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Fiscal Sponsorship Q&A

Your organization may be too new — or too small — to have obtained its tax-exempt status. Or, if you're well-established, you may have an opportunity to expand your programs by joining forces with a smaller or newer organization. In either case, fiscal sponsorship is a structural arrangement with another organization that you may want to consider.

Here are the answers to some questions you may have about this special relationship.

Q: What is fiscal sponsorship?

A: It's a relationship in which a not-for-profit with 501(c)(3) status sponsors a societal-minded project/group that doesn't have tax-exempt status. The fiscal sponsor is legally and financially responsible for the project. "Project" typically refers to either an ongoing group or a one-time project.

Q: How does it work?

A: The fiscal sponsor is responsible for managing funds and acts as a "guardian" for the donations and grants the project receives. Donations are made to the sponsor, which qualifies the donors for a tax deduction. The sponsor employs the staff that works on the project and monitors activities to the same extent it monitors any of its other programs.

It's the sponsor's responsibility to ensure that the project is within its mission and doesn't adversely affect its tax-exempt status.

Q: What are the benefits for the "sponsoree"?

A: Sponsorship allows an entity to fulfill a mission without going through the process of incorporating and applying for tax-exempt status. The sponsor can provide the back-office support that small not-for-profits often lack.

Also, because donations to a 501(c)(3) organization are tax-deductible, the potential for donations is greater. And the sponsor may have much greater name recognition than the smaller or newer organization.

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Q: What are the pros and cons for the sponsor?

A: The sponsor benefits because the added project could bring additional recognition in the community for "doing more." This, in turn, might attract new funders. The downside is that the sponsor may assume responsibilities that carry unanticipated risks or require additional infrastructure or cost not beneficial to the organization. The added responsibilities also might divert the sponsor from its primary programs and purpose.

Q: What types of groups are right for fiscal sponsorship?

A: New not-for-profits who want to start operating, but have yet to receive 501(c)(3) status, are logical sponsoree candidates. So are very small groups that lack infrastructure. Sometimes even individuals are sponsored. For example, Fractured Atlas is a not-for-profit that sponsors a national community of individual artists as well as art organizations.

Q: What's the difference between a fiscal agent and a fiscal sponsor?

A: A fiscal agent accepts donations and merely moves them on to the intended recipients. The IRS regards such donations as a direct donation to the intended recipients. A fiscal sponsor is legally responsible for the project and the funds. The sponsor doesn't merely receive the funds — it controls the project and accounts for the activity in its financial statements and on Form 990.

Q: What should you look for in a fiscal sponsor?

A: The two entities should have a similar mission and vision. And the sponsor should be financially strong enough to enable the sponsoree to run continuously without interruption. Look for elements — and your financial advisor can help you with this — such as: strong internal controls based on Generally Accepted Accounting Principles and other federal regulations, written policies and procedures for administration and risk management, and enough staff to fulfill agreed-upon services.

Q: How do you get started?

A: Both organizations need to work out the terms of the relationship before getting started, such as who will have the authority to make decisions. You'll also need to determine how disbursing funds will be handled and who will take care of reporting requirements. For example, typically the sponsor is responsible for fiscal reporting to the foundations or other grant-giving bodies. You also should agree on how long the project will last, as well as how assets and activities will be severed from the sponsor when the two entities part ways.

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