

# **A WHITE PAPER:** **On Comprehensive Fiscal Sponsorship**

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The purpose of this paper is to provide readers with a thorough understanding of the emerging field of Comprehensive Fiscal Sponsorship (CFS).

It is intended for use by:

- Individuals and groups considering using a fiscal sponsor to facilitate their mission-related work
- Organizations considering offering fiscal sponsorship services
- Nonprofit, foundation and legal practitioners who wish to inform themselves about this topic

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## EXECUTIVE SUMMARY

This white paper examines the contours and constructs of Comprehensive Fiscal Sponsorship (CFS), a sub-practice of the broader field of fiscal sponsorship. Typically fiscal sponsorship describes a relationship in which an unincorporated group wishing to conduct charitable activities affiliates with an existing 501(c)(3) nonprofit with a compatible mission. With Comprehensive Fiscal Sponsorship, the “parent” organization, in accepting the group as one of its programs, provides legal and financial oversight as well as accounting, human resources and other back-office support.

Fiscal sponsorship has been practiced in varying degrees since at least 1959 when the Massachusetts Health Research Institute, now Third Sector New England (TSNE), incorporated and began sponsoring research and community-based public health activities. In 2004, a group of fiscal sponsors from around the country created the National Network of Fiscal Sponsors (NNFS) to share and promote effective, responsible practices in the field.

Fiscal sponsors receive grants and other tax deductible contributions that are allocated in support of project activities. Such payments are usually disbursed in the form of payments to project staff, vendors, contractors and grantees.

Fiscal sponsors provide this support only to groups whose activities further the sponsor’s mission and tax-exempt purpose. The level of engagement between sponsor and project varies, but at a minimum all fiscal sponsors:

- Retain control and discretion as to the use of the funds
- Maintain records establishing that the funds were used for section 501(c)(3) purposes
- Limit distributions to specific projects that are in furtherance of their own exempt purposes.

### **A UNIQUE AND VITAL ROLE**

Comprehensive fiscal sponsorship contemplates a more integral, connected role for the sponsor than other models. The nature of CFS means that sponsors must exercise great care in screening potential new projects. When, after careful consideration, a fiscal sponsor accepts a new project, the project becomes a program of the sponsor, part of the same legal entity. The sponsor, therefore, has a vested interest in its success. Because of the total assumption of legal and financial liability, such relationships should not be equated with so-called “fiscal agency,” “conduit” or pass-through arrangements. In fact, a CFS relationship is the converse of an agency arrangement, in which a principal is in control and directs an agent to carry out activities on its behalf. In CFS, the sponsor and the project are both part of the same legal entity, governed by the sponsor’s board of directors.

CFS furnishes projects with comprehensive personnel policies, liability insurance, financial and administrative expertise, and keeps projects abreast of and trained on new government regulations as they arise. Having these reliable operational mechanisms in place affords project leaders peace of mind, eliminating many of the stresses that can derail an operation.

## **IMPROVING PROGRAMS**

The intangible benefit of CFS to projects and their leaders is critical. A leader's time and attention will not be sidetracked by the plethora of issues inherent in managing back office operations. Project staff work towards mission fulfillment knowing that all administrative and compliance issues are being efficiently addressed. CFS keeps the engines of their projects humming, allowing passionate, mission-driven project leaders and staff to focus on the activities that are core to the project's existence.

Even large projects may find that the quality service and support offered by CFS are advantageous and cost effective. The large size and unified infrastructure of most CFS organizations create economies of scale otherwise unavailable to stand-alone smaller entities, maximizing administrative efficiencies while minimizing the costs of back office support and overhead. This is one reason why existing 501(c)(3) nonprofits are increasingly seeking out established comprehensive sponsors as long-term solutions to meet their needs of lower costs and increased proficiency.

Despite the growth and widespread acceptance of fiscal sponsorship, certain misconceptions linger. One concern voiced occasionally by foundations is that fiscal sponsors are actually "sponsoring organizations" that manage donor advised funds. However, it is clear from a careful analysis that, with rare exceptions, these two constructs are not at all similar. The three-pronged definition of donor-advised funds contained in the Internal Revenue Code is different in key respects from the practice of fiscal sponsorship. Such misconceptions are fully addressed in this White Paper.

Often an afterthought, ease of exit is a significant advantage of CFS. When a stand-alone nonprofit organization winds up its operations, it must do so in compliance with time-consuming and often complex IRS and state requirements. When a CFS project terminates its operations, all assets previously maintained by the project will simply be spent out on mission-related purposes. Likewise, if a project remains viable but wishes to become independent or find a new sponsor, a well-drafted fiscal sponsorship agreement should provide that all project specific assets and liabilities be transferred to the new entity upon termination of the agreement.

Sponsorship with a reputable CFS practitioner conveys several messages to foundations, other funders and the public. It says: (1) this project has been through a thorough evaluation process that determined it has the capacity to achieve its underlying objectives; (2) all back-office operations of the project are managed by competent, experienced professionals ensuring maximum transparency; (3) project staff receive proper compensation and good benefits, increasing retention and minimizing burnout; and (4) the project will be able to focus on the mission and not be distracted by administrative burdens and complex compliance issues.

Whether foundation, charitable initiative or fiscal sponsor, due diligence coupled with an open mind to creative solutions like comprehensive fiscal sponsorship can contribute substantially to advancing the purposes for which the social sector exists. CFS stretches charitable dollars further and more effectively than most stand-alone small to mid-sized and even many large nonprofits could ever on their own. CFS also offers a realistic, honest approach to not only survive, but excel in the challenges of our day and those that lie ahead.



## WHAT IS FISCAL SPONSORSHIP?

The term “fiscal sponsorship” actually refers to several different, often overlapping arrangements. The common denominator is generally that a group wishing to conduct a charitable program without incorporating or obtaining Internal Revenue Service (IRS) recognition finds an existing 501(c)(3) nonprofit to serve as its fiscal sponsor. Many groups, though charitable in nature, lack the legal status they need to receive grants from foundations, individual donors and government agencies. In recent years, existing tax exempt charities have also turned to comprehensive sponsors, realizing benefits that extend beyond tax-exempt status such as enhanced back office efficiencies, cost savings and other value inherent in comprehensive fiscal sponsorship.

Fiscal sponsors receive tax deductible contributions that are then allocated in support of projects. Such funds are usually disbursed in the form of payments to project staff, vendors, contractors and grantees.

A fiscal sponsor is able to offer this support only to groups whose activities further the sponsor’s mission and tax-exempt purpose. The level of engagement between sponsor and project varies greatly, but at a minimum all fiscal sponsors must:

- Retain control and discretion as to the use of the funds
- Maintain records establishing that the funds were used for section 501(c)(3) purposes
- Limit distributions to specific projects that are in furtherance of their own exempt purposes.<sup>1</sup>

501(c)(3) organizations acting as fiscal sponsors that fail to conform to these requirements jeopardize their own exempt status.

Fiscal sponsorship has been practiced in varying degrees since at least 1959 when the Massachusetts Health Research Institute, now Third Sector New England (TSNE), incorporated and began sponsoring community-based public health projects and research laboratories.<sup>2</sup> TSNE has since expanded and now offers Comprehensive Fiscal Sponsorship (CFS) to groups of people involved in many types of civic engagement activities in their communities.<sup>3</sup> Over the years, TSNE, along with other like-minded organizations throughout the country, independently developed a unique brand of fiscal sponsorship known as CFS.

In 2004 these groups came together and created the National Network of Fiscal Sponsors (National Network) to share and promote effective, responsible practices in the field as well as gain a deeper understanding of the current practice of fiscal sponsorship around the country. Founders of the National Network included Community Partners, Colorado Nonprofit Development Center, Earth Island Institute, PHFE Management Solutions, CIF of the San Francisco Foundation (now Community Initiatives), TSNE, and Tides Center.<sup>4</sup>

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1 Rev. Rul. 68-489, 1968-2 C.B. 210

2 *Chronology of Fiscal Sponsorship*, The Fiscal Sponsor Directory at <http://www.fiscalsponsordirectory.org/chronology.php>

3 *Brief History*, Third Sector New England at <http://www.tsne.org/about/mission>

4 National Network of Fiscal Sponsors at <http://www.tides.org/community/networks-partners/nnfs/>

A core tenet and legal requirement of any fiscal sponsorship relationship is that the purposes of a potential project must be consistent with the sponsor's own mission.

Most members of the Network practice a type of fiscal sponsorship commonly referred to as Model A sponsorship. Under a Model A relationship, the project becomes a part of the sponsor; “the sponsor takes the project in-house. The project has no separate legal existence.”<sup>5</sup> All employees of the project become employees of the sponsor. The sponsor’s payroll tax withholding, workers’ compensation insurance, unemployment benefits, and health and retirement plans offered all are applied to the project staff in the same manner as the organization’s other employees. The sponsor will be liable for the actions of project employees within the scope of their employment as well as any other liabilities the project accrues. Additionally, all tax reporting is done by the sponsoring organization.

Although the Model A “direct project” is the most commonly practiced form of fiscal sponsorship, other manifestations occur throughout the charitable community and their use as legitimate, creative models should not be discounted. Gregory Colvin’s *Fiscal Sponsorship; Six Ways To Do It Right* provides the most thorough treatment of the various incarnations of fiscal sponsorship to date.

CFS can best be characterized as a subset of fiscal sponsorship, typically patterned after the Model A relationship, where the sponsor plays a deeper, more nurturing role than contemplated by any other model. In addition to serving as the legal employer of project employees, offering insurance, and seeing to state and federal compliance matters, sponsors provide a comprehensive suite of services designed to enhance the capacity and effectiveness of projects. Most of these offerings fall into four broad categories: financial management, human resources management, information systems support, and capacity building.

Comprehensive sponsors run the essential back office operations of their projects in a highly competent, cost-effective manner, allowing agents of change to focus their passions and energies on activities central to project purposes. These sponsors also engage the projects in a wide array of capacity building endeavors, and beyond that, a host of intangible benefits begin to accrue the moment a project finds a home with a credible comprehensive sponsor.

The end result of CFS is that progressive movements are able to minimize administrative burdens and maximize project impact and society’s corresponding return on investment. Below, the parameters of CFS are thoroughly explored.

## MISSION ALIGNMENT

A core tenet and legal requirement of any fiscal sponsorship relationship is that the purposes of a potential project must be consistent with the sponsor’s own mission.<sup>6</sup> This threshold requirement is the first standard articulated in *Guidelines for Comprehensive Fiscal Sponsorship* (Guidelines), a must-read set of guidelines and recommended best practices for any nonprofit organization contemplating a role

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<sup>5</sup> Colvin, Gregory. *Fiscal Sponsorship; 6 Ways To Do It Right*, Study Center Press, 2005.

<sup>6</sup> See Rev. Rul. 68-489, 1968-2 C.B. 210



as comprehensive fiscal sponsor or for any group seeking a responsible sponsor.<sup>7</sup> These guidelines, created through the collaborative effort of the members of the National Network, will be referenced throughout this paper.

Before a project can be taken under the supportive umbrella of a fiscal sponsor, it should be carefully scrutinized to establish that its goals and vision are both compatible and consistent with the sponsor's own mission.<sup>8</sup> This initial step is necessary because 501(c)(3) exempt organizations must operate in furtherance of a specific charitable purpose found in their organizing documents and forms filed with the Internal Revenue Service (IRS).

The activities of all nonprofits, not just those practicing fiscal sponsorship, must operate in accordance with a stated tax-exempt purpose. If a project's mission is not compatible with that of its sponsor, that sponsor is not serving its exempt status, and its 501(c)(3) classification could be jeopardized. Although the vetting processes used by organizations engaged in comprehensive fiscal sponsorship vary, all must be thorough, ensuring mission compatibility. Review and approval of the project by the fiscal sponsor's board of directors is an essential step in the process.

## THE MEMORANDUM OF UNDERSTANDING AND ADVISORY BOARDS

The union between project and Model A sponsor is typically described in a memorandum of understanding between the fiscal sponsor and the unincorporated organization.<sup>9</sup> This agreement establishes the project as a legal part of the sponsor. The parameters of employment and project management, delegations of authority, the use and roles of advisory boards, property rights, and the duration and terms of project closure are typically addressed in this document.

The fiscal sponsor must be cautious in selecting projects because it assumes total legal responsibility for the project, and all current and future project employees become direct employees of the fiscal sponsor. This is a serious matter, as any previous legal issue attached to a project is generally absorbed by the sponsor.

Likewise, the sponsor becomes liable for all subsequent legal issues that arise in connection with the project. Until this arrangement concludes, the project is not a legally separate entity. The sponsor's assumption of liability is a necessary component of a CFS relationship. All nonprofits practicing CFS have established sets of criteria used to evaluate prospective projects. This total assumption of legal and financial liability differentiates fiscally-sponsored relationships from so-called conduit or pass-through arrangements, where control and responsibility remain with other parties.

Advisory boards are responsible for providing assistance in the areas of project policy development, fundraising, and organizational development.

<sup>7</sup> Guideline 1, *Guidelines for Comprehensive Fiscal Sponsorship* at <http://www.tides.org/fileadmin/user/NNFS/NNFS-Fiscal-Sponsorship-Guidelines-for-Comprehensive.pdf>

<sup>8</sup> *Id.*

<sup>9</sup> Guideline 7, *Guidelines, Id.*

Ease of entry into community engagement is a key benefit of fiscal sponsorship.

After a project joins the fiscal sponsor, project and sponsor maintain regular contact in order to properly manage all risks. CFS practitioners recommend and sometimes require that projects establish advisory boards that function similarly to a traditional board of directors.<sup>10</sup> Although these advisory boards have no legal or governing authority, they provide an important mechanism of accountability and support for many projects.

Advisory boards are responsible for providing assistance in the areas of project policy development, fundraising and organizational development. They also monitor and evaluate the performance of project directors and provide the fiscal sponsor with advice and recommendations regarding personnel, financial and administrative matters as well as other issues related to their projects.

Likewise, when an existing 501(c)(3) nonprofit transitions into a comprehensive sponsorship relationship, the organization's board of directors often assumes the role of project advisory board. The activities of the new advisory board remain substantially similar to those of the previous board except that fiduciary duties and legal liability are now vested in the sponsor's board of directors, which must exercise final decision-making authority to ensure that the project is in compliance with all state and federal laws.

## EASE OF ENTRY

Ease of entry into community engagement is a key benefit of fiscal sponsorship. The prospect of obtaining 501(c)(3) status and forever-after complying with complex requirements can be daunting to many would-be social entrepreneurs. Organizing under state law, attaining an employment identification number, and filing the lengthy Form 1023 along with other required documents and accompanying fees are the first steps an organization must take to become tax-exempt under IRC §501(c)(3).<sup>11</sup>

After all necessary filings have taken place, it can take many months to hear back from the IRS, which may respond with follow-up inquiries. Although the date of exemption is usually retroactive to the filing date or the date the organization was created, foundations and other donors are understandably hesitant to extend monetary support to groups that have yet to receive an affirmative determination from the IRS. This arduous undertaking siphons time, money and energy from a project, often leaving it “dead in the water.” Costly legal assistance is often necessary and always recommended.

Many projects, such as small grassroots movements, may lack the resources to even begin this process. For others organized with a short-term charitable goal in mind, the process of obtaining an affirmative determination letter from the IRS may take more time than it's worth. Speed is of the essence for many important nonprofit

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<sup>10</sup> Guideline 6, *Guidelines, Id.*

<sup>11</sup> *Lifecycle of a Public Charity* at <http://www.irs.gov/charities/charitable/article/0,,id=122670,00.html>

endeavors. Large nonprofit organizations and their set agendas are often too slow to respond to urgent, emerging issues. For these time-sensitive movements, independent 501(c)(3) status is not a viable option. For many groups unwilling to drain limited resources engaging with the IRS, fiscal sponsorship represents an attractive alternative.

Under a properly constructed CFS relationship, the unincorporated project becomes a program of the fiscal sponsor and will not be burdened with navigating IRS red tape. As the project is now part of a larger nonprofit, its activities become part of the sponsor's exempt activities. The project can immediately solicit and receive funding in the fiscal sponsor's name.

In fulfillment of their fiduciary duties, CFS nonprofits carefully monitor project fund-raising efforts and will sign off on grant applications, RFP's, and legally binding project commitments.<sup>12</sup> Under the legal control of a CFS organization that also runs all back office operations, projects are afforded a great deal of autonomy in both crafting and achieving their goals so long as the activities continue to further the exempt purpose of the sponsor. For groups that need tax-deductible donations to achieve a charitable purpose, fiscal sponsorship is the most straightforward and time-tested alternative to obtaining an affirmative determination letter from the IRS.

## ONGOING COMPLIANCE

Once an organization has received an affirmative determination letter from the IRS, it must meet a host of annual and semi-annual filing requirements under state and federal law.<sup>13</sup> This process is costly and time consuming, but failure to comply properly can result in forfeiture of the organization's exempt status. Once again, these organizations are frequently forced to seek the assistance of costly legal counsel. With CFS, all required informational reporting occurs in a streamlined, consistent, and transparent fashion on the sponsor's Form 990.

The IRS also gains from the organized infrastructure comprehensive sponsors provide. For instance, a fiscal sponsor with 100 projects files one Form 990. This single 990, assembled by experienced professionals, presents all required information for the 100 projects that make up the organization. The IRS thus has to review a single return rather than 100 shorter returns often prepared by nonprofessionals.

CFS organizations also have annual financial audits that serve to maintain the highest standards of accountability and transparency.<sup>14</sup> With over 1.4 million nonprofits operating in the United States<sup>15</sup>, fiscal sponsors serve to ease the burden on the IRS, making efficient use of the corresponding tax dollars spent on the Service's operations.

Comprehensive Fiscal Sponsorship organizations also have annual financial audits that serve to maintain the highest standards of accountability and transparency.

<sup>12</sup> Guideline 5, *Guidelines Id.*

<sup>13</sup> See Ongoing Compliance and Required Filings of a public charity at <http://www.irs.gov/charities/charitable/article/0,,id=122670,00.html>

<sup>14</sup> Guideline 4, *Guidelines, Id.*

<sup>15</sup> The National Center for Charitable Statistics at <http://nccs.urban.org/statistics/quickfacts.cfm>

The back-office support structure inherent in Comprehensive Fiscal Sponsorship creates fluidity and continuity in project operations.

## NURTURING SUPPORT

Some commentators have likened fiscal sponsorship to a pass-through arrangement where the sponsor is used as a vehicle to steer deductible contributions to improper parties and individuals. This description does not stand up to scrutiny. Indeed, even a cursory review demonstrates that CFS is best described as a “capacity nurturing relationship.”

When, after careful consideration, comprehensive sponsors adopt a project, they are not merely extending a mission-consistent program their tax-exempt status in exchange for a fee. The unincorporated project is transformed into a program of the fiscal sponsor. The sponsor and the project are now one and the same. The sponsor has a vested interest in project success, because success or failure is a reflection of the fiscal sponsor’s abilities.

By effectively nurturing thousands of projects, CFS nonprofits such as Colorado Nonprofit Development Center, Community Partners, Earth Island Institute, Tides Center and Third Sector New England have built up outstanding reputations for growing capacity and fostering positive societal transformations. In order to fulfill their missions and protect and enhance hard-earned brand equity, a fiscal sponsor must take all necessary steps to maximize the potential of the projects it serves.

When a comprehensive sponsor adopts a project, the project benefits immediately from its interactions with the sponsor’s experienced staff and well-designed systems. The sponsor handles all aspects of finance, administration, human resources, governance, compliance and risk management, enabling project teams to focus all their talents on project advancement.

This expertise relieves project leaders of the need to invest precious resources in creating infrastructure. It also frees up significant time leaders might otherwise spend hiring, training, monitoring and retaining the staff necessary to perform these critical administrative functions. Many fiscal sponsors see their role as helping to build the internal capacity of projects and project staff. In those relationships, training and institutional knowledge transfer is part of the service package.

The back-office support structure inherent in CFS creates fluidity and continuity in project operations. With typical small to mid-sized stand-alone organizations, one to several individuals provide all of the above functions often while being tasked with other duties. If key staff members become unavailable – even for a brief period – other members of the organization, though not always trained or qualified, must fill this void.

As staff attempt to perform job functions they are not trained to handle, while scrambling to fulfill their own duties, the mission inevitably suffers. The level of in-depth, consistent support that comprehensive fiscal sponsors provide ensures stability and eliminates inefficiencies, resulting in optimal usage of project funds and talent. This, of course, maximizes the societal return on investment.

The supportive role CFS organizations provide costs money. Like all nonprofits and for-profit programs, effective CFS requires that funds be allocated to cover administrative and back office expenses. Some CFS organizations direct a portion of a project's funds towards administrative expenses when the funds are spent by the project. Others make the allocation as funds are received. Either way, CFS offers high quality services – most often at a cost lower than possible for small to-medium independent nonprofits.

Even large projects may find that the quality service and support offered by CFS are advantageous and cost effective. Much of these savings are achieved through economies of scale. The large size and unified infrastructure of most CFS organizations create economies of scale otherwise unavailable to stand-alone smaller entities. This maximizes administrative efficiencies while minimizing the costs attributable to back office support and overhead.

Large comprehensive sponsors are able to utilize their size and corresponding bargaining power to secure better coverage at favorable prices on health insurance coverage and other fringe benefits. The substantial benefits fiscal sponsors provide all employees make CFS projects enticing employment options, attracting well-qualified, passionate job applicants.

Capacity building is also emerging as a key component of CFS, adding more value to the projects served. Some sponsors offer training seminars and webinars to complement their back office support. Through these offerings, projects are schooled by nonprofit leaders on diverse topics such as fundraising, strategic planning, information technology, and diversity and inclusion. Some sponsors further build capacity by providing projects with periodic assessments, crafting solutions to the myriad of issues nonprofits commonly face.

Surprisingly, terminology such as “client” and “fee” – that does not accurately reflect the true legal structure of CFS relationships – persists both within and outside the fiscal sponsorship community. Such terms add ambiguity and fuel skepticism among those not familiar with this brand of fiscal sponsorship. Widespread adoption of consistent language by the fiscal sponsorship sector will serve to eliminate confusion from project staff and prospective funders. Accurate terminology such as “project” rather than “client” and “project administrative expense” instead of “client fee” is gaining currency as a clearer understanding of the parameters of CFS evolves.

Capacity building is also emerging as key component of Comprehensive Fiscal Sponsorship, adding more value to the projects served.

Cash and in-kind donations that support specific projects are frequently solicited by sponsored project staff.

## ADDRESSING MISCONCEPTIONS

### **DONOR ADVISED FUND VS. FISCAL SPONSORSHIP**

Despite the success and growth of fiscal sponsorship, certain misconceptions surrounding the practice of CFS linger. One concern occasionally voiced by foundations is that fiscal sponsors are actually “sponsoring organizations” that manage donor advised funds. The Pension Protection Act of 2006 created new rules and restrictions governing donor advised funds, putting foundations on heightened alert.

However, a brief examination of how a sponsoring organization maintaining donor advised funds is defined and how this definition differs from CFS makes it apparent that, with rare exceptions<sup>16</sup>, they are not the same or even remotely similar.

Prior to the Pension Protection Act, the term “donor-advised fund” was not defined in the Code or Regulations. IRC 4966(d)(2) now defines the term as “(1) a fund or account owned and controlled by a sponsoring organization, (2) which is separately identified by reference to contributions of the donor or donors, and (3) where the donor (or a person appointed or designated by the donor) has or reasonably expects to have advisory privileges over the distribution or investments of the assets.”

All three elements of the definition must be met in order for a fund or account to be treated as a donor-advised fund.”<sup>17</sup> The practice of CFS does not qualify under this definition.

Starting with the second prong, a distinct fund or account of a sponsoring organization must refer to contributions of a donor or donors, “such as by naming the fund after a donor, or by treating a fund on the books of the sponsoring organization as attributable to funds contributed by a specific donor or donors.”<sup>18</sup>

Nonprofits practicing CFS do not maintain accounts that identify donors by reference. Rather, funds donated to specific projects are typically held in accounts referencing the project’s name or purpose such as “Immigrant Support Services” or “Save the Right Whales.” No reference is made to the actual donor, as that individual or entity is irrelevant for purposes of administering project funds. Once a donation is made, all control over those funds previously exercised by the donor ceases.

Cash and in-kind donations that support specific projects are frequently solicited by sponsored project staff. In this respect, a donor can reasonably expect that the contribution will go toward that particular project of the fiscal sponsor. However, once the donation is made, the donor has no actual or implied influence on the fiscal sponsor’s use of the funds.

<sup>16</sup> See Colvin, Esq., *Is a Fiscal Sponsorship Account Maintained for a Project by a Public Charity Also a Donor-Advised Fund?* at [http://www.fiscalsponsorship.com/DAF%20definition%20for%20fiscal%20sponsor%20\\_00211211\\_.pdf](http://www.fiscalsponsorship.com/DAF%20definition%20for%20fiscal%20sponsor%20_00211211_.pdf)

<sup>17</sup> IRC 4966(d)(2) see also *Donor-Advised Funds Guidesheet* at [http://www.irs.gov/pub/irs-tege/donor\\_advised\\_guide\\_sheet\\_073108.pdf](http://www.irs.gov/pub/irs-tege/donor_advised_guide_sheet_073108.pdf)

<sup>18</sup> *Donor Advised Funds Guide Sheet Explanation* at [http://www.irs.gov/pub/irs-tege/donor\\_advised\\_explanation\\_073108.pdf](http://www.irs.gov/pub/irs-tege/donor_advised_explanation_073108.pdf)

Allowing foundations and the general public to contribute to specific projects of Model A sponsors is identical to the practices that large nonprofits operating multiple programs have successfully engaged in for decades. For example, when a donation is made to the National Geographic Society, “donors can designate their gifts to one or more of the five major areas of the National Geographic Society’s Mission Programs: education, research and exploration, conservation, cultures and public outreach.”<sup>19</sup>

Also offered are “additional designation opportunities ranging from purpose-specific funds to special initiatives.”<sup>20</sup> For example, donors may make charitable contributions that will go into a fund dedicated to saving the Amboseli Lions.<sup>21</sup> If this were not possible, a separate nonprofit would have to be created to protect these lions, a time-consuming undertaking that may not be set up until the lions are further endangered.

Without the ability to donate to this specific project of National Geographic, individuals would not be able to offer direct financial support to the project and receive a tax deduction. Using the Public Broadcast Service as another example, donations to PBS may be directed to local stations, which often encourage donors to designate support for specific programs.<sup>22</sup>

Donations to CFS projects and other nonprofits operating several programs are, properly maintained in accounts that reference the project or campaign, never the individual donor. After these donations are made, donors have no control of the disposition of the funds. CFS practitioners do not maintain donor advised funds and are, therefore, not sponsoring organizations.

### **NONPROFITS AND THE GREAT RECESSION**

Although typically utilized on behalf of unincorporated projects, CFS is also an option worth considering for existing 501(c)(3) public charities. In today’s competitive climate, even financially healthy nonprofits are seeking ways to reduce costs and increase efficiencies. Many other cash-strapped organizations are being pressured to alter their mission and composition through merger. Although this trend is in its early stages, a small but growing number of nonprofits are embracing CFS as a model enabling both short-term regrouping and long-term stability.

### **CONTINUED NEED**

The Great Recession hit the independent sector before it steamrolled Wall Street and Main Street, and its devastating effects continued to affect nonprofits even after the dust had settled elsewhere. Many believe the nonprofit landscape has been changed permanently. Against this backdrop nonprofits faced immense pressure to

Many believe the nonprofit landscape has been changed permanently. Against this backdrop nonprofits faced immense pressure to merge with other organizations or fold altogether.

<sup>19</sup> National Geographic Society, Donation FAQ page at <http://www.nationalgeographic.com/donate/questions.html#specify>

<sup>20</sup> *Id.*

<sup>21</sup> National Geographic’s Maasailand Emergency Fund Donation page at <https://donate.nationalgeographic.org/SSLPage.aspx?pid=608&srcid=608>

<sup>22</sup> Support PBS at [http://www.pbs.org/aboutpbs/aboutpbs\\_support.html](http://www.pbs.org/aboutpbs/aboutpbs_support.html)

Having more players in the “marketplace of ideas” ensures that innovative ideas are brought to the forefront and old, worn-out models fall by the wayside rather than becoming institutionally entrenched.

merge with other organizations or fold altogether. Much of this pressure is coming from foundations and government agencies that support nonprofit endeavors. We’ve seen this dynamic before in down cycles.

“Too many nonprofits!” can be a popular but misguided mantra voiced by foundations during periods of economic crisis. And it is important to note that the number of private foundations has ballooned by more than 85% over the past 15 years – twice the growth rate of the nonprofits they serve.<sup>23</sup>

The nonprofit sector has indeed experienced substantial growth over the past decade. However, this growth came about as the overall economy expanded, government social service programs were dramatically cut or eliminated, and civil liberties were being attacked. At the same time, income and wage disparities between rich and poor grew to unprecedented levels, and the realities of climate change were just beginning to be felt.

This is precisely the time that the need for charitable services would logically spike. And this need remains as nonprofits play a vital role in picking up the pieces and creating a sustainable future.

Merger, though appropriate in certain circumstances, is a costly and immensely complex option that will not always achieve an optimal or even positive outcome.

Multiple nonprofits with overlapping, complementary services are not necessarily indicative of inefficiencies requiring remediation. Indeed, one commentator suggests that there are actually too few good nonprofits.<sup>24</sup>

There is no rule or law dictating that only one nonprofit may offer a particular service in a given area. Competition breeds innovation and drives efficiencies. Having more players in the “marketplace of ideas” ensures that innovative ideas are brought to the forefront and old, outmoded models fall by the wayside – rather than becoming institutionally entrenched.

Further, although it may often appear that two nonprofits are performing identical functions, a closer examination will often reveal that their operations are substantially distinct or offered within a distinct geographic area.

### **COMPREHENSIVE FISCAL SPONSORSHIP FOR THE 501(C)(3)**

Many nonprofit inefficiencies reside at administrative and not programmatic levels. Comprehensive Fiscal Sponsorship addresses these issues by offering a “safe haven” for merger-leery nonprofits, preserving their missions while providing high-level administrative support and the time and space to regroup. Unlike merger, there is never any sense that one organization is being “overtaken” by another, undermining employee morale and service to constituents.

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<sup>23</sup> National Center for Charitable Statistics

<sup>24</sup> Masaoka, Jan, *Too Many Nonprofits? No—There Aren't Enough Good Nonprofits*, The Blue Avocado at <http://www.blueavocado.org/content/too-many-nonprofits-no-there-arent-enough-good-nonprofits>



Certainly, the consequences of merger can be devastating. Depending on the bargaining power of the parties, a nonprofit may find that post merger its mission is diluted or completely lost. The real losers are the constituents and “causes” squeezed through the cracks during these consolidations. So, the call for nonprofit merger must be carefully weighed against its possible consequences.

“Far from being a hostile takeover or a predatory acquisition that benefits one party only, a fiscal sponsorship transition, done properly, is a creative alternative whose objective is to enable the development and nurturing of grassroots solutions to community problems.”<sup>25</sup>

The organization retains its own brand identity and unique web presence with CFS. Absent are time and asset-consuming negotiations over assets or programmatic control or direction since the sponsored project will continue to control its funding and programs. There is no potential board clash as boards may stay intact, providing an extra layer of oversight in conjunction with the fiscal sponsor.

Nonprofits transitioning into a CFS relationship go through a process similar to that of unincorporated projects, with a few minor variations. This transition is cheaper and far less complex than a merger or acquisition. Outside consultants, accountants and legal counsel are often unnecessary. Mission compatibility remains a threshold requirement.

The employees of the nonprofit become employees of the sponsor, gaining access to attractive fringe benefits administered by the sponsor. Operating funds of the nonprofit are typically transferred into an account held by the sponsor in the name of the project. However, funds not needed to support project operations as well as other assets, both real and intangible, may be retained by the nonprofit in its own separate accounts.

A memorandum of understanding specifically tailored for nonprofit projects should clearly define the parameters of the relationship. If this option is exercised, meticulous records must be maintained by both fiscal sponsor and the nonprofit, fencing off assets subject to the sponsor’s control from those that remain vested with the independent 501(c)(3).

While the project is under the supportive umbrella of a CFS practitioner, its corporate and 501(c)(3) designation will not be used in support of the CFS project’s purposes. If all staff and assets are transferred to the sponsor, the nonprofit essentially goes into hibernation until the project resumes independent operations. When and if independent operations resume and the sponsored project is transferred back to the 501(c)(3), the entire fund balance and other assets residing with the sponsor are directed back to the nonprofit.

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<sup>25</sup> Spack, Jonathan, *Let’s Slow Down the M&A Express*, TSNE ED Forum at [http://www.tsne.org/edforum/slow\\_down\\_merger\\_express](http://www.tsne.org/edforum/slow_down_merger_express)

Comprehensive Fiscal Sponsorship offers a cheaper, faster, less stressful alternative to merger. Any nonprofit feeling the pressure to merge should carefully consider all available options including Comprehensive Fiscal Sponsorship.

The advantages of Comprehensive Fiscal Sponsorship are by no means limited to small or new organizations. The flexibility, reduced burden on project directors, greater capacity, professional expertise, and cost savings flow to fiscally sponsored projects of all sizes.

Undoing a merger can be even more complex than creating one, if not impossible. The process for terminating a relationship with a fiscal sponsor, addressed in the “Ease of Exit” section below is far simpler. CFS offers a cheaper, faster, less stressful alternative to merger. Any nonprofit feeling the pressure to merge should carefully consider all available options including CFS.<sup>26</sup> Likewise, financially healthy nonprofits simply interested in increasing back office efficiencies and renewing mission focus may wish to investigate what CFS has to offer.<sup>27</sup>

### **INCUBATOR ONLY?**

Some observers mistakenly believe that fiscal sponsors are limited to serving as incubators for future independent nonprofits. However, like professional employer organizations<sup>28</sup> and other shared service models utilized by the private sector, fiscal sponsors frequently play a long-term role in the functioning of charitable endeavors.

As far as Comprehensive Fiscal Sponsorship practitioners are concerned, serving as an incubator to future nonprofits is the exception rather than the rule. Results of the most thorough survey of fiscal sponsors to date indicate that less than half of the projects of fiscal sponsors with over 50 projects have sought to be independent 501(c)(3) nonprofits.<sup>29</sup> The rate of retention is as high as 80 to 90% with some organizations.

Although CFS practitioners generally adopt and foster the development of young, experimental projects, after these projects mature, they often remain sponsored programs. The advantages of CFS are by no means limited to small or new organizations. The flexibility, reduced burden on project directors, greater capacity, professional expertise and cost savings flow to fiscally sponsored projects of all sizes. These advantages, both measurable and intangible, often render “leaving the nest” an unpalatable option for many, if not most, comprehensively sponsored projects.

## **THE INTANGIBLE BENEFITS OF COMPREHENSIVE FISCAL SPONSORSHIP**

Every day, charitable organizations and their staff and volunteers add tremendous value to our society. This value is often impossible or prohibitively expensive to quantify. A group offering companionship to the elderly in their last days may not add to our national GDP, yet has a profound effect on those served.

An organization that facilitates physical activity and teaches inner city children healthy eating habits may be responsible for millions of dollars in medical cost reductions years down the road for which it will never receive credit. An environmental nonprofit that, through litigation, protects a water supply from pollution

<sup>26</sup> For more information see Spack, Jonathan, *Fiscal Sponsorship as a Nonprofit Merger Alternative* at [http://www.tsne.org/edforum/fiscal\\_sponsorship\\_merger\\_alternative](http://www.tsne.org/edforum/fiscal_sponsorship_merger_alternative)

<sup>27</sup> All members of the National Network of Fiscal Sponsors practice CFS. <http://www.tides.org/?id=212>. A national directory of fiscal sponsors can be found at <http://www.fiscalsponsordirectory.org/>

<sup>28</sup> See National Association of Professional Employer Organizations at <http://www.napeo.org/>

<sup>29</sup> *Fiscal Sponsorship Field Scan* at [http://www.tidescenter.org/fileadmin/tc\\_pdfs/WP\\_FiscalSponsorFieldScan.pdf](http://www.tidescenter.org/fileadmin/tc_pdfs/WP_FiscalSponsorFieldScan.pdf)

saves thousands of lives, though attributing a single saved life to that organization's actions can be elusive.

Likewise, Comprehensive Fiscal Sponsorship provides projects that create societal value and advance culture with a wealth of benefits that are not readily identifiable and rarely mentioned. Nevertheless they are real. As soon as a project becomes fiscally sponsored and these intangible benefits begin to accrue, projects often reevaluate their independent aspirations.

Because CFS staff work with a diverse group of projects, they gain valuable knowledge that they can then pass on to individual projects. Examples include spotting and flagging potential financial and human resource concerns before they become problems, understanding the intricacies of funders' requirements, and thinking strategically about project needs. CFS projects are, therefore, in a better position to weather economic downturns, navigating potential human resource issues and stretching donor dollars farther.

Beyond back office operations, several sponsors now provide their projects with capacity building services designed to infuse the projects with the capabilities and best practices that the sponsors themselves operate under.

These sponsors foster a culture of sharing – with shared back-office operations being only one component of an accessible network created through CFS. Fiscal sponsors that have operated for decades offer their projects access to an extensive list of contacts and relationships cultivated over many years. Individuals and groups that have worked with comprehensive sponsors in the past realize the immense value these organizations bring.

Thus, frequently they are willing to make themselves available, extending their expertise and contacts to sponsored projects. Individual projects themselves derive great value from sharing experiences, lessons and best practices with one other.

### **FOCUS AND INNOVATION**

Several organizations are taking the culture of sharing to another level, operating 'nonprofit centers,' buildings that offer both affordable and stable office space to nonprofits and fiscally sponsored projects.<sup>30</sup> Traditionally, nonprofits have been subject to the ebbs and flows of the real estate market. When rent rates balloon, these groups are often forced to relocate to the fringes of urban centers impeding access to public transportation and the constituents they serve.

Nonprofit centers provide a solution to this persistent problem. They may consistent rents – often below market value – and may also offer shared conference spaces, IT support, and even lunchtime seminars and yoga classes.<sup>31</sup> Having

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<sup>30</sup> See The Nonprofit Centers Network at <http://www.nonprofitcenters.org>

<sup>31</sup> Sacha Pfeiffer, *A haven in a high-rent world*, The Boston Globe at [http://www.boston.com/news/local/massachusetts/articles/2008/04/02/a\\_haven\\_in\\_a\\_high\\_rent\\_world/](http://www.boston.com/news/local/massachusetts/articles/2008/04/02/a_haven_in_a_high_rent_world/)

Comprehensive Fiscal Sponsorship keeps the engines of their projects humming, allowing passionate mission-driven project leaders and staff to focus on the activities that are core to the project's existence.

Sometimes a project reaches a point in its development where a spinoff from its fiscal sponsor is appropriate.

significant numbers of mission driven groups in one location promotes collaboration and increases networking opportunities through both planned networking events and on an informal basis.

As noted, Comprehensive Fiscal Sponsorship furnishes projects with comprehensive personnel policies, liability insurance, and financial and administrative expertise. It also keeps projects abreast of and trained on new government regulations as they arise. Having these reliable operational mechanisms in place affords project leaders peace of mind, eliminating many of the stresses that can derail an operation. This intangible quality cannot be underestimated.

A project leader's time and thoughts will not be sidetracked by the plethora of issues inherent in managing the back office operations of any organization. Project staff works towards mission fulfillment knowing that administrative tasks and compliance matters are being efficiently addressed. CFS keeps the engines of their projects humming, allowing passionate mission-driven project leaders and staff to focus on the activities that are core to the project's existence.

## EASE OF EXIT

Sometimes a project reaches a point in its development where a spinoff from its fiscal sponsor is appropriate. It is imperative that the process and terms of any such separation be anticipated and memorialized in the memorandum of understanding or similar agreement. Otherwise, unnecessary complications may occur. Under the typical memorandum of understanding, the project may retain the funds raised and allocated for it along with any real and intangible property it has developed so long as it attains its own 501(c)(3) tax-exempt statuses or locates another suitable fiscal sponsor.

For a number of reasons, projects occasionally cease to operate without being spun off into new entities. The project may have fulfilled its purpose or is no longer financially viable. Winding up a project's operations highlights the final advantage fiscally sponsored projects may realize: ease of exit.

When a nonprofit organization winds up its operations, it must do so in compliance with IRS requirements. This usually entails, at a minimum, completing Schedule N on Form 990 and listing the disposition of organizational assets in excruciating detail.<sup>32</sup> When a Comprehensive Fiscal Sponsorship project terminates its operations, all assets previously maintained by the project will simply be spent on purposes in furtherance of the sponsor's mission.

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<sup>32</sup> *Termination of an Exempt Organization* at <http://www.irs.gov/charities/article/0,,id=156422,00.html>

Further, individual states have various regulations and procedures that must be followed when a registered entity dissolves. None of these complicated filing requirements are present when a fiscal sponsored project is terminated. The dissolution of the project is simply reflected on the fiscal sponsor's Form 990. The use of fiscal sponsorship eliminates considerable expenses (often legal) associated with complying with dissolution.

## CONCLUSION

Savvy, forward-looking funders are taking notice of the numerous advantages that comprehensive fiscal sponsors offer and are becoming more receptive to funding programs that find homes at credible sponsors. These fiscal sponsors increasingly play the role of project authenticator, vouching for a project's credibility to prospective funders. Becoming a program at a reputable Comprehensive Fiscal Sponsorship practitioner conveys several messages to foundations, other funders and the public. It says:

- 1) This project has been through a thorough evaluation process that determined it has the capacity to achieve its underlying objectives.
- 2) All back-office operations of the project are managed by competent, experienced professionals ensuring maximum transparency.
- 3) Project staff members receive proper compensation and preferable benefits, increasing retention and minimizing burnout.
- 4) The project will be able to focus on the mission and not be derailed by administrative burdens and complex compliance issues.

A program utilizing Comprehensive Fiscal Sponsorship also communicates that it has the wherewithal to recognize its strengths as a passionate, mission-driven organization that properly addresses its need for efficient, seasoned back office support.

### NEW SOLUTIONS FOR NEW REALITIES

"Fiscal sponsorship" is still sometimes referred to – incorrectly – as "fiscal agency."<sup>33</sup> Fortunately, this outdated terminology is rapidly disappearing. Similarly, old assumptions regarding nonprofits and the social sector are being shed as new realities demand innovative solutions.

For many years, a premium was placed on the independence of organizations operating in the nonprofit sector even as the private sector realized the advantages offered through shared services, collaborative pricing and strategic outsourcing. This thinking is both illogical and counterintuitive. Crisis breeds opportunity and organizations practicing Comprehensive Fiscal Sponsorship represent part of a

The use of fiscal sponsorship eliminates considerable expenses (often legal) associated with complying with dissolution.

Crisis breeds opportunity and organizations practicing Comprehensive Fiscal Sponsorship represent a piece of a young but rapidly maturing movement in the social sector that thrives on the sharing of resources and information.

<sup>33</sup> Under the law of agency, an agent acts on behalf of another person or organization. That entity has the power to direct and control the activities of its agent. Using this terminology to describe the relationship between a 501(c)(3) and a project implies that the project exerts control over the nonprofit charity. To comply with IRS dictates and assure accountability,

the sponsor must walk a fine line and play the role of steward; allowing a great deal of project autonomy while exercising final authority by only signing off on contracts and other encumbrances that further the charity's exempt purposes and comply with all applicable laws.

Comprehensive Fiscal Sponsorship offers a realistic, honest approach to not only survive, but excel in the challenges of our day and those that lie ahead.

young but rapidly maturing movement in the social sector that thrives on sharing resources and information.

Creative solutions abound including the multitenant nonprofit centers now found throughout the world and alliances of nonprofits that turn over their back office operations to one supporting organization, such as the MACC Commonwealth currently being pioneered in Minnesota.<sup>34</sup> Likewise, innovative ventures like Ann Arbor's Nonprofit Enterprise at Work (NEW), through their npServ™ system, offer nonprofits shared IT services that reduce hardware and software costs, increase reliability, enhance data security and allow for easy remote access.<sup>35</sup>

These forward-thinking organizations and alliances breathe long-term stability into groups that, like themselves, are dedicated to strengthening the presence, voice and effectiveness of civil society. Though the methods employed vary, all of these groups enable nonprofits and progressive grassroots movements to focus on mission-related activities by assuming or sharing time-consuming and often complex tasks that, though essential, are not mission-related. By transferring jobs to organizations better-positioned to perform them efficiently and effectively, precious time and money are saved, maximizing the potential impact of the nonprofit sector.

It is crucial to the future success of Comprehensive Fiscal Sponsorship and the charitable sector in general that foundations and individuals providing financial support to nonprofits understand and embrace these solutions. The bottom line is that comprehensive fiscal sponsorship stretches charitable dollars further and more effectively than typical stand-alone small to midsized nonprofits – and even many larger organizations can. Comprehensive fiscal sponsorship offers a realistic, honest approach to not only survive, but excel in the challenges of our day and those that lie ahead.

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<sup>34</sup> MACC Commonwealth at <http://maccommonwealth.org/>

<sup>35</sup> Nonprofit Enterprise at Work (NEW) at <http://www.new.org/whatwedo/technology.html>



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