Fiscal Sponsorship: What Does it Mean for You?

As the leader in global giving, CAF America often receives questions from both prospective donors and charities asking whether we offer fiscal sponsorship services. The existing definition of "fiscal sponsorship" leaves significant space for interpretation, however, it is a term that has been resurfacing with increased frequency. We want to take this opportunity to dig deeper into this concept, exploring the various scenarios that can be considered to constitute "fiscal sponsorship". Our goal here is not to propose a solution on how to reconcile these models, but merely to provide a brief overview of how they function. More importantly, we encourage our readers to consider whether we all are asking the right questions.

The environment for fledgling US charities is a tough one. High initial overhead costs and a resource-intensive 501(c)(3) (or other) registration process create formidable barriers that charitable groups must overcome before they are able to scale up and out. Furthermore, establishing an effective mechanism for foreign organizations to receive tax-effective donations from US donors can be burdensome for those international organizations.

Because of this, some US charities offer services as fiscal sponsors, through an arrangement in which an existing charitable organization provides a tax-exempt home for groups or projects that align with their mission. While there are different models for fiscal sponsorship, the underlying premise is the same: an established 501(c)(3) provides a means for another group to receive tax-effective donations. Models of fiscal sponsorship can vary drastically, so it is important for charities looking for sponsorship to know what services they are looking for and what types of organizations provide the model they want.

Is your group or project unregistered? You'll be looking at what some in the field call "Model A", where the sponsor actually takes ownership and assumes all control over the project. Legally, your project becomes part of the established 501(c)(3).

Similar to this, "Model B" results in the project be controlled by the sponsor "but the actual operation of the project is contracted out to a separate legal entity". This results in the sponsor having far more control over the project than in the following scenario, Model C, but not as much control as in Model A.

Is your group a legal entity but needs a way to offer tax-effective donation options? This scenario, often called "Model C", is effectively a grantor-grantee relationship. You could be a for-profit entity that merely wants to raise money for a charitable cause, such as funding and supporting a water access program. Or you could be an international organization that is charitable in nature, but because you are located abroad cannot raise or tax-receipt funds directly from US donors.

The Model C version of fiscal sponsorship is relatively hands-off for the sponsor and the sponsored entity. In this arrangement, the sponsor has the responsibility for ensuring that the funds that are intended for the sponsored party are used specifically on the charitable project for which they are given. When supporting foreign organizations' charitable projects, this arrangement is indistinguishable from a traditional expenditure responsibility (ER) grantor-grantee relationship.

Fiscal sponsorship is a convenient means for receiving tax-effective donations but it does come with some complications, both for the sponsor and the organization itself:

- There is no defined IRS designation for fiscal sponsorship – the practice occupies a gray area when it comes to tax filing and exemptions. The National Network of Fiscal Sponsors (NNFS) and the Council on Foundations recommend conducting in-depth consultation with legal counsel when drawing up sponsorship agreements to avoid any penalties from regulators. This may be a solution for avoiding possible legal pitfalls, however, it often undermines the initial goal of lowering costs.

- For donors and organizations seeking sponsorship for international projects, there is an even more comprehensive level of due diligence required and it's wise to find a sponsor that is adept or has experience specifically sponsoring international projects. Sponsors of international projects should be following all international grantmaking regulations and abiding by the best practices for anti-money laundering procedures.

So how does the sponsorship model differ from other giving solutions? Under other models, foreign organizations looking to fundraise from multiple US donors have a few options to consider. They can apply to be vetted by a US 501(c)(3), such as a donor-advised fund (DAF) sponsor, to establish their eligibility for receiving donations from US donors. In this scenario the US donors would make a tax deductible donation to the intermediary organization (through their donor-advised fund) and would advise this organization to make a grant to the foreign recipient organization. DAFs are a popular vehicle for facilitating this process, however, as defined in the Pension Protection Act, donor-advised donations must not be restricted by the donor in support of one single beneficiary organization.

An alternative option for foreign charities looking for support from multiple donors is the "Friends Fund", which shares aspects of the pre-approved grant relationship described above. Friends Funds allow charities to solicit donations from multiple donors in support of a single international charity, in full compliance with IRS regulations.

To better show how this would work in practice, we'd like to share a recent real-life example. An individual contacted CAF America inquiring whether we offered fiscal sponsorship services. The potential donor had recently returned from a trip to Myanmar and wanted to support the work of a local organization. After discussing with the individual about the type of work the organization was engaged with, we understood that the group was conducting charitable activities and that they were looking to raise funds from US donors. The individual wished to financially support the organization and

help them establish a means of receipting tax-effective donations from other US donors. This potential donor believed that they needed a fiscal sponsor. After we explained what Friends Funds entail, which is very similar to Model C sponsorship, the donor realized that this would address the needs of the organization — they were not seeking bookkeeping, payroll, or human resources, nor project management — just an effective way to safely and securely raise funds from the US.

For many international charities and projects, often their goal is the same: to secure a tax-effective fundraising mechanism in the US without having to establish a “Friends of” Organization, which is a more costly solution and involves going through the process for registering a 501(c)(3) entity. Fiscal sponsorship is a smart and tax-effective means to achieve this, but the multifaceted definition of sponsorship could lead to many international charities and their supporters approaching sponsors that only offer Model A or B. This can be frustrating if the international charity is really seeking an arrangement similar to Model C. Fiscal sponsorship can be complicated, and until there is a more refined definition we recommend that you approach conversations leading with your needs and problems and allow the provider to explain the solutions they can offer.

For more information on Fiscal Sponsorship, find examples of community-based FS programs here, here, and here, and find out more information about the practice in general on the NNFS website.