

Fiscal Sponsorships: Managing Risk and Reward

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This week we speak with Colleen Lazanich, CEO of CalNonprofits Insurance Services, the only social enterprise insurance brokerage in California. She has more than 30 years of experience across the insurance industry, with more than 20 years specializing in nonprofits. Colleen has worked for carriers, wholesale brokers and retail brokers so she has seen the industry from all sides. When she isn't working, you can find her scuba diving in exotic locations. Colleen is also currently serving on the board of Walnut Avenue Family & Women's Center in Santa Cruz, CA.

NRMC: Colleen, in speaking this afternoon you mentioned an interest in charitable projects involving fiscal sponsorship. What is fiscal sponsorship? Can you begin with a brief definition?

CL: Fiscal sponsorship is an arrangement between an entity or group (called a project) that lacks their own tax-exempt status and a tax-exempt, 501(c)(3) nonprofit; the arrangement allows the project to solicit and accept tax-deductible donations and operate legally under the umbrella of the tax-exempt nonprofit. The project must fit within the overall mission of the tax-exempt nonprofit.

NRMC: What are the advantages to this arrangement?

CL: Obtaining a 501(c)(3) designation letter can be a long process and sometimes an idea needs to be "proven" in the real world; fiscal sponsorship is one way to test a project. Sometimes the project is of limited duration so incorporating and then filing to obtain tax-exempt status under Section 501(c) of the Internal Revenue Code simply isn't feasible, at least not in the short-term. Importantly, fiscal sponsorship of a project ensures funds are used in a manner that furthers the sponsor's own mission and is in compliance with their own standards. It can also be a revenue source to the tax-exempt nonprofit; fiscal sponsors generally charge an administrative fee to act in this capacity.

NRMC: What might these fees for services involve?

CL: Done well, a fiscal sponsorship acts as a proving ground for a new idea or a new nonprofit, while utilizing the administrative resources of the sponsor. There is a long list of possible services sponsors can offer projects: accounting/bookkeeping, tax filings, human resources, insurance, office space, grant writing, volunteer/donor networks; and, something that's less quantifiable, but nonetheless of tremendous value, the sponsor's reputation. Through fiscal sponsorship a project is able to get up to speed very quickly.

NRMC: Can you walk us through a typical path to fiscal sponsorship?

CL: There are a few different models of fiscal sponsorships, but the two most common types are:

- **Direct Model** - The Direct Model is where the project is not a separate legal entity and belongs to the 501(c) nonprofit sponsor. The sponsoring organization is responsible for ensuring the project fits within their mission. The sponsor is fiscally and legally responsible for the project. This is the most common arrangement.
- **Grant Model** - The Grant Model is where the project is a separate legal entity. Under the Grant Model the sponsor is only responsible fiscally for the project. The project and the sponsor enter into a grantee-

grantor relationship. The project writes a grant request to the sponsoring organization for funds that were donated to the 501(c)(3) tax-exempt sponsor nonprofit. Under the Grant Model, the board of directors for the sponsor organization should approve each grant, and the grants should be aligned with the mission of the sponsor nonprofit. The project maintains its own legal and tax filing responsibilities, but the sponsor is fiscally responsible for the project because they receive the tax-deductible donations and provide the grant to support the project. The sponsor must assure that the project fulfills all of the conditions of the grant agreement.

NRMC: What are some considerations for sponsoring organizations?

CL: First and foremost, does the project you are considering have a similar or compatible mission? Missions must be aligned, or the sponsor risks jeopardizing their tax-exempt status. Next, does the project already have a legal entity, infrastructure, resources, and insurance? Also, consideration must be given to the infrastructure and resources the project will require from the sponsor. Finally, since the funds will be raised in the sponsor's name, the question must be asked, is there the possibility of any reputational risk to the sponsor?

On the project side, additional considerations include:

- What resources and infrastructure will the sponsor provide?
- Can the sponsor provide the support this project needs?
- What reporting will the sponsor require?
- How much is the sponsor charging for administration fees?

NRMC: Two of the questions risk leaders are likely to ask include: 1. What happens when the project ends? and 2. What happens if a project wants to separate itself from the fiscal sponsorship arrangement?

CL: The agreement should be clear on what happens—under both scenarios—to the money, the personnel, and the intellectual property, especially with a “direct” sponsorship relationship. Any agreement should provide for a process for disengagement that avoids arbitrary or disruptive actions.

NRMC: How does Fiscal Sponsorship impact insurance?

CL: Under the Direct Model of fiscal sponsorship, the sponsor is responsible for the project in every way. The sponsoring nonprofit must include the project as though it is a program of the sponsor, as it is liable for everything that the project does. The nonprofit must include all revenue and expenses on their financials. Project personnel are employees and volunteers of the sponsor and must be subject to the same policies and procedures used in the organization.

NRMC: Can you break out the insurance considerations for us, based on the two fiscal sponsorship models you mention above?

Insurance Considerations Using a Direct Model

- **General Liability** - All operations of the project must be included in the application for coverage. The carrier may require a copy of the sponsorship agreement. Some carriers will exclude fiscal sponsorships from coverage unless they are disclosed on the application. It is a good idea to disclose them at renewal even if operations were previously reported.
- **Directors' and Officers' Liability (D&O)** - The sponsor's board should approve all fiscal sponsorships to ensure they fit within the mission of the organization. The board should ensure that projects adhere to the same policies and procedures as the sponsoring organization.
- **Employment Practices Liability** - The sponsoring organization could face claims alleging wrongful termination, discrimination, harassment, or wage and hour violations related to the project.
- **Workers' Compensation** - Any employees must be included in the reported payrolls and classifications.
- **Volunteer Accident** - Include the project volunteers on the policy.

Insurance Considerations Using a Grant Model

- Insurance considerations with the Grant Model essentially require the project to obtain all of the insurances that the sponsor maintains in the Direct Model. If the project can name the sponsor as an Additional Insured, particularly under the general liability policy, that would be a benefit to the sponsor.
- **General Liability** - The project should indemnify the sponsor and seek Additional Insured status for the sponsor on the project's policy. The sponsor should also disclose the project and agreement with their

insurance carrier.

NRMC: Can you give us a few of your best practices concerning fiscal sponsorship?

CL: This may seem obvious, but it's essential to have fiscal sponsor agreements in writing, explicitly outlining the responsibilities of each party. I can't stress enough that the sponsor's board of directors should review and approve each project and fiscal sponsorship. The sponsor has a fiduciary duty to direct and control the money, as donations are in their name. All other risk management practices apply that will ensure appropriate methods of oversight are followed.

For readers who would like more detailed information on the Direct and Grant Models, or the advantages and disadvantages of Fiscal Sponsorship, Colleen recommends the following resources:

- Fiscal Sponsorship resources from the National Council of Nonprofits: councilofnonprofits.org/tools-resources/fiscal-sponsorship-nonprofits
- Tips for Nonprofits Considering Fiscal Sponsorship from Erin Bradrick, Senior Counsel at NEO Law Group: www.youtube.com/watch?v=iAJ06g_v90Y