Fiscal Sponsorship after 25 Years
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I. The Models.

A. Model A (“Comprehensive” or “Direct”). Along with Model C, Model A is the most common form of fiscal sponsorship. In Model A, the sponsor agrees to directly undertake the project with its own employees and volunteers. The project is not a separate legal entity, and so the sponsor is liable for project activity. The sponsor receives donations, issues receipts, and spends funds for the project’s purposes.

B. Model B (Independent Contractor). In Model B, the sponsor pays an individual or entity to conduct the work of the project as a service provider to the sponsor. The sponsor receives donations and issues receipts, and pays the project service provider for the work performed at or below fair market value. The sponsor and service provider might both be liable to third-parties, but can allocate risk and responsibility by contract.

C. Model C (“Re-grant” or “Indirect”). Along with Model A, Model C is the most common form of fiscal sponsorship. In Model C, the sponsor receives donations and grants, and in furtherance of the sponsor’s purposes, re-grants them to the project (which can be an individual or entity), exercising discretion and control. The project receives grants from the sponsor and reports to the sponsor on their use.

D. Model D (Group Exemption). In Model D, the sponsor receives a group exemption from the IRS and, stepping into the shoes of the IRS, confers tax-exempt status on subordinate organizations over whom it exercises supervision or control. The project can receive grants and contributions directly.

E. Model L (Single-Member LLC). In Model L, the project is a single-member LLC of which the sponsor owns 100%. As such, the project is disregarded for most federal tax purposes, and takes on the tax-exempt status of the sponsor. Because the LLC is regarded for all other purposes, however, the sponsor is generally protected from liabilities of the project.

F. Model F (Technical Support). In Model F, the sponsor assists the project with administrative and technical issues of the parties’ choosing, for example, bookkeeping, accounting, and donation-receipting. In a classic Model F, the sponsor does this at substantially below cost and so the sponsor must subsidize its work by grant or other means, and fees from the project do not generate UBIT. Sponsors that provide technical assistance above this threshold may generate UBIT.

G. Blends. In practice, many or most projects fall outside the neat categories above and instead mix aspects of two or more models. For example, a project that begins as a pure Model A - conducted entirely by the sponsor’s employees or volunteers - may quickly need to
hire independent contractors (Model B) for particular aspects of the project, and may find that making grants (Model C) furthers project purposes.

II. Interesting Issues.

A. IRS Recognition of Fiscal Sponsorship. Fiscal sponsorship is not legally defined, but in the last few decades, IRS has acknowledged it in various contexts and even revoked the exemption of organizations where it has been done improperly.

1. 1994 CPE Text, Topic K (Community Foundations). In the FY 1994 CPE Text, IRS attorneys George Johnson and David Jones found “nothing inherently wrong with fiscal sponsorship. … However, it can and has been misused.” They then illustrate examples of legitimate fiscal sponsorship arrangements (consistent with models described in the book), and improperly earmarked or conduit arrangements.

2. IR-2005-93, Sept. 6, 2005. In the wake of Hurricane Katrina in 2005, the IRS acknowledged that it would expedite applications of organizations seeking to provide relief, but encouraged the use of existing charities “because such organizations, including churches, are frequently able to administer relief programs more efficiently than newly formed organizations, because they already have fund-raising and distribution infrastructures in place.” See [https://www.irs.gov/newsroom/irs-expedites-charity-applications-urges-use-of-existing-charities](https://www.irs.gov/newsroom/irs-expedites-charity-applications-urges-use-of-existing-charities) or [https://tinyurl.com/y3e9fapd](https://tinyurl.com/y3e9fapd).

3. June 6, 2012 ACT Recommendation to IRS. In June 2012, the Advisory Committee on Tax Exempt and Government Entities (ACT) recommended that the IRS, Treasury, and the Chief Counsel’s office coordinate to issue “precedential guidance about the use of tax-compliant alternatives to the creation of new Section 501(c)(3) organizations, such as fiscal sponsorships. . . .” The ACT expressed concern that organizations seek recognition of exemption under Section 501(c)(3) “without exploring possible alternatives that might be more appropriate in light of their goals and objectives.” Examples included “a specific short-term project--such as providing assistance following a local disaster, or construction of a new playground or dog park.” The ACT acknowledged that fiscal sponsorship has “become a significant part of the Section 501(c)(3) landscape.”

4. Private letter rulings. Fiscal sponsorship has also cropped up in private letter rulings issued by the IRS.

   a. PLR 201740022 (10/6/17). In this letter ruling, the IRS revoked the Section 501(c)(3) status of the organization. Among other problems, the organization, a purported fiscal sponsor apparently under Model C, could not confirm the end use of the funds, and so could not verify its discretion and control. (The IRS wrote twice that the organization acted as a “conduit”.) The organization requested semi-annual reports from its projects, but could not produce any reports to the IRS. When funds were diverted for non-exempt purposes, the organization failed to try to recover the funds. The IRS also noted that many of the projects would not be approved for their own tax-exempt status under Section 501(c)(3).
b. **PLR 201712014 (3/24/17).** The IRS revoked the organization’s tax-exempt status under Section 501(c)(3). Of the charity’s fiscally sponsored projects, the IRS stated, “Many of these programs/projects would not qualify to be tax-exempt on their own merits; some programs/projects benefitted specific individuals or a small group of individuals; at least one program/project . . . had the potential to be supporting an illegal activity. . . . [The fiscal sponsor] acted more as a conduit than as a fiscal sponsor. [The organization] . . . would fail to retain control and discretion over use of the funds and maintain records establishing that the funds were used for Section 501(c)(3) purposes.”

c. **PLR 201408030 (2/21/14).** The IRS rejected an application for Section 501(c)(3) status where the organization planned to carry out social justice activities such as research and training. It had a tandem relationship with an affiliated 501(c)(4), and also planned to serve as fiscal sponsor for various projects of the 501(c)(4). The IRS rejected its application for exemption in part because “You solicit grants for specific projects that further the purposes of [related Section 501(c)(4) organization] that are not within the scope of exempt activities under section 501(c)(3).”

d. **PLR 201609006 (2/26/16).** The IRS revoked the exempt status of a would-be church for numerous problems, of which just one appeared to be improperly conducted fiscal sponsorship, described in one instance by the organization as being a “forwarding agent.” The IRS observed that the organization had no written agreement of any sponsorship (which the organization acknowledged was a “big mistake”) and the organization had no evidence that the funds were used for any exempt purpose.

B. **Cases Involving Fiscal Sponsors and Projects.**

1. **Earth Island Institute v. U.S. Forest Service, 2006 WL 3359192 (E.D. Cal. 2006).** Earth Island Institute sponsored a Model A project called the John Muir Project. In furtherance of the purposes of its project, Earth Island Institute sued a national forest logging operation under the National Environmental Policy Act, obtained a preliminary injunction, and posted a bond of $1,000 in case the injunction was found to be wrongful. Sierra Pacific Industries, a defendant, intervened and asked that the bond be increased to $200,000.

   Sierra Pacific argued that Earth Island Institute’s tax returns showed assets of almost $6 million and that Earth Island Institute could afford a sizeable bond. The court disagreed, noting that funding responsibility to pursue the lawsuit rested with “a discrete project within the organizational umbrella” of Earth Island Institute, and that only $56,000 was earmarked for forest litigation in 2006, and every dollar was needed for payroll and costs of current cases. Earth Island Institute explained that it served as fiscal sponsor of forty different projects and that diverting restricted funds from one program to another would “violate donor intent” and “put the entire organization at risk.” The court agreed, ruling that “no additional bond should be required.”

supervision, and other grounds. The U.S. Forest Service was the funding source, awarding more
than $250,000 to the sponsor in support of an internship project “to help build the next
generation of environmental leaders, stewards, and volunteers from underrepresented and
minority communities.” The project and sponsor had signed a written temporary fiscal
sponsorship agreement with a 2% administrative fee. The complaint charged that the sponsor
did not pay project bills on time, failed to provide fiduciary oversight and financial management,
and would not transfer the project to MobilizeGreen’s new fiscal sponsor. The court held that it
lacked jurisdiction over the lawsuit and remanded it to the Superior Court for the District of
Columbia. The judge noted, however, that even if MobilizeGreen did not “own” the funds
awarded by the Forest Service, a fiscal sponsorship agreement could create a fiduciary
relationship “of good faith, demanding trust and confidence.”

3.  

**Boat People S.O.S., Inc. v. Urban Affairs Coalition, 2018 WL 558432**
(E.D. Pa. 2018). Urban Affairs Coalition (“UAC”) sponsored a Model A project called
VietLEAD, whose apparent purpose was to offer youth development services to the Vietnamese
community in the Delaware Valley. UAC entered into a fiscal sponsorship agreement with an
unincorporated association formed by VietLEAD, placing it “under the legal control and
authority of UAC,” delegating responsibility for day-to-day operations to VietLEAD’s advisory
committee and director, and paying its personnel as at-will employees of UAC. Some of the
project leaders had worked in the Delaware Valley offices of Boat People S.O.S. but switched to
pursuing similar activities as VietLEAD under UAC’s sponsorship. Boat People S.O.S. sued
UAC and the individuals, alleging civil conspiracy and other unlawful acts to divert the
operations and assets of Boat People S.O.S. in New Jersey and Pennsylvania to VietLEAD. The
court dismissed the complaint against UAC, saying that the allegations were insufficient to infer
that UAC participated in any “plot” against BPSOS. Rather, it was equally plausible that UAC
acted “for the legitimate business purpose of providing fiscal sponsorship of a new partner
organization.”

4.  **Others.** Several other cases in the last few years mention fiscal
sponsorship, but the characteristics of fiscal sponsorship are not critical to the issues in dispute.

C.  **Model L.**

1.  **Summary.** See I.E above.

2.  **Basis.** Model L is based on the following two pieces of guidance:

   a.  **Information Letter 2010-0052.** Confirms that a private foundation
   making a grant directly to a single-member LLC whose sole owner is a Section 501(c)(3) public
   charity, and that has not elected corporate tax treatment, may generally count the grant as a
   qualifying distribution and not treat it as a taxable expenditure. Available at

   b.  **Notice 2012-52.** Confirms that donor gifts to a single-member
   LLC that has not elected corporate tax treatment and whose sole owner is a domestic U.S. charity
described in Section 170(c)(2) may be treated as a deductible gift under Section 170. Available at https://www.irs.gov/pub/irs-drop/n-12-52.pdf.

3. **Mechanics.** The LLC is formed under state law with the sponsor as its sole member. As with any other formation, choice of state should be carefully considered; some states can be more logistically challenging than others. Because the LLC is disregarded under federal tax law for most purposes and takes on the tax status of the sponsor, the project LLC may receive deductible gifts and private foundation grants without expenditure responsibility (assuming the sponsor is a Section 501(c)(3) public charity). Also because of its disregarded nature, the project LLC’s activities will be attributed to the sponsor for federal tax purposes, including any lobbying, electioneering, unrelated business income, or non-charitable activity. As such, the sponsor must monitor the LLC’s activities.

4. **Liability.** Because the project LLC is a separate entity for all other purposes, the sponsor should not be liable for project activities, provided that corporate formalities are respected and there are no other reasons for piercing the corporate veil. The reverse is not necessarily true; however, because the project LLC is an asset of the sponsor, there is some risk that project assets in the LLC could be used to satisfy liabilities of the sponsor. Charitable trust restrictions under state law may help, making use of project assets to satisfy liabilities of the sponsor more difficult.

5. **More information.** For detailed discussions of Model L, see:


D. **Fiscal Sponsorship Funds and DAFs**

   1. **When are fiscal sponsors DAFs?** Unless it meets an exception, any fund, including one labeled a “fiscal sponsorship fund,” that meets all three elements of Section 4966(d)(2)(A) is a donor advised fund. The elements are that the fund or account:

      a. is separately identified by reference to contributions of a donor or donors,

      b. which is owned and controlled by a sponsoring organization, and

      c. with respect to which a donor (or any person appointed or designated by such donor) has, or reasonably expects to have, advisory privileges with respect to the distribution or investment of amounts held in such fund or account by reason of the donor’s status as a donor.
In practice, the fiscal sponsorship funds most likely to fall into the DAF definition are those funded principally by a donor who then serves as the project’s director. To avoid the reporting and other consequences of being a donor advised fund (such as being subject to Sections 4967 and 4958(c)(2)), the sponsor and project may wish to avoid this classification if possible.

2. Ways to avoid DAF classification.

a. Multiple donor fund. The legislative history in the Joint Committee Report\(^1\) of the Pension Protection Act indicated that a fund “that pools contributions of multiple donors” generally will not meet the first prong of the DAF test so long as there is no tracking of a separate donor balance for each specific donor or group of related donors.

b. Single-entity beneficiary fund. Section 4966(d)(2)(B)(i) provides an exception for any fund that “makes distributions only to a single identified organization.” So, even if a fiscal sponsorship fund meets all three prongs of the DAF definition, it might escape DAF classification if only one entity will receive grants from the fund. This may exempt many or nearly all Model C pre-approved grant relationships from the DAF definition. However, regulations may eventually require the single entity beneficiary to be domestic, to be a Section 501(c)(3) public charity, or impose other limits.

c. Minority of project committee. In some circumstances, a donor who constitutes a minority of a project advisory committee might fit into an exception. See, for example, IRC 4966(d)(2)(C).

E. California legislation after collapse of fiscal sponsors. In 2012, the International Humanities Center, a large fiscal sponsor based in Pacific Palisades, California, became financially insolvent, taking with it the funds in many of its restricted funds.\(^2\) As a result, California enacted Government Code 12599.8, which states:

12599.8. For any year that the balance sheet of a charitable organization shows that it holds restricted net assets, while reporting negative unrestricted net assets, the organization shall provide an explanation of its compliance with its charitable trust responsibilities and proof of directors’ and officers’ liability insurance coverage to the Attorney General’s Registry of Charitable Trusts.

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\(^1\) Staff of the Joint Committee on Taxation, Technical Explanation of H.R. 4, The “Pension Protection Act of 2006,” as passed by the House on July 28, 2006, and as considered by the Senate on August 3, 2006.

In other words, if the year-end balance sheet shows positive restricted assets, but unrestricted assets are negative, it may mean that the organization (sponsor) did not have sufficient assets at that time to cover the balances in its restricted (project) funds. (Due to accounting rules, it could instead reflect, for example, large investment losses in an endowment.)

III. Resources.

A. www.fiscalsponsors.org (National Network of Fiscal Sponsors website)

B. www.fiscalsponsordirectory.org