

The Downside of Private Foundations Using Restrictive Grant Agreements

Contrary to popular belief, federal tax law does not require private foundations to include lobbying prohibitions in grants made to public charities. Many foundations unfortunately make restricted grants by using grant agreement letters that prohibit their grantees from using grant funds for “any propaganda or attempt to influence legislation.” Such language is overly restrictive and may undermine the grantee’s ability to effectively and efficiently achieve its goals. The prohibition on using grant funds for lobbying *only* applies to private foundation grants to non-public charities, such as 501(c)(4) organizations.

Although any money paid or incurred by a private foundation to carry on propaganda, or to attempt to influence legislation, constitutes a “taxable expenditure” (and subjects both the foundation itself and any foundation managers who approve the taxable expenditure to a tax), private foundations may still fund public charities that lobby.

Under federal tax law, private foundations may make two types of grants that avoid creating taxable expenditures – general support and specific project grants – while permitting grantees flexibility in the use of their funds. Making restrictive grants is not necessary since these two safe harbors, if properly applied, allow grantees to use private foundation resources for their projects without sacrificing their ability to lobby and without exposing the private foundation to tax liability.

A general support grant is a grant given to a grantee for its general operating expenses. It is not earmarked for any particular purpose and specifically is not earmarked to be used in an attempt to influence legislation. The public charity may use the grant funds for any purpose, including lobbying. If the grantee uses the money for lobbying, the private foundation will not incur a taxable expenditure. A grant is considered earmarked for lobbying if it is conditioned upon an oral or written agreement that the grant be used for lobbying purposes. The prohibition on earmarking does not mean that private foundations must require grantees to refrain from using grant funds for lobbying.

Private foundations may also fund specific projects, even those that include lobbying. Before making a specific project grant, the private foundation must receive and review a proposed budget for the project that identifies the project’s lobbying and non-lobbying costs. The foundation may give a grant in an amount up to the non-lobbying portion of the budget. The public charity must use the grant funds only for the specific project. If these conditions are met, the private foundation will not incur a taxable expenditure, even if the grantee subsequently uses some of the grant money for lobbying under the designated project.

As a general rule, private foundations should not make restricted grants. Rather, foundations and grantees will be better served, and fully protected, by the careful application of the safe harbors. Whenever a foundation wants to include lobbying restrictions in its grant agreements, it should first consider the potential benefit for the foundation and the likely impact to the grantee. Unless the potential benefit to the foundation outweighs the impact to the grantee, restrictions should not be imposed.

For more information, including sample non-restrictive general support and specific project grant agreements, see Alliance for Justice’s publication *Investing in Change: A Funder’s Guide to Supporting Advocacy*.

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