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6 THINGS NON-PROFITS NEED TO KNOW ABOUT OMB'S MAJOR PROPOSED OVERHAUL OF THE FEDERAL GRANT RULES

Insights
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6 Things Non-Profits Need to Know About OMB's Major Proposed Overhaul of the Federal Grant Rules

Federal financial assistance may soon come with more strings attached and less certainty, and non-profits that depend on federal funding must pay close attention. The Office of Management and Budget (OMB), along with many other federal grantmaking agencies, issued a sweeping proposed rule on May 29 that would rewrite the government-wide rules for federal grants for the first time in over a decade. If finalized, the rule would tighten the conditions attached to federal money and give agencies far more power to walk away from awards. The proposed changes would reach almost every non-profit that touches federal funding, whether received directly or as a subrecipient. Below are six key takeaways your organization should keep in mind regarding the proposed rule so that you are prepared for what comes next.

1. "Guidance" Becomes Binding "Regulation" and Enforcement Gets Stronger

OMB proposes to reclassify its government-wide requirements from "guidance" to an "OMB regulation" that carries legal effect, and to rebrand Part 200 – the framework most people know as the "Uniform Guidance" – as the "Uniform Grants Regulation." Future OMB amendments would then take effect on a government-wide basis, without each agency being responsible for its own rulemaking.

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The re-labeling itself does not create new potential liability, because the Uniform Guidance is already incorporated into awards. However, it removes a buffer and, when paired with the new substantive conditions described below, increases the practical risk of clawbacks, terminations, and even False Claims Act exposure if funds are later found to have been used in a prohibited way.

The proposal would also allow agencies, at their discretion, to cooperate with private parties pursuing their own lawsuits or civil remedies against recipients accused of noncompliance, which is a new and potentially significant litigation exposure point for non-profits.

2. New Funding Conditions Restrict DEI, "Gender Ideology," Disparate Impact, and Gender Transitions for Children

Significantly, the proposal would prohibit using federal award funds to "fund, promote, encourage, subsidize, or facilitate" diversity, equity, and inclusion policies that violate federal anti-discrimination laws, "gender ideology" as defined in the administration's executive order, or the "transition" of a child under 19. A separate new provision would bar the use of awards to promote or support theories of disparate-impact liability, with a narrow carve-out for internal analysis that is not funded by the award and is not used in connection with activities under the award. Violations would be treated as a material breach, which strengthens the government's ability to recover funds or terminate an award.

There are two important caveats for employers to keep in mind:

- First, the restrictions appear to be tied to activities carried out under the federal award, and OMB's own analysis stresses that recipients remain free to use their non-federal funds as they choose.
- Second, employers should not treat the reference to policies "that violate federal anti-discrimination laws" as a safe harbor. OMB has taken an expansive view of those laws, and the prohibition on activities that "promote, encourage, subsidize, or facilitate" such policies could sweep in program design and implementation. That makes it more important than ever to maintain a clear separation between federally funded and non-federally funded activities.

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The proposal also adds a pre-issuance review by senior political appointees, who must screen proposals for consistency with applicable law, agency priorities, and the national interest, including whether an award advances the President's policy priorities.

3. Agencies Gain Broad New Power to Terminate or Suspend Awards

The proposal would give agencies (and pass-through entities) significant new discretion to terminate awards when they determine the award no longer effectuates "program goals, Federal agency priorities, or the national interest." That approach resembles the "termination for convenience" tool long used in federal procurement contracts. The proposal would also authorize temporary stop-work suspensions. Certain categories of funding would generally be carved out, including entitlement, formula, block, and disaster-recovery grants, along with certain trade, CHIPS Act, and infrastructure awards.

For non-profits, the practical takeaway is clear: federal funding may become less predictable. Recipients generally may recover allowable costs incurred through the effective date of a termination but recovery of costs incurred after a discretionary termination would be left to the agency's discretion. And unlike a termination based on noncompliance, a discretionary termination generally would only require a brief statement of reasons, and it would not trigger the same administrative hearing or appeal rights.

OMB instead frames a recipient's recourse as a contract-style claim for money. Such claims are typically heard in the US Court of Federal Claims, which generally awards money damages rather than ordering the government to reinstate the award. Multi-year projects, along with the subawards and vendor commitments that depend on them, would be especially exposed under this framework.

4. Agencies Gain New Authority to Limit Eligibility and Screen Out Applicants

The proposal would let agencies, to the extent permitted by law, restrict eligibility to certain types of non-profits. A funding opportunity could, for example, make 501(c)(3) organizations eligible while excluding 501(c)(4) organizations, as long as it states that clearly.

Agencies could also weigh more factors when assessing an applicant's risk, including, based on publicly available information, a history of "questionable practices" or affiliations with organizations that undermine public safety or national security. On the other side, and consistent with recent Supreme Court developments, agencies would be prohibited from discriminating for or against an applicant based on its religious character or affiliation, and faith-based organizations could apply on the same basis as other entities.

If your organization is a 501(c)(4), a social welfare or advocacy group, or a faith-based provider, this is an area worth watching closely as each funding opportunity is released.

5. Common Costs Like Advertising and Memberships Would No Longer Be Covered

The proposed rule would make several costs that organizations routinely charge to federal awards unallowable. Advertising and public relations costs would be off the table, with narrow exceptions such as costs required by statute, buying goods and services for the award, and limited program outreach such as recruiting participants. Publication and open-access fees would be impermissible unless required by statute or approved in advance. In addition, conference attendance would be allowable only if the agency expressly approves it in the award, and memberships would need prior approval.

The proposal would also narrow the carve-out that lets some non-profits use the more flexible for-profit cost rules. Going forward, only non-profits that receive 90% or more of their federal funding through contracts, or that operate a federally funded research and development center, could use those rules, while most non-profits would apply the standard cost principles.

6. New E-Verify, Payment, Subaward-Reporting, and Other Requirements

The proposal also layers on several new operational rules:

- **Agencies** would be required to run recipients through the Treasury "Do Not Pay" system before disbursing funds, states would have to screen payees against that system or a comparable alternative.

- **Recipients and subrecipients** would be required, among other things, to:
  - enroll in and use E-Verify for employees and contractors working under a federal award;
  - include written justifications when submitting payment requests; and
  - disclose whether anyone who worked on a proposal recently worked for the awarding agency.
- **Pass-through entities** would face heightened duties, including:
  - reporting subawards on SAM.gov;
  - treating transfers to affiliates and related entities as subawards or contracts rather than internal transfers; and
  - consulting with the agency about terminating a subaward if a subrecipient's conduct could significantly damage the reputation of the pass-through, the agency, or the federal government.
- **Fixed amount awards and subawards** would be eliminated, pushing everyone toward cost-reimbursement models.

Together, these changes would add administrative work, especially for pass-through entities that fund and oversee subrecipients.

Conclusion

This proposal would reshape the relationship between the federal government and the non-profits it funds, and you may submit a public comment here by July 13. OMB wants a final rule in place by October 1, 2026, so that a single set of requirements applies to all new awards in fiscal year 2027. Several provisions are likely to draw legal challenges. Consider reaching out to the FP Advocacy team to help develop best strategies for having your voice heard on this subject.

We will continue monitoring this rulemaking and any legal challenges to it, so make sure you are subscribed to Fisher Phillips' Insight System to receive the most current updates

directly in your inbox. If you have questions about how these proposed changes may affect your organization's federal funding, contact your Fisher Phillips attorney, the authors of this Insight, or any member of our Non-Profit and Tax-Exempt Organizations Team.

Summer law clerk Rachel Budzilek contributed to the development of this Insight.