FISCAL SPONSORSHIP

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I. INTRODUCTION

This memorandum provides a brief summary of the concept of fiscal sponsorship. It will also distinguish a properly structured fiscal sponsorship arrangement from fiscal agency. There are many variations on the theme of fiscal sponsorship. This memorandum will describe two commonly utilized models of fiscal sponsorship: the “re-grant” model and the “direct project” model.

II. WHAT IS FISCAL SPONSORSHIP?

Fiscal sponsorship is generally an arrangement between a Section 501(c)(3)[1] public charity (sponsor) and an entity, group or individual that desires to carry out a charitable project, but has not obtained tax-exempt status (non-exempt project). Depending on how the relationship is structured, the sponsor may adopt the project as its own, or provide financial or other resources to support the project.

Such an arrangement may be desirable for a variety of reasons. Frequently, fiscal sponsorship provides a practical solution to the fundraising challenges faced by a charitable project that is not recognized by the U.S. Internal Revenue Service as a tax-exempt organization described in Section 501(c)(3). These could be new organizations that have not had time to develop a business plan and apply for tax-exempt status, or projects that will achieve their goal in a short period of time so it does not make sense to create a separate Section 501(c)(3) organization to carry out the project goal.

Many funders (such as private foundations, governmental agencies, corporations and individuals) will not donate funds directly to such projects. By properly establishing a fiscal sponsorship relationship with an existing Section 501(c)(3) public charity, a project that has not obtained its own tax-exempt status can successfully attract grant funding and individual charitable contributions to support its work in the community.

III. DISTINGUISHING A SPONSOR FROM AN AGENT

When advising nonprofit organizations about fiscal sponsorship options, it is important to use accurate terminology. Specifically, we should take care to distinguish a “fiscal sponsor” from a “fiscal agent.” The term “fiscal agent” implies that the sponsoring organization is acting

[1] All Section references, unless otherwise noted, are to the Internal Revenue Code of 1986, as amended.

as the legal agent (i.e., it is under the direction and control) of the sponsored non-exempt project. Fiscal sponsorship, on the other hand, requires the sponsoring organization to maintain ultimate discretion and control over the use of the assets that it receives in its role as fiscal sponsor.

There may be situations when it is appropriate to enter into an agency relationship. However, fiscal agency frequently results as the unintended consequence of an improperly structured fiscal sponsorship arrangement, resulting in a conduit or step transaction. That is, the parties intended to enter into a fiscal sponsorship arrangement, but the sponsor did not exercise sufficient oversight and control over the contributed funds, and served as a mere agent of the non-exempt project. In that case, the desired legal and tax benefits may be lost. In a conduit arrangement, where the charity acts as a mere agent of a non-exempt project, private foundation grants passed through by the charity could be treated as taxable expenditures made directly to a non-charity, and individual donations may not be deductible charitable contributions.

Before entering into a fiscal sponsorship arrangement, the sponsor should carefully evaluate and determine whether funding a particular non-exempt project will further its charitable purposes. The sponsor should also clearly document that it did not serve as a mere agent of the non-exempt project.

IV. TWO MODELS OF FISCAL SPONSORSHIP: "RE-GRANT" AND "DIRECT PROJECT" MODELS

Fiscal sponsorship can be structured in many different ways to meet the needs and goals of the parties involved. Two of the most common models of fiscal sponsorship are the "re-grant" and "direct project" models.

A. RE-GRANT MODEL

Under the re-grant model, a grantor-grantee relationship is established between the sponsor and the non-exempt project. The sponsor agrees to accept gifts from various funding sources that are designated in support of the sponsored project. The sponsor then disburses (or "re-grants") those funds for the specific pre-approved project that the sponsor has determined will advance its charitable mission.

The sponsor should monitor the non-exempt project's use of the grant funds to ensure that they are used for the intended charitable purpose. Generally, the non-exempt project is required to provide periodic reports to the sponsor regarding how the grant funds were used and the progress toward accomplishing the charitable purposes of the grant.

Under the re-grant model, there is greater risk of creating a conduit/agency arrangement, as discussed in Section III. Proper documentation is critical to demonstrate that the sponsor exercised appropriate discretion and control over the funds. The written agreement should clearly state that the sponsor retains the right, in its sole discretion, to redirect the funds or other assets that it receives in its role as sponsor to another charitable beneficiary.

One of the benefits of the "re-grant" model of fiscal sponsorship is that the sponsor does not take on all of the liabilities of the sponsored organization, as in the direct project model described below.

B. DIRECT PROJECT MODEL

Under the direct project model, the sponsor conducts the non-exempt project as its own. The individuals who will carry out the project's activities are generally hired by the sponsor as employees or independent contractors. Legally, it should be viewed no differently than any of the sponsor's other programs. It is important for the sponsor to understand that it is entirely responsible for all of the activities and liabilities of the sponsored project. While the sponsor may appoint an advisory committee to assist with the project management, the project does not have a separate legal existence and its revenue and expenses are reported on the sponsor's IRS Form 990.

V. RESOURCES

- Gregory L. Colvin, *Fiscal Sponsorship: 6 Ways to Do It Right* © 1993, 2005 (available for purchase at: http://fiscalsponsorship.com/)