Ready to spin out?
A Framework for Assessing Readiness

The Impact Commons Toolkit

SOCIAL IMPACT COMMONS

Reframing

>> Spin out isn't an isolated event, it's part of a *relationship* process.

The conversation and expectations around spin out start at the *beginning* of the project relationship and unfold *throughout* the relationship. Regular check-ins are necessary.

**>> In relationship management, mutual feedback is key.**

Regular *mutual* reporting and annual check-ins on all six dimensions of our framework can help ensure strong and intentional relationships, as well as strategic (not reactive) spin out.

Project Lifecycle
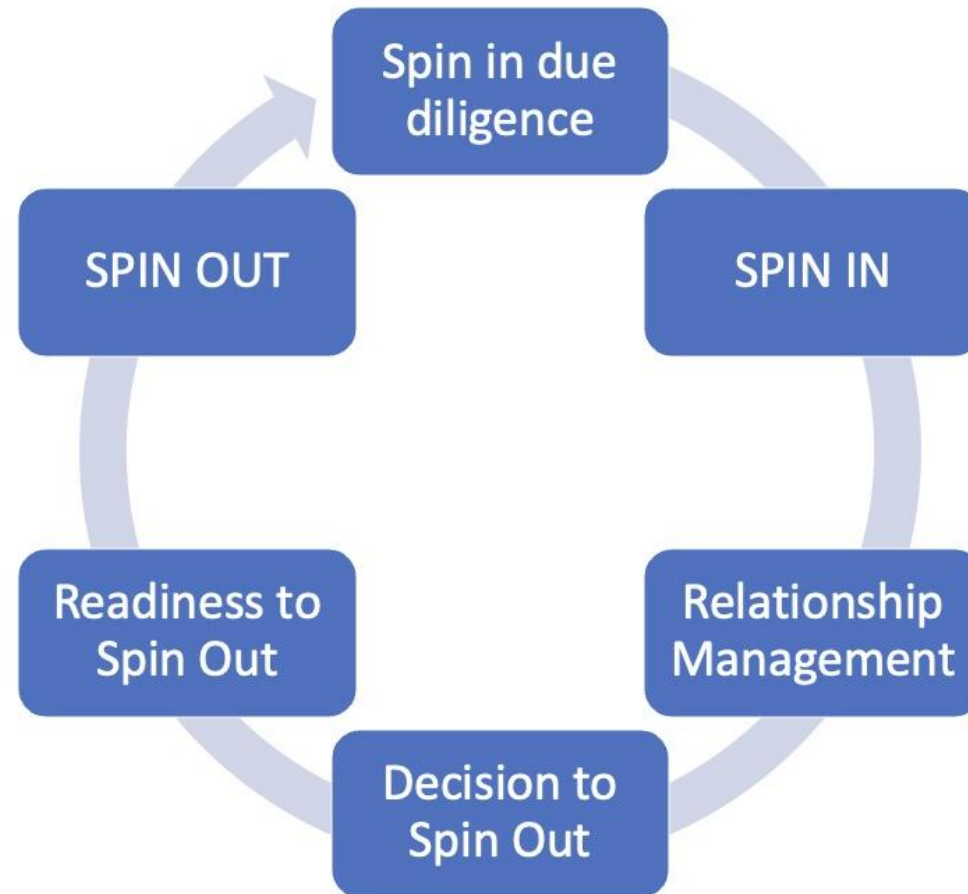
Spin Out to Stand-alone Status

Most projects (49%) transitioned away from fiscal sponsorship to stand-alone nonprofit 501(c)(3) status, followed by 28%, which transitioned to another fiscal sponsor. Under "other" reasons for departure sponsors cited that projects "completed their mission", "were short-term projects", or "dissolved due to shortage of funds or inactivity".
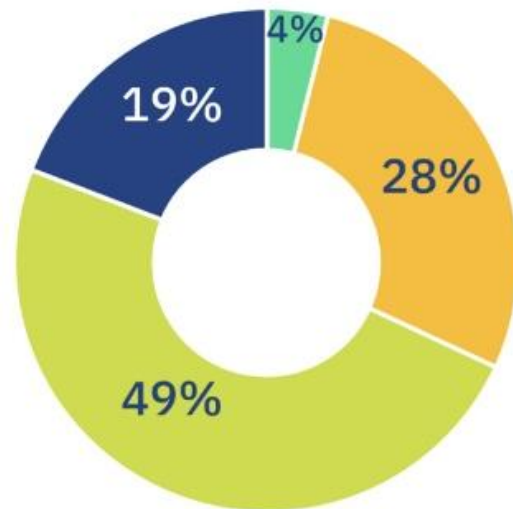
(e) Reasons for projects transitioning out of fiscal sponsors   n=83

Legend:
- To be an independent 501(c)(3) organization
- To go to another fiscal sponsor
- Other (please specify)
- Don't know

Considerations

Once a project has decided to spin out, regardless of the destination, the sponsor has a fiduciary responsibility to assess readiness with respect to:

- **Compliance -** Is there a legal 501(c)(3) in good standing ready to receive the project?

- **Operating Capacity -** Does the new home have appropriate operating capacities?

Basic compliance is relatively straight forward:

- ❏ Articles of Incorporation (formation)
- ❏ IRS Tax Exemption Letter
- ❏ Latest IRS Form 990 and State Regulatory Filings (if applicable)

Operating Capacity, however, is more complicated…

Challenges

Assessing whether the project is ready to spin out to stand-alone operations mostly concerns *replacing* the operating and governance capacities provided by the sponsor.

This involves a kind of comparative analysis (sponsor vs. new home) examining the direct and indirect supports and related costs the sponsor was providing (distinct from those of the project) that would need to be *replaced* under the new home, however...

- Level of readiness assessment will vary with size and complexity of the project.
- Supports may not be *directly* (1:1) replaceable.
- Costs, quantity, and quality of supports will vary from sponsor to sponsor.
- Costs for vendors, services, and employees will vary from market to market.
- Deficits in capacities may be "hidden" from both sponsors and projects.
- Virtual operations can impact cost comparisons significantly.

Assessment

Assessing *replacement capacity* helps answer...

>> **FOR THE PROJECT** - Are we ready to finalize the decision to spin out? If not, what are the key milestones we need to achieve to be ready?

>> **FOR THE SPONSOR** - When have we satisfied our fiduciary duty to ensure the project is moving to an adequate home?

There is no bright-line standard for answering these questions for either party.

Framework

>> Direct or "Hard" Support and Systems Value*:

- Staff salaries/vendor costs (i.e., for project management, finance, HR, compliance)
- Benefits (i.e., employee benefits and their administration)
- Insurances (i.e., general liability, D&O, others)
- Compliance (i.e., financial statements, tax, and charitable filings)
- Software and financial systems (i.e., financial systems, bank account set up, integrations, and others)
- Policies, processes, practices (i.e., finance, HR, risk management)
- Other (i.e., workspace, special technologies/equipment, new nonprofit formation/exemption)
- Transfer costs (i.e., there are costs associated with transitioning finances and systems)

>> Indirect or "Soft" Support Value:

- Governing board (i.e., quality and experience of directors)
- Network and reputation value (i.e., knowledge exchange, mentorship, collaboration, reputation)
- Economy of scale (i.e, the financial benefits of economies of scale operating under the sponsor)
- Subject matter expertise (i.e., sponsor staff and leadership knowledge)

(*) Depending on whether the project is spinning to a newly formed or established entity, some direct supports may not be accompanied by incremental or "new" hard costs, i.e., such as the cost to form and seek exemption for a new charitable organization.

Method

>> Direct or "Hard" Support and Systems Value:

- Compare costs in general as percent of revenue/expense: current sponsor vs. future home.
- Use average or median salary per job title *for the region(s) (if virtual) where the future home operates*.
- Assess employee benefit costs based on new plan/group structure.
- Benchmark other vendors and direct systems costs likewise per new operating location(s).
- Include checklist of key policies and itemize estimated costs to replace, where needed.
- If forming a new nonprofit, include legal and filing costs for formation, tax exemption.

>> Indirect or "Soft" Support Value:

- Assess these areas based on a qualitative rubric of comparative *quality* and/or *criticality* to future operations.
- Include an cost adjustment (% addition) to account for *economy of scale loss*.*

(*) Social Impact Commons created a calculator for this difference for the arts and culture community, based on analyzing over data in the SMU Data Arts set. Other similar calculators could be developed, provided similar data exists for other nonprofit subverticals.

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