



# Fiscal Sponsorship

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## **When to Use a Fiscal Sponsor, by David Barlow CPA**

Most funders only give grants to organizations that are considered tax-exempt as defined by the Internal Revenue Service (IRS). This means organizations need to apply for and be approved for 501(c)(3) status from the IRS. The IRS gives this status to organizations whose activities are charitable, educational, scientific, religious, literary or cultural in nature. Public schools, libraries and other government organizations fall into this category without having to formally apply to the IRS.

Sometimes a group of people conduct charitable activities but are not formally recognized by the IRS as tax-exempt. In order to be eligible to receive grants, many of these groups identify a fiscal sponsor, an organization that does have tax-exempt status and is willing to work closely with the group to get started.

There are many legal issues that both a fiscally sponsored and sponsoring organization should be aware of before entering into a partnership. The following questions and answers are reprinted with permission from the “Nonprofit Genie,” a free web site sponsored by CompassPoint Nonprofit Services. Anyone can visit this web site at [www.genie.org](http://www.genie.org) for more information about fiscal sponsorship and many other topics related to nonprofit management. David Barlow, CPA has written the answers to each question.

### **How can a new nonprofit get started right away without waiting to file all its papers and obtain tax-exempt status?**

Individuals or groups in a hurry to begin operations and accept tax-deductible donations can become sponsored by an organization that already has 501(c)(3) status. By doing so, the group can apply for and accept grants, accept tax-deductible donations, and carry on other activities under the tax-exempt status of their sponsor. However, the activities of the sponsored group must be consistent with those of the sponsor. For example, a group that intends to provide services to homeless people cannot be sponsored by a 501(c)(3) that is tax-exempt for the purposes of providing classical music concerts.

### **What is a "fiscal agent"? Is a fiscal sponsor different from a fiscal agent?**

Legally, the term “fiscal agent” does not exist. When people use the term “fiscal agent” what they really mean is “fiscal sponsor.” If a group wants to be covered by a 501(c)(3) designation they must be part of, not merely affiliated with, a 501(c)(3) organization.

### **In what situations do groups use fiscal sponsors? What types of groups find them the most useful?**

There are many situations where using a fiscal sponsor could make sense. New groups that aren't sure if they are really viable can test the waters before committing money and time setting-up an independent 501(c)(3). Groups who only intend to operate for a limited period of time may benefit from fiscal sponsorship, as they do not have to first establish and then dismantle a nonprofit corporation. If a group is a coalition of several groups, or even 501(c)(3)'s working together on a common issue, a fiscal sponsor may be seen as neutral territory for accepting funds. If the group is committed to its mission but just has no interest, or experience, in managing all the administrative functions of a business, a fiscal sponsor could be a good option. Finally, individuals who are unaffiliated with any group or nonprofit (such as independent filmmakers) seeking grants and donations may find it convenient to work under a fiscal sponsor.

Here's an example. In the hours immediately following the shootings in San Francisco at the 101 California office building, many people wanted to donate funds to help the families of the victims (many of whom worked for a law firm), and to educate the public about gun violence and gun control. A group of attorneys contacted a fiscal sponsor and were able immediately to begin collecting donations and conducting an educational campaign on the subject. Later, the group decided to become permanent and incorporated separately as the Legal Community Against Violence.

### **What are the benefits of using a fiscal sponsor?**

**Speed** - It normally takes four to six months from the time an application for tax exemption is filed with the IRS to receive notice that tax-exempt status has been granted, and that is IF the IRS has no questions about information contained in the application. Theoretically, one could make arrangements to be fiscally sponsored in a day or less, although a couple of weeks is more typical.

**Efficiency** - Especially for small groups, having someone else provide most of your administrative, or infrastructure functions may be cheaper than doing it yourself. This is especially true if you are a group that is only expecting to be in existence for a short period of time.

**Convenience** - Most groups, start up or otherwise, want to focus their energy on their charitable activities. Having to create and maintain an infrastructure can be distracting from the mission of the group.

**Necessity**- There are some funding sources that will not fund brand-new groups. One way around this restriction is to become part of a group that has some history.

### **What are the disadvantages?**

As a sponsored project of an already existing 501(c)(3), your "parent organization" is legally responsible for everything you do. This includes the responsibility to comply with the terms of the grants you have been awarded and how you operate. If you and your sponsor disagree, you may be forced to "do it their way."

Some foundations have policies that do not permit them to make grants through fiscal sponsors.

### **What can a fiscal sponsor provide us that we couldn't do on our own?**

A fiscal sponsor can often provide useful advice and help point you in the right direction. Hopefully, the sponsor will also have solid experience in the areas where they are providing services to you. But the bottom line is, except for groups needing to get around being new with funders, if you wanted to put in the resources necessary to do everything on your own, you could do it all yourself.

### **What happens if we want to leave a fiscal sponsor?**

It is important to both you and the sponsor that the terms of the relationship are in writing before the relationship begins. If you don't, and later decide you want to leave, you may find that the sponsor wants to keep the project but not you. Any good sponsorship agreement will have a mechanism to deal with how to terminate the relationship. There are certain legal restrictions on how the project's activities and assets are severed from the sponsor but that should be disclosed in the sponsorship agreement.

### **What are the reasons to provide fiscal sponsorship to another organization?**

The most common reason a 501(c)(3) would agree to provide sponsorship to another group is because the other group wants to engage in an activity that is substantially similar or complementary to the activities of the 501(c)(3). By acting as a fiscal sponsor, an organization can nurture a new, complementary effort, and manage funds for a temporary project, etc.

### **What are the risks of being a fiscal sponsor for others?**

Often the sponsored project operates from a different physical location from the sponsor so the sponsor may forget to provide proper oversight and support. Conversely, the sponsored project needs to remember that it is part of a larger organization and the sponsee has agreed to give up some of its autonomy. Frequent, open communication is the key to making the relationship work for both sides. Since the law considers the project and the sponsor to be one legal entity, each can be held responsible for the actions of the other.

### **What are some of the services typically provided by fiscal sponsors?**

There is really no such thing as a "typical" bundle of services provided by a sponsor. The services available from professional sponsors vary from nothing to those listed below.

- Financial: Federal, state and local tax & informational returns; receipt and acknowledgment of tax deductible donations and grants; payroll tax remittance and filings; monthly financial statements; financial record keeping; independent audit check processing and issuance for expenses; I-9s, 1099s.
- Insurance: Directors' and Officers' insurance; volunteer insurance; general liability; umbrella; commercial automobile.
- Human Resources Administration: Payroll processing; W-2s; personnel policies in compliance with federal, state and local laws; comprehensive benefits package; benefits administration, 5500; technical assistance on personnel issues.
- General Administration: Bulk rate postal permit; resale permit; sales tax reports; legal advice; grant progress reports.

### **How much do fiscal sponsors charge?**

There are almost as many fee arrangements as there are fiscal sponsors. Some charge nothing, some charge up to 40 percent. Some sponsors pay projects interest on the money the project has on deposit, some don't. A full-service professional sponsor will probably cost a group between 5 and 12 percent of gross receipts. Large projects may be able to negotiate a lower fee.

## Do we need an attorney to work out a fiscal sponsorship agreement?

When a project sets up a relationship where it voluntarily gives up some control over its activities, it is always a good idea to have a written contract. Often a sponsor will have a standard contract that it uses with new projects. A good contract will have a procedure outlined in it as to how to terminate the relationship if for some reason either side becomes uncomfortable. Read the contract carefully and don't be afraid to ask the sponsor questions. The sponsorship agreement is a legally enforceable document so unless the group has experience in this area, a review of the document by an attorney paid to represent your interests is a good idea. Make sure you know what you are getting yourself into.

An example of a fiscal sponsorship agreement between two nonprofits can be found at [www.genie.org/faqpages/fiscal\\_spons\\_arts.htm](http://www.genie.org/faqpages/fiscal_spons_arts.htm). An example of a fiscal sponsorship agreement between a professional fiscal sponsor and its projects can be found at [www.genie.org/faqpages/fiscal\\_spons\\_sff.htm](http://www.genie.org/faqpages/fiscal_spons_sff.htm).

If my group is operating under a fiscal sponsor, and we've decided to become an independent nonprofit, what are the steps we should take?

If you have decided to separate from your current sponsor and don't want to affiliate with another, the process to become independent begins with informing your current sponsor of your decision. Most often, you will then create a public benefit corporation that will file applications with both the IRS and state taxing authority asking to be exempt from income taxes. From the time the applications are submitted it usually takes four to six months to receive your determination letters (notice that exemption has been granted). When you receive your notice it is retroactive to the date of your original application. While you are waiting for your letter you will need to do all those things that any new business does (open bank accounts, hire employees, obtain insurance, etc.). The final step is arranging to have your sponsor transfer the project's assets and liabilities to the new nonprofit.

Where can I read more about fiscal sponsorship?

The most complete book on the subject is, *Fiscal Sponsorship: Six Ways To Do It Right*, available for \$14.95 + \$3.50 shipping/handling from San Francisco Study Center, 415-626-1650 or 888-281-3757; [www.studycenter.org](http://www.studycenter.org) or from [www.amazon.com](http://www.amazon.com).

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