Fiscal Sponsorship

A brief article describing how fiscal sponsorship works including the legal responsibilities and duties of a fiscal sponsor and the sponsored organization.

DISCLAIMER

This material should be used as a reference only. **It is not a substitute for legal advice.** The law changes frequently. The information provided may not apply to your specific set of facts or circumstances. If you require legal advice, please consult your attorney. Nonprofit organizations are encouraged to contact Michigan Community Resources to apply for pro bono legal assistance.

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What is Fiscal Sponsorship?

Fiscal sponsorship is one entity (the "sponsor") accepting and managing funds for another (the "beneficiary"). As a fiscal sponsor, an entity collects all the funds for either another organization or a specific project and then disperses the funds to the organization or project as needed. Each beneficiary will generally apply for its own grants from public agencies, foundations, corporations and individual donors, using the tax-exempt status of the sponsor to assist in obtaining the donations. The tax-exempt donation is then made to the fiscal sponsor, which earmarks the funds for the donor's intended beneficiary. This allows the beneficiary to apply to prospective donors under the auspices of 501(c)(3), increasing both the array of potential donors and the donors' incentive to donate. A fiscal sponsorship requires a written agreement between the fiscal sponsor and the beneficiary outlining the terms of their relationship.

All beneficiary programs must be pre-approved by the fiscal sponsor. Approval requires meeting both the requirements set by 501(c)(3) nonprofit standards and those of the particular sponsor's mission and goals. After approval the beneficiary must continue to demonstrate compliance throughout the project or program.

There are various benefits and limitations associated with a fiscal sponsor relationship. By understanding these considerations, an entity is better able to determine whether a fiscal sponsor relationship may be right for it. Evaluating how the benefits may further the goals of the beneficiary program and how the limitations may hinder its efforts, the beneficiary can determine whether it should pursue the possibility of fiscal sponsorship. In addition, the fiscal sponsor must also evaluate the costs and obligations of providing sponsorship and the value of supporting the beneficiary program.

Benefits of Fiscal Sponsorship

Beneficiary Benefits

Several foundations, government agencies, and corporate sources only grant donations to nonprofit organizations with IRS tax-exempt status. To be considered exempt, an organization must hold a current 501(c)(3) acknowledgment of tax-exempt status letter from the IRS. Rather than attempting to obtain 501(c)(3) certification on their own, new or emerging organizations with missions and goals consistent with the sponsor's can work with a fiscal sponsor to realize the benefits of tax-exempt status.

Fiscal sponsorship enables the beneficiary organization to receive the benefits of 501(c)(3) certification without the long process of obtaining certification. Once fiscal sponsorship is obtained, the beneficiary organization can apply for funds from the government, foundations, and corporations that would otherwise be unavailable. Due to the reputation of a fiscal sponsor, many foundations and government entities may be familiar with, and comfortable donating to, a proven fiscal sponsor rather than an uncertain, unknown, project or organization.

Sponsor Benefits

Organizations with 501(c)(3) certification can benefit by choosing to become fiscal sponsors. Fiscal sponsorship allows the fiscal sponsor to collect an administrative fee from the beneficiary on any money granted. These proceeds enable the organization to increase its operating budget. As discussed below, fiscal sponsorship requires that each sponsored program share a purpose with its sponsor. It also requires that the sponsor retain some control of the administration of funds in order to ensure that the spending is in furtherance of the proposed project and the purpose of the sponsor. Sponsorship, therefore, enables the fiscal sponsor to grow its presence in the very areas of concern in which it is already involved.

Limitations of Fiscal Sponsorship

Beneficiary Limitations

A beneficiary organization is limited in several ways by entering into a fiscal sponsorship relationship with a non-profit organization. Though the beneficiary organization can receive donations under the auspices of a 501(c)(3), it does not have independent 501(c)(3) status. The project does not receive tax exempt purchasing power, nor any of the other benefits associated with being a 501(c)(3).

The beneficiary project must remain non-commercial. It is not permitted to be organized for or seek to make a profit, or to have investors. To do so would not only jeopardizes its agreement with the sponsor, but also the sponsor's 501(c)(3) status. The IRS requires that the sponsor remain non-profit. If any of its beneficiary projects were to become for-profit, the certification for the sponsor and all of its projects would be lost. The beneficiary project and program is, therefore, limited in its scope and its potential donors once it enters into a fiscal sponsorship arrangement with a 501(c)(3).

Vision and purpose are also limited in a fiscal sponsor relationship. Fiscal sponsorship requires that the project be in furtherance of the sponsor's purpose and vision. In order to apply its 501(c)(3) exemption to a beneficiary project, the IRS requires that the project be in line with the sponsor's mission. Any notable differences in purpose or vision are in breach of the sponsorship agreement and jeopardizes the sponsor's tax-exempt status.

Projects must remain apolitical. Political themes and purposes aimed at influencing elections or political objectives are barred from 501(c)(3) exemption, and therefore there is no organization capable of sponsoring this type of beneficiary project.

Compliance with the central purpose also places several limitations on the day-to-day function and operation of a beneficiary project. Fiscal sponsorship requires pre-approval of both the purpose and budget. Further, the beneficiary project must continually demonstrate that its usage of the funds is in in-line with the proposed mission and budget. The sponsor is also given oversight and supervisory privileges. All three are done in order to protect the sponsor's 501(c)(3) status. With this oversight, the beneficiary project's flexibility in achieving its goal may be limited.

<u>Sponsor Limitations</u>

As discussed above, the sponsor is limited in providing its service and status to beneficiary projects that share its tax-exempt purpose. In ensuring this, the sponsor incurs substantial responsibility and administrative burdens: managing each project's funds, keeping their donations separate, making sure that they are adhering to the non-profit guidelines, and overseeing projects. Each beneficiary project taken on by the sponsoring non-profit organization brings new burdens and these increasing burdens create additional strain on the sponsor's internal resources. Each non-profit organization, accordingly, is only able to enter into a fiscal sponsor relationship with a limited number of groups or individuals.

Conclusion

Entering into or creating a fiscal sponsorship can create excellent financial opportunities for a new or developing organization or program. Sponsorship increases the availability of grants and donations, and brings together groups and individuals working towards a common goal. At the same time, sponsorship can impose several limitations. An organization must therefore weigh the independence needed, the availability of private investors, and the desire to make a profit from the work, against the need for government, corporate, and individual tax-exempt grants. For the right types of projects, and the right non-profit entities, fiscal sponsorship can provide significant, previously untouched, resources.