?

Donors and foundations regularly ask about establishing scholarships intended for students who are people of color. Scholarship applications can ask applicants to self-identify their race. Common practice in the field for selection criteria includes consideration of a number of characteristics of recipients, which may include race but also financial need and/or being a first-generation student at a higher education institution, or something similar. The current Treasury Regulations permit grants to be geared toward racial or ethnic minorities. (Note that internships should be analyzed under an employment law context, which is significantly narrower.)

Organizations considering establishing this category of scholarship or grant program should consult with qualified legal counsel. Further information is also available via CollegeBoard's resource, "[Key Non-discrimination Principles and Actionable Strategies for Institutions of Higher Education and Private Scholarship Providers.](#)"

It is important to note that in Michigan and certain other states, state funds (even if granted to a community foundation) may not be used for affirmative action purposes, including gender- and race-based scholarships that would otherwise be permitted by a private institution.

In 2023, the U.S. Supreme Court held that the use of race-conscious admissions programs by two universities (one public, one private) violated the 14th Amendment of the Constitution and, although the 14th Amendment does not apply to private universities, a violation of the 14th Amendment constitutes a violation of Title VI of the Civil Rights Act of 1964 because the private university received federal funds.

In 2024, an 11th Circuit Appeals Court upheld an injunction against a charity, the Fearless Fund, and its related investment fund running a contest that would provide grants to the winning Black woman-owned businesses, based upon the premise that the contestants signed contractual agreements regarding certain matters pertaining to the contest. The Appeals Court found that the plaintiff was likely to succeed on the merits of the case because limiting a contract to a particular race is in violation of Section 1981 of the Constitution, which applies to both public and private parties, and remanded the case to be tried on its merits.⁴ It is important to note that the applicability will be limited to the three states in the 11th Circuit, although we would expect that cases in other jurisdictions will follow.

The effect of the Supreme Court rulings is uncertain. This issue is still evolving and there are many other areas of state and federal law at play, so foundations should consult legal counsel when structuring race-conscious programming.

Can a donor establish a scholarship specifically for students of a particular gender?

Scholarship applications can ask applicants to self-identify their gender. Male or female applicants (depending on additional criteria) are a sufficiently large group to constitute a charitable class, which is defined as a group that is large enough that the potential beneficiaries cannot be individually identified. Foundations should be cautious about how to choose to limit a group of potential scholarship grantees, as restricting eligibility too much may disqualify the pool from being a charitable class. In some situations, a very small class or school could be too narrow, while some schools are sufficiently large that females (for example) within a specific graduating class would be sufficient to be considered an indefinite class. Examples of scholarships tailored to either gender have been upheld as being charitable.

Scholarship recipients should be selected based on criteria related to the grant itself. In the case of gender-based scholarships, the foundation should consider if there is a compelling reason that it is only for males or females, in addition to any other criteria. For example, in considering a scholarship for women going into STEM or aviation fields, there is compelling data available that illustrates the relative

⁴ *Students for Fair Admissions, Inc. v. President and Fellows of Harvard College and Students For Fair Admissions, Inc. v. University of North Carolina*, 600 U.S. 181 (2023); *American Alliance for Equal. Rights v. Fearless Fund Mgmt. LLC*, No. 23-13138, 2023 WL 6520763 at *1 (11th. Cir. Sept. 30, 2023).

percentage of men versus women in those fields. The scholarship criteria would then need to match with that purpose (i.e., women who are enrolled or planning to enroll in a STEM (or aviation) program at a college or university). As another example, there is substantial evidence of the need for male teachers in school districts, which could lead to a scholarship focused on supporting male education majors.

In some cases, it makes sense to use such phrasing as "preference to a female applicant," as it gives the foundation latitude in the case that relatively few qualified applicants apply for the scholarship.

It is important to note that in Michigan and certain other states, state funds (even if granted to a community foundation) may not be used for affirmative action purposes, including gender- and race-based scholarships that would otherwise be permitted by a private institution.

Foundations should consult legal counsel when structuring a gender-based scholarship program.

Are there special rules for making grants to individuals involved in a disaster situation?

Foundations can provide disaster relief grants to individuals in response to federally-declared or local disasters that do not receive a federal emergency declaration. Grantmaking efforts may serve as an extension of a foundation's standard grantmaking program or follow a special set of procedures that are only followed in the case of a federally qualified disaster. Often these grants are given to efforts within local communities. In some cases, foundations or giving programs may use discretionary funds to fast-track disaster grants. Rules against impermissible private benefit, self-dealing and recipient charitable class still apply for disaster situations and grants of this kind should not be intended to benefit disqualified persons.

The declaration of a national emergency under the [Robert T. Stafford Disaster Relief and Emergency Assistance Act](#) (such as occurred during the COVID-19 pandemic) triggers the provisions of Internal Revenue Code ("IRC") [Section 139](#). This section provides guidance to employers for providing "emergency relief payments" to staff without those payments being considered as taxable income to the employee and exempts such payments from being subject to unemployment insurance taxes to the employer.

Additional information about disaster grantmaking and forms of individual assistance is available in [IRS Publication 3833](#). This resource outlines how employer-related foundations, charities and donor advised funds can provide relief to individuals. This publication also outlines important restrictions for grantmakers interested in assisting local businesses and business owners who are impacted by disasters.

Disaster grants for individuals, as well as employee hardship funds, are not designed to, and may not, duplicate Federal Emergency Management Agency (FEMA) payments or insurance or other payments to individuals or families. As a result, emergency relief from community foundations and other charitable efforts are designed to help cover the remainder of basic needs created by the federally-declared emergency. An individual applying for this category of funding may receive assistance with medical expenses, funeral expenses, temporary housing, travel expenses for family members assisting a victim of

a disaster, and other similar expenses resulting from the qualified disaster. Beyond the immediate aftermath of a disaster situation (when all individuals directly impacted may be in need of assistance), organizations must use objective criteria for evaluating victims' financial need to be considered charitable. These funds cannot be used to provide aid to pre-determined individuals or families (i.e. funds created to help a family facing a devastating fire), but these individuals can benefit from previously-established funds that assist families facing crises or funds can be created to benefit them and similar disaster situations with an open-ended charitable class.

The IRS Publication 3833 provides further clarity for employee hardship funds and similar efforts that are designed to benefit employees and their immediate family members. These funds can be used to provide assistance to the employee directly, in the case of the disaster impacting the employee's spouse or children, or to assist the family in the unfortunate case of the employee's injury or death.

To learn more about disaster grantmaking, visit CMF's "[Frequently Asked Questions About Disasters: A Resource for Grantmakers.](#)"

MANAGING SCHOLARSHIPS AND GRANTS TO INDIVIDUALS

Can scholarship funds be sent directly to a specific student or to their school?

Foundations may prefer to send scholarship funds directly to the educational institution attended by the grant recipient. The school then becomes responsible for monitoring the use of the funds, ensuring they are used for the charitable/educational purpose for which they are intended. Otherwise, foundations providing grants directly to students must require reporting from the students about how they used the funds, in keeping with the original criteria of the scholarship program.

If the scholarship funds are paid to the school to offset the costs of tuition (and living expenses, if applicable), oversight is much easier as there is certainty that the funds are being used for charitable purposes. However, if the funds are paid directly to the student there must be oversight to ensure they are used for charitable purposes. Since funds are fungible, then proof of tuition bill, expenses, etc. would be sufficient to show that those costs add up to the scholarship amount or greater. If the student is no longer enrolled, the school (or student) would return the funds.

When private foundations make grants to individuals there is always the requirement to (i) ensure funds were spent for charitable purposes (see "[IRS Regulations](#)" section above); (ii) take reasonable steps to recover any unused funds; and (iii) not make any more grants to the person who diverted funds until they have fully restored any diverted funds and have provided assurances ("extraordinary precautions") that a diversion will not occur again.

What records should be maintained by the foundation for scholarships and other individual grants?

Foundations should maintain records of all grants, including those directed to individuals through scholarship programs and similar initiatives. 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 individual 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 or scholarship.
- 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.

Can scholarships be used for room and board or students' basic needs? Are these scholarships taxable for students?

Scholarships for tuition, fees, books and supplies specifically required by a course (not general school supplies) are considered not taxable. However, costs such as room and board are considered taxable income to the recipient. Likewise, other support to cover a student's basic needs would be considered taxable income. This would include support of a student's health care, transportation and other categories of funded activities beyond those immediately affiliated with tuition, fees, books and supplies required by the student's course of study.

While some scholarship programs managed by community foundations and similar institutions may permit their funds being used to cover these types of costs, payments for room and board and other basic needs, while permissible, are taxable income to the student. The IRS does not require withholding when these funds are paid to U.S. citizens or "resident aliens," only certain foreign students active within the U.S.

Scholarships have a purely educational purpose and are not required to be based on financial need. However, grants and scholarships that are not based on financial need should be evaluated to ensure that the activity remains charitable. For example, supporting students through a grant to cover child care or other living expenses while the student attends classes would not fall under the standard definition of a scholarship. As a result, a grant program to cover this category of activity would require "means testing," indicating a charitable class who require extra assistance is being served.

Should the foundation provide a 1099 to a scholarship awardee or individual grant recipient?

Although 1099s are typically required to be issued to a non-employee (individual or entity) to which payment of \$600 or more is made, there are exceptions for certain types of scholarships. Specifically,

1099-MISC is not intended to be used to report scholarship or fellowship grants. Scholarship programs that require teaching or similar services are considered taxable wages that must be reported on a Form W-2. Generally, other taxable scholarship or fellowship payments do not have to be reported to the IRS. Questions about the completion of tax forms for grant recipients as it applies to specific scholarship programs should be directed to qualified tax counsel.

Can family members of selection committee members or donors receive scholarships?

In most cases, community foundations and other organizations that manage scholarships have pre-established rules that define who is eligible for a scholarship or other grant program. Generally, best practice in the field dictates that these grants cannot be made to a board member, staff person, member of a selection committee or a donor, or their family members. Exceptions may be made, for example, if the high school principal always sits on the selection committee and the principal's child is a potential grant recipient.

Some organizations go so far as to define who constitutes a "family member" or only provides this limitation to "substantial contributors" or those who created the specific scholarship fund. In addition, many procedural documents indicate that scholarships cannot be given to family members of these individuals, including those on the selection committee itself. In some cases, internal procedures may allow for selection committee members to recuse themselves for decisions that may impact family members' eligibility to be considered for a scholarship program.

Scholarships provided by private foundations and DAFs may not benefit any disqualified persons to the private foundation (as defined in IRC 4946; substantial contributors, officers, directors and their family members). For more information about disqualified persons and prohibitions on self-dealing, see the CMF resource, "[What Boards and Executives Need to Know About Self-Dealing.](#)"

Are scholarship applications and related materials considered to be confidential?

Application materials should be considered confidential, and selection committee members should be reminded of their duty of confidentiality. Note that anyone other than an officer and director of the foundation does not have a legal duty of confidentiality, so they should be required to acknowledge a volunteer policy that includes confidentiality, conflict of interest, etc.

Recognizing that applicants may reasonably assume their submissions to the foundation's scholarship programs are confidential, foundations may want to add a "confidentiality statement" to the scholarship submission to clearly indicate what elements of the application are confidential and under what circumstances relevant information may be shared. For example, in promoting a scholarship program the funder may share a scholarship recipient's name, high school, and/or hometown as part of its communications. As another example, a funder might want to note that if an applicant reveals a current abusive situation in their essay, the foundation may choose to report that to the appropriate authorities.

Can a scholarship program specific to a school be structured as a designated fund?

A donor may open a designated fund that is for the purpose of scholarships at a particular charitable school (public or private). In that case, the community foundation may pay over the funds to the school to be awarded for scholarships as the school determines, or the community foundation may handle the administration of the scholarship program. If the school administers the program, the community foundation should require the school award the scholarships on an “objective and non-discriminatory basis” and “in accordance with all laws.” Applicants should be told that the information that they submit to the school will be shared with the community foundation and that the names of awardees may be shared with donors and the public.

Can a grant be directed to a specific individual?

Typically, grants and scholarships cannot be directed to a specific individual. Scholarships and grant programs require that there is a sufficiently large charitable class.

However, there are rare situations where a nonprofit is seeking support for a specific individual served by the organization. This type of case arises most frequently when a foundation is a regular supporter of a nonprofit that serves individuals in a community. In this case, the foundation would make a grant to the nonprofit to support a pre-selected program. The foundation should ensure that any potential conflicts of interest are managed appropriately and that additional funds are not raised with the intent of supporting the individual beyond existing grant funds used to support the organization. These grants are typically highly-reliant on the facts and circumstances specific to each situation. Please consult with qualified legal counsel prior to moving forward with one of these relatively unusual grants.

CHANGING AND UPDATING SCHOLARSHIPS AND GRANTS TO INDIVIDUALS

How can the foundation make changes to existing scholarships or other fund agreements?

Under certain circumstances, it *may* be possible to change or update scholarships and other fund agreements. For further information, see CMF’s resource, “[Frequently Asked Questions About Fund Agreements](#),” particularly the section on “Changing a Fund Agreement” (starting on page 13). The following questions are included in that resource:

- “How can the foundation change a fund agreement with donor involvement?” – page 13
- “How can the foundation change a fund agreement without donor involvement?” – page 14
- “How can the foundation change a fund agreement when multiple donors contribute, or a fundraising event/effort was involved in supporting the fund?” – page 14

Can the foundation increase the size of its scholarship fund pool?

Typically, it is fine for the donor to add to the principal for future years or for the current year, so long as the selections have not yet been made. Once the selections are made, the grants are arguably earmarked for particular individuals and should not be increased.

Can the foundation change the size or other attributes of a scholarship?

In some cases, a donor or the foundation will show interest in increasing the size of a scholarship amount offered annually or adjust other elements of the scholarship, such as timing, criteria, renewability (being able to be re-awarded to an existing scholarship recipient), etc. These types of changes *may* be feasible, so long as the selections have not yet been made. Once the selections are made, the grants are arguably earmarked for particular individuals and should not be changed. In the case of situations where a student has already received the scholarship in past years and a change could impact their eligibility for a renewed award, this type of change should go into effect with new applicants only.

Can a donor request that a scholarship be changed to a different fund type?

Scholarships have additional legal requirements and aspects of their fund agreements that are functionally different from other types of funds intended to broadly benefit charitable entities. Additional counsel may be required when considering substantial changes to a fund agreement.

What happens to overly narrow scholarship funds?

Over time, foundation staff may discover that certain scholarship funds are overly narrow in their criteria, resulting in an insufficient number of qualified applicants or potential recipients. In some extreme cases, too many restrictions may result in the foundation not granting the scholarship each year. If the original donor is still alive, the foundation may decide to approach the donor about approving changes to the fund agreement, specifically to broaden the criteria for the scholarship fund. Otherwise, the foundation board may need to use variance power to broaden the terms of the scholarship.

RECOMMENDED RESOURCES

- Central Valley Community Foundation. "Laws and Regulations Affecting Scholarship Programs." <https://www.centralvalleycf.org/wp-content/uploads/2018/01/Scholarship-Laws-05082017.pdf>.
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- Council of Michigan Foundations. "Choosing a Corporate Philanthropy Approach: A Comparison of Corporate Philanthropy Structures." <https://www.michiganfoundations.org/resources/choosing-corporate-philanthropy-approach>.
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The Philanthropic Initiative. "Funding Education: Approaches and Considerations for Supporting Scholarships via a Donor Advised Fund." 2017. <https://www.tpi.org/resources/funding-education-approaches-and-considerations-for-supporting-scholarships-via-a-donor>.

Petit, Stephanie. "A Basic Guide to Corporate Philanthropy." Adler and Colvin. 2010. <https://www.adlercolvin.com/wp-content/uploads/2017/12/A-Basic-Guide-to-Corporate-Philanthropy-00283643xA3536.pdf>.

ABOUT ASK CMF

This document is 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 Miller 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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