



# At Last – A Way to Evaluate Fiscal Sponsors



Is fiscal sponsorship right for you? This checklist will help you decide.

By Gerald R. Solomon

**F**iscal sponsorship has become quite common in the nonprofit world. Yet fiscal sponsorship is alarmingly misunderstood. Many nonprofits agree to become fiscal sponsors and lend their 501(c)(3) status to others without realizing the legal risk of doing so. Many don't fully understand what fiscal sponsorship entails. And few think carefully enough about what such a partnership means and what the consequences could be.

Till now, there hasn't been a set of criteria that a nonprofit can check before agreeing to become a fiscal sponsor or that others can use if they want to hire one. This article fills that gap by providing a set of desperately needed metrics. You can use this list of benchmarks to evaluate a fiscal-sponsorship arrangement and answer that

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all-important question: Is this partnership right for my organization?

### What Is Fiscal Sponsorship?

Fiscal sponsorship is a relationship among three entities: **(1) a funder** (individual, foundation, or government); **(2) a service provider** (the group that performs the services for which the funds are given); and **(3) a fiscal sponsor** (a nonprofit) charged with responsibility to manage the funds and the delivery of services.

The fiscal sponsor must be a

nonprofit that agrees to let another group use its 501(c)(3) tax-exempt status. Those seeking fiscal sponsorships are usually groups that have ideas for a project but lack the 501(c)(3) designation necessary to obtain a grant. Often these are short-term or pilot projects. Sometimes the group looking for a fiscal sponsor hopes to become a nonprofit organization but needs time to develop the necessary infrastructure. Or it may be a group that has applied for tax-exempt status, is awaiting IRS approval, and needs a sponsor in order to receive grant money in the meantime.

The fiscal sponsor receives the funds, writes checks for program expenses, includes the grant in its annual tax return, and is liable for all deliverables for the project. In

addition, the fiscal sponsor may provide personnel, payroll, training, publicity, and other management services.

The fiscal sponsor also assumes 100% of the risk and liability in the partnership. That's why, if a group approaches you and asks you to become their fiscal sponsor, it's important not to agree too quickly. First, be sure your organization has the capacity needed to support such a partnership.

Here are standards you can use to decide if a fiscal sponsorship is right for you. If you're a group looking for a fiscal sponsor, you can apply these benchmarks to assure that the nonprofit you choose will make a good partner for you. If you're a nonprofit organization thinking of becoming a fiscal sponsor, you should first be sure you comply with all these standards. Otherwise, you may be putting your organization at risk.

### Mission-Related Benchmarks

If a group asks your organization to become a fiscal sponsor for them, or if you're choosing a nonprofit to be your fiscal sponsor, the first questions you need to ask are these: Does it feel right? Will we work well together? Does the potential partner understand our project and mission? Without that common foundation of values, purpose, and internal cultures, the relationship begins with a lack of stability.

In its broadest sense, it's about how well both groups' cultural competency<sup>1</sup> and mission are aligned (see *Standard 1* in "Standards to Evaluate a Fiscal Sponsorship," page 12). Engaging in a mission dialogue will help you identify strengths and challenges so that you can put appropriate safeguards in place.

If you're the one being asked to take on the fiscal-sponsor role, make certain that the project proposed by your potential partner furthers your own mission. If it doesn't, you could risk losing your tax-exempt status.

If both groups decide to go ahead with the fiscal sponsorship, the next step is to have an attorney prepare a contract setting forth the

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roles each party will play (*Standard 2*). This agreement should address such fundamental issues as:

- the fees the fiscal sponsor will charge for its services
- how the fiscal sponsor will deal with risk and what insurance coverage it possesses
  - the financial and human-resource policies that will be used
  - how communication systems will be managed
  - how conflicts will be resolved
  - the responsibilities of each of the parties
  - termination provisions, including who can terminate, when, and the ramifications of doing so.

### Fiscal Standards

Financial principles of accountability, transparency, and integrity are the cornerstones of a fiscal sponsorship. It's crucial for the fiscal sponsor to comply with applicable regulations (*Standard 3*), such as:

- Generally Accepted Accounting Standards (GAAP) (guidelines for financial accounting and reporting)
- Federal Acquisition Regulations (FAR) (rules on competing for contracts)
- Circular A-133 (audit requirements for nonprofits)
- the Sarbanes-Oxley Act (standards to deter fraud and increase accountability)<sup>2</sup>

The openness with which the fiscal sponsor operates (*Standard 4*) will reveal whether the organization is following all necessary regulations.

To evaluate a fiscal sponsor's compliance with financial standards (*Standard 5*), ask the following questions:

- Are the fiscal sponsor's financial records accessible on demand?
- What written policies provide checks and balances to safeguard

funds?

- What role does the fiscal sponsor's board play in overseeing finances?

- What system does the fiscal sponsor use to monitor program expenditures and activities?

Next, it's important to assure that the fiscal sponsor has the financial stability and resources to provide a continuum of services without interruption (*Standard 6*).

- Does the fiscal sponsor have a good relationship with its bank, including a credit line to cover unforeseen costs?

- Does the fiscal sponsor arrange for an annual audit of its finances (*Standard 7*), overseen by an independent audit committee?<sup>3</sup>

- Does the fiscal sponsor post its 990 and the results of its annual audit on its Web site?

- What are the qualifications of the fiscal sponsor's staff (*Standard 8*)?

At least once a year, an attorney should review and approve the employee handbook.

### Human-Resource (HR) Capacity Standards

Fiscal sponsors sometimes provide their partner groups with human-resource services, such as personnel management, payroll processing, and benefits management. In today's litigious environment, it's essential for the fiscal sponsor to manage people and the associated risks effectively. If you're considering becoming a fiscal sponsor, remember that you can be exposed to liability for the actions of the projects you sponsor for your partner. Ask these questions to be sure risks are well controlled:

- Does the fiscal sponsor have a written risk-management program (*Standard 9*)?

- What measures are used to mitigate risk and educate people about possible risks?

- Does the fiscal sponsor have sufficient insurance policies in the

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# Standards to Evaluate a Fiscal Sponsorship

## MISSION

**Standard 1. Alignment.** The mission and cultural competency of the fiscal sponsor and its partner group should be in alignment.

**Standard 2. Engagement Agreement.** The fiscal sponsor must provide its partner group with a written agreement for its services. This contract should clearly set forth the terms and conditions of the relationship, including (but not limited to) provisions covering fees, costs, risk of loss, financial and personnel management policies, respective duties, and conflict-resolution procedures.

## FINANCIAL CAPACITY & INTEGRITY

**Standard 3. Compliance.** The fiscal sponsor must comply with all government and philanthropic requirements, including nonprofit governance regulations, Sarbanes Oxley, GAAP, and Circular A-133.

**Standard 4. Financial Accountability.** The fiscal sponsor must provide its financial services in an open, accountable manner with the highest level of integrity.

**Standard 5. Secure Financial Systems.** The fiscal sponsor needs to use an accounting system that insures the highest level of checks and balances, as well as board oversight.

**Standard 6. Financial Stability.** The fiscal sponsor must maintain sufficient resources and credit capacity to provide continual and uninterrupted financial service.

**Standard 7. Annual Audit.** The fiscal sponsor should have an audit committee. This committee should arrange for an outside firm to conduct an annual audit, with results open to public view.

**Standard 8. Financial Staffing.** The fiscal sponsor's financial staff should consist of highly trained professionals with certifications or experience indicating the highest level of financial knowledge and ability. For example, the Chief Financial Officer (CFO) should hold a CPA degree or have at least 10 years of high-level CFO experience. Department or division supervisors should possess certifications or degrees in their respective disciplines.

## HUMAN RESOURCE CAPACITY

**Standard 9. Risk Management.** The fiscal sponsor should maintain a comprehensive risk-management program. This program should be overseen by a certified risk-management professional responsible for securing, managing, and implementing the widest variety of insur-

ance coverage. Coverage should include: general-liability insurance, directors' & officers' liability insurance, employment-practices' liability insurance, workers'-compensation insurance, fiduciary insurance, crime insurance, and property & casualty policies with a minimum policy limit of \$1,000,000 per occurrence.

**Standard 10. Whistle-Blower Program.** The fiscal sponsor should have an independently operated whistle-blower program that encourages people to report fraudulent activity, violations of government regulations, and unsafe work practices. This program should ensure that anyone who makes such a report will be protected from retaliation.

**Standard 11. Human Resource (HR) Policies.** The fiscal sponsor needs to maintain an employee handbook (a written set of employment policies and procedures) and thoroughly explain these policies to all employees. Staff members should sign statements declaring that they understand and agree to follow these policies and procedures. At least once a year, an attorney should review and approve the employee handbook. The attorney should note as an addendum to the handbook that the organization complies with all local, regional, state, and federal regulations.

**Standard 12. Human Resource (HR) Staffing.** The fiscal sponsor's HR staff should consist of highly trained professionals with certifications or experience demonstrating the highest level of knowledge.

**Standard 13. Legal Counsel.** The fiscal sponsor must have (in house or under contract) competent legal counsel to provide legal review, support, and assistance as needed.

## BOARD GOVERNANCE

**Standard 14. Board Responsibilities.** The fiscal sponsor's board of directors needs to provide appropriate oversight. Board members must avoid conflicts of interest and adhere to a formal, written code of conduct.

## GRANTS MANAGEMENT

**Standard 15. Infrastructure System.** The fiscal sponsor must use a secure database system to manage its relationships with funders and customers.

## TECHNOLOGY INFRASTRUCTURE

**Standard 16. Security and Compliance.** The fiscal sponsor needs to provide its services in a technologically secure environment. This environment should be overseen by a director who holds the requisite technology certifications and whose department maintains current software and hardware licenses.

areas of general liability, directors' & officers' (D & O) liability, employment practices, and workers' compensation?<sup>4</sup>

- Does the fiscal sponsor have a whistle-blower program? Are measures in place to ensure that people who report problems are free from

retaliation (*Standard 10*)?

- If the fiscal sponsor uses volunteers, is there sufficient insurance to cover them?<sup>5</sup>

- Does the fiscal sponsor have legally approved personnel policies (*Standards 11 and 13*)? Do its human-resource employees have

the proper credentials and experience (*Standard 12*)?

## Board Governance Standards

The fiscal sponsor must have a highly functioning board. Board members must be active and  
*continued on page 14*

## Are You Ready to Be a Fiscal Sponsor?

Before becoming a fiscal sponsor, make sure you're complying with the 16 standards discussed in this article. Here are *Nonprofit World* articles (available at [www.snpo.org](http://www.snpo.org)) to help you do so:

- **The Most Likely Lawsuits — and How to Protect Yourself** (Vol. 19, No. 1)
- **Finding the Right Bank** (Vol. 11, No. 4)
- **What Is the Board's Role in Managing Risk?** (Vol. 15, No. 5)
- **How to Avoid Retaliation Claims** (Vol. 21, No. 6)
- **Conflict of Interest in the Board Room** (Vol. 17, No. 2).
- **Setting Up a Control System for Your Organization** (Vol. 16, No. 3)
- **How to Prepare Board Members to Govern Effectively** (Vol. 25, No. 6)
- **Analyze Your Finances to Ensure Your Mission** (Vol. 19, No. 5)
- **Your Duty to Investigate Workplace Complaints** (Vol. 19, No. 3)
- **Six Ways to Reduce Risk & Comply with the Law** (Vol. 25, No. 6)
- **How to Write Excellent HR Policies** (Vol. 24, No. 5)

knowledgeable in overseeing the organization's activities (*Standard 14*). The fiscal sponsor should provide extensive training and development opportunities for its board members.

### Infrastructure Standards

The fiscal sponsor needs to have a secure system to track and manage grant funds (*Standards 15 & 16*). ■

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You could risk losing your  
tax-exempt status.

### Footnotes

<sup>1</sup>Cultural competency is the ability to accept people with different beliefs, work effectively with them, and communicate adeptly across cultures. See "Cultural Competence: What Does It Mean for You?," *Nonprofit World*, Vol. 26, No. 5, [www.snpo.org](http://www.snpo.org).

<sup>2</sup>More information on Generally Accepted Accounting Standards (GAAP) is available from the FASB (Financial Accounting Standards Board, [www.fasb.org](http://www.fasb.org)), the FASAB (Federal Accounting Standards Advisory Board, <http://www.fasab.gov/accepted.html>), and the AICPA (American Institute of Certified Public Accountants, [www.aicpa.org](http://www.aicpa.org)). More on Federal Acquisition Regulations (FAR) is available at [www.arnet.gov/far](http://www.arnet.gov/far). For information on Circular A-133, issued by the Office of Management and Budget, see [www.whitehouse.gov/omb/circulars](http://www.whitehouse.gov/omb/circulars). For more on Sarbanes-Oxley, see "The Sarbanes-Oxley Act & Nonprofits: But I Thought That Didn't Apply to Us," *Nonprofit World*, Vol. 22, No. 5, [www.snpo.org](http://www.snpo.org).

<sup>3</sup>See *Nonprofit World* articles on audit requirements at [www.snpo.org](http://www.snpo.org), including: "How to Have an Audit without Breaking the Bank" (Vol. 20, No. 4), "Nonprofits without Audit Committees Risk Disaster" (Vol. 22, No. 2), and "How to Find the Perfect Auditor" (Vol. 22, No. 3).

<sup>4</sup>Many *Nonprofit World* articles on insurance for nonprofits are available at [www.snpo.org](http://www.snpo.org), including: "Does Your Board Need Liability Insurance?" (Vol. 12, No. 6) and "Get the Best Protection for Your Insurance Dollar" (Vol. 24, No. 4).

<sup>5</sup>See these *Nonprofit World* resources at [www.snpo.org](http://www.snpo.org): "What Are We Doing to Protect Our Volunteers from Lawsuits?" (Vol. 9, No. 4), "Volunteer Protection Act: What Does It Mean for You?" (Vol. 16, No. 2), "Don't Let Volunteers Put Your Organization at Risk" (Vol. 10, No. 1), and "Volunteers: Resource or Risk?" (Vol. 15, No. 5).

Articles in this department are written by the staff and members of the Alliance for Nonprofit Management ([www.allianceonline.org](http://www.allianceonline.org)).

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