

INVESTING IN PEOPLE: MAKING GRANTS TO INDIVIDUALS



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Introduction

Rules differ for private foundations and public charities

Private foundation rules also provide best practice guidance for public charities to ensure:

- Charitability
- Avoidance of private benefit
- Objective and nondiscriminatory selection process

Agenda

- Grants for travel, study or other similar purposes
 - Selection process
 - Grants to intermediaries
- Other individual grants
 - Grants in recognition of past achievement
 - Disaster relief/individuals in need
 - Payment for services vs. grant
- Donor-advised funds
- Other legal considerations

IRC 4945(d)(3)

The term “taxable expenditure” means any amount paid or incurred by a private foundation...

as a grant to an individual for travel, study, or other similar purposes by such individual, unless such grant satisfies the requirements of IRC 4945(g)...

Initial 10% tax and an additional 100% tax if not timely corrected, plus penalties on managers.

IRC 4945(g)

Objective and nondiscriminatory procedure must be approved by the IRS and must:

- Constitute a scholarship or fellowship grant for study at an educational organization;
- Constitute a prize or award, if the recipient is selected from the general public; or
- Be for achieving a specific objective, producing a report or other similar product, or improving or enhancing a literary, artistic, musical, scientific, teaching, or other similar skill of grantee.

Advance Approval of Procedures

Once given, effective as long as no material changes in procedure.

To receive approval, foundation must demonstrate:

- Objective and nondiscriminatory selection process;
- Procedure reasonably calculated to result in performance of the activities grant is intended to finance; and
- Reports required to determine whether grantees have performed the intended activities (grades for scholarships!).

Selection – “Objective and Nondiscriminatory Basis”

Generally, grants must be awarded through a program that is consistent with the foundation’s charitable status and certain selection rules.

Ordinarily requires the group from which the grantees are selected to be defined based on criteria reasonably related to the purposes of the grant.

Group must be sufficiently broad/large so that the giving of grants to members of such group would be deemed charitable.

Selection – “Exceptionally Qualified”

Broad group of potential grantees is not always necessary. Grantor may reasonably restrict pool of potential grantees.

- Consider the purposes of the grant.
- May select one or several persons if they are exceptionally qualified to carry out grant purpose.
- Must be otherwise evident that the selection is particularly calculated to effectuate the charitable purpose of the grant rather than to benefit (a) particular person(s).

Selection Process

Wide solicitation (avoid word of mouth, institution friends).

Criteria used must be related to the purpose of the grant.

- Scholarship criteria, e.g.: prior academic performance, recommendations, interviews, essays, etc.
- Cannot give preference to relatives.

No grants permitted to grantor managers, trustees, directors, officers, or their family members.

Selection Committee

Selection committee members cannot derive private benefit from the selection of certain grantees.

Use outside experts when possible.

Establish review procedures if grantees selected by one person.

Develop procedure for conflict of interest disclosure and management (e.g., recusal).

Ford Foundation Procedures

Publicly announced competition – announced broadly; selection made with advice of three experts who are not employees of the Foundation; selection committee members not in a position to derive private benefit directly or indirectly.

OR

Nomination/Direct application – nominations by 501(c)(3)s, government, or at least two experts; if nomination made by staff member must be evaluated by a senior staff member; exceptional cases can be approved by an executive officer.

Grants to Intermediary Organizations

Grants to organizations subsequently paid to individuals are not 4945(d)(3) grants if:

- Not earmarked for a named individual;
- No agreement whereby foundation causes the selection of the recipient by the grantee organization; and
- Not an expenditure responsibility grant to the intermediary.

Example: Grants to Public Charities

Grants to public charities for the benefit of an individual will not be subject to 4945(d)(3) if:

- Grant is supervised by the public charity; and
- Public charity controls selection of individual “although the selection need not be made completely independently of the private foundation.”

Example: ER Grants to Intermediaries

Grants to organizations that require expenditure responsibility (e.g., foreign universities that are not public charity equivalents, other non-US public charities) for the benefit of an individual are treated as a 4945(d)(3) individual grant.

- Grantee must follow the private foundation's individual grant procedures.
- Applies even where the grantee organization exercises de facto control over the selection process and makes the selection independently of the private foundation.

Grants Not Covered by 4945(d)(3)

- Grants in recognition of past achievement with no restrictions on use or future conditions
- Salary/compensation for services
- Grants for disaster relief/to needy individuals

Disaster Relief / Individuals in Need

Does not fall under Section 4945(d), and therefore permitted without pre-approval of process, but document!

The IRS defines a needy person as someone who lacks the basic necessities of life—food, clothing, shelter, medical help or transportation—because of poverty or temporary distress.

Class of beneficiaries must be large or indefinite/open-ended, not targeting a specific small group of individuals.

Company foundations may make disaster payments to employees and their survivors without violating the prohibition on self-dealing if it is a “qualified disaster” and certain other criteria are met.

Individual Grant vs. Payment for Services

Payments to individuals or reimbursement for expenses for services to further the private foundation's goals are not individual grants.

- Examples: salaries, consultants' fees, and reimbursement for travel expenses to individuals for personal services in assisting a foundation by consulting, advising, or participating in conferences organized by the foundation.

Donor-Advised Funds

Grants to individuals must be for IRC 4945(g) purposes and meet the following criteria:

- Sponsoring organization appoints all members of the committee and the donor's advice is given solely as a member of the committee;
- Donor and donor-appointed/-designated parties do not control the committee directly or indirectly; and
- All grants are awarded on an objective and nondiscriminatory basis approved by the board of the sponsoring organization.

Travel Grants Programs

May allow individuals to attend conferences, trainings, seminars, etc. in a field of interest to the grantor.

Typically, a qualified candidate must be:

- Exceptionally qualified in the field of interest; or
- In a unique position to benefit from or contribute to the event/benefit the field.

Grantor should have written guidelines that staff must follow to award travel grant.

Individual Grantee Considerations

Anti-terrorism/money laundering and Excluded Party prohibitions require screening of potential grantees before grant agreement or any payments. Rescreen periodically during grant term.

If grant includes international study or travel, specific visa and sponsorship regulations may apply. Determine visa sponsorship provider and visitor activity monitoring responsibilities.

Grant Agreement

Description of grant should make clear the purpose of award is for charitable, educational, etc. purposes.

Grantee expectations should be concrete and deadlines for reports, other deliverables set out.

Payment schedule: if grant is over a semester or year or longer, consider installment payments tracked to reporting schedule.

Allow for grantor site visits/audits.

Supervision/Monitoring

Generally, grantor must receive annual “verified” report if grantee is receiving grades:

- Exception: If grant is paid to educational org directly and it agrees to disburse funds only if grantee is enrolled and in good standing.
- If no grades, grantor must receive an annual progress report from grantee that is approved by host institution.

Non-educational grants: grantor should require at least annual reports on the use of the funds and the progress made by the grantee.

Travel grants: should require narrative report, receipts.

Monitoring/Non-Compliance/Duty to Investigate

Travel or study grants that do not comply with pre-approved IRS requirements are considered taxable expenditures if foundation does not investigate and correct.

- Substantial penalties for both foundation and management.

If the private foundation believes from reports that grant is not being used for its purposes, or if grantee fails to submit report, the private foundation has a duty to investigate.

- Grantor must withhold further payments until cleared to pay.

Tax Treatment of Scholarships

Grants to individuals can be subject to U.S. income tax reporting and withholding if activities take place within the U.S. (rates depend on grantee status)

Scholarships and fellowship grants are taxable unless grantee is a degree candidate at an eligible educational institution; and

- Only certain expenses are tax free: tuition, books, materials required for courses. Room and board expenses are taxable.
- Payment for service associated with grant – even if required in the future and even if part of scholarship -- are taxed.
- IRS Publication 970

Disclosure of Grantee Information

IRS requires private foundations to disclose each individual grantee in Form 990-PF information return.

Public charities are required to disclose some grantee information in their Form 990 information return.

Form 990/990-PF may be required and made public by states in which grantor does business or solicits donations.

Grant letter should inform grantee of public disclosure.

Records Retention

Grantor must retain records for all IRC 4945 individual grants.

Records must be retained for each year grant is given, plus 4 years.

Records include:

- Identification of the grantee;
- Amount and purpose of the grant (grant letter);
- Why grantee was selected (and application);
- Approval memo listing grantee, program, and grant amount; and
- Follow-up information (reports, investigations).

Intellectual Property Issues

Under law, all rights to copyrightable materials remain the property of the authors unless expressly transferred.

Ford Foundation generally allows author to retain ownership but requires a Creative Commons license, unless extenuating circumstances exist.

Royalty clawback provisions sometimes used to avoid private benefit.

Questions?