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Misreporting Nonprofit Lobbying Engagement and Expenses: Charitable Regulation and Managerial Discretion

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Abstract:

On the one hand, nonprofits are expected to protect values, promote ideals, and effect change, and on the other hand, they are normatively and legally discouraged from engaging in advocacy and lobbying. These countervailing forces produce a tension that nonprofit managers must navigate. Although previous research suggests that normative boundaries and legal implications constrain lobbying efforts, it is possible that these factors merely influence how some charities report their lobbying activities to authorities. Indeed, incentives to misreport lobbying engagement exist at the federal level where regulatory oversight is lax. This article compares state data obtained for a sample of charities to contemporaneous federal data regarding the lobbying engagement, payments, and expenses of these organizations and their registered lobbyists. Findings demonstrate that roughly half of the charities sampled engage in more lobbying than they report to federal authorities, lending support to the premise that managerial discretion influences nonprofit reporting.

Keywords: nonprofit lobbying, charitable regulation, nonprofit law, Form 990, expense misreporting


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Public charities “are almost always founded for some purpose other than advocacy in the policymaking process” (Berry and Arons 2005, 25). And yet, nonprofits are trusted and experienced agents, uniquely positioned to advocate for policies that will benefit the people they serve and engage the community in public dialogue around important issues (Avner 2016, 397). As a consequence, many stakeholders encourage charities to get involved in the policymaking process, to: represent and magnify the voice of the disenfranchised, protect and endorse individual and group values, propose and pursue policies that address root causes of the problems they confront in direct service, or promote some social, political, or economic change (Avner 2016; Berry and Arons 2005).

Paradoxically, however, previous scholarship shows that nonprofit managers face normative and legal boundaries that discourage and constrain lobbying engagement (Bass et al. 2007; 2005; 2007). For section 501(c)(3) organizations in particular the legal repercussions associated with performing substantial lobbying are severe, such as possible taxation and loss of tax-exempt status. Several rationales exist for limiting charities from engaging in substantial lobbying activities. For some observers, lobbying is inconsistent with the historical concept of charity, raising concerns that excessive lobbying could produce divisiveness and polarization that would lead to a decline in the independence, legitimacy, and strength of the charitable sector (Simon, Dale, and Chisolm 2006). Other critics point to government subsidies granted charities through the tax code and contend that the U.S. Treasury and other governmental bodies responsible for overseeing charitable activity should remain neutral stakeholders in policy matters (Berry and Arons 2005). Finally, some commentators assert that permitting charities to influence the outcome of governmental decisions substantially is undemocratic and counter-majoritarian because it intensifies the disproportionate influence of their wealthy donors in the political process (Simon, Dale, and Chisolm 2006).¹

These countervailing forces produce a tension that nonprofit managers must navigate. On the one hand, nonprofits are expected to protect values, promote ideals, and effect change, and on the other hand, they are normatively and legally discouraged from engaging in advocacy and lobbying (Berry and Arons 2005). How, then, do nonprofit practitioners manage this tension? Although previous research suggests that normative boundaries and legal implications constrain lobbying among public charities, it is possible that for some entities these factors merely influence how they report their lobbying activities to authorities. Indeed, incentives to misreport lobbying engagement exist at the federal level where regulatory oversight is lax. The Internal Revenue Service’s Exempt Organizations division is ill-equipped to audit the activities of the roughly 500,000 charities that file

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Form 990 each year (Lott and Fremont-Smith 2016). Further, recent efforts by the 113th and 114th United States Congresses to minimize federal oversight of some tax-exempt groups and substantially reduce the IRS's budget have arguably created an even weaker federal regulatory regime (Colinvaux 2016; Lott and Fremont-Smith 2016).

Although federal agencies other than the IRS “oversee, or are implicated in, certain activities of charitable organization,” including, among others, the Federal Bureau of Investigation, Federal Emergency Management Agency, Federal Trade Commission, and United States Postal Inspection Service (Fremont-Smith 2004,), state authorities remain “the primary regulatory and enforcement players in the federalist scheme” (Lott et al. 2016,). This uneven regulatory environment creates opportunities for nonprofit managers to act strategically, and may influence how charities account for and report on their lobbying engagement and expenses to federal authorities.

In this article I compare IRS Form 990 data obtained for a sample of charities ($n = 143$) to contemporaneous data regarding the lobbying engagement, payments, and expenditures of these organizations obtained from the North Carolina Secretary of State. To my knowledge this is the first attempt to empirically verify the accuracy of lobbying expense reporting. In the first part of the article I briefly examine nonprofit lobbying research, identify inconsistencies in previous findings, and propose that unreliable data are undermining scholarship development. In the following sections, I rely on statutes, regulations, and prominent legal interpretations to detail the legal limits of lobbying for charities, and review state and federal reporting requirements.

Next, I turn to the analysis of lobbying data obtained from state and federal sources. Findings from the comparison of state and federal data suggest that charities report lower levels of lobbying activity and expenditures to federal authorities. Whether misreporting is intentional – i. e., “creative accounting” is used to cast the organization in a positive light by showing low lobbying involvement – or unintentional – i. e. illiteracy regarding what constitutes lobbying, how to allocate expenses, and how to report lobbying activity – is subject to interpretation, but findings are indicative.

Nonprofit Lobbying Literature

Nonprofit research over the last two decades has sought to understand the factors that influence whether nonprofits will engage in lobbying (e. g., Child and Grønberg 2007; Mosley 2010; Nicholson-Crotty 2007, 2009; Suarez and Hwang 2008), which nonprofits are more likely to lobby (e. g., Child and Grønberg 2007), how much nonprofits will spend to influence legislation (e. g., Harris, Leece, and Neely 2017), how nonprofits will report their lobbying (e. g., Harris, Leece, and Neely 2017; Nicholson-Crotty 2007), and which lobbying strategies nonprofits will employ (e. g., Chaves, Stephens, and Galaskiewicz 2004; Mosley 2011; Nicholson-Crotty 2009). According to this literature, managerial professionalization (e. g., manager's tenure in position, work experience, level of education), organizational financial support (e. g., amount of individual donations and government grants), organizational capacity (e. g., nonprofit's age and size), and context (e. g., political and policy environment, level of competition in policy area) affect whether and to what extent nonprofits lobby.

Although our understanding of nonprofit lobbying has improved considerably, several unknowns remain. For example, despite concerted effort to uncover the influence of government funding on lobbying, studies report divergent findings. Numerous studies indicate government funding “crowds-in” or stimulates nonprofit advocacy (e. g., Harris, Leece, and Neely 2017; Mosley 2011; Moulton and Eckerd 2012; Salamon 2002), while others find that government funding “crowds-out” or constrains nonprofit advocacy (e. g., Child and Grønberg 2007; Guo and Saxton 2010; Suarez and Hwang 2008). The inconsistency in studies emanates, at least in part, from scholars' variable operationalization of lobbying (Almog-Bar and Schmid 2014) and dependence on unreliable or localized data (Prentice 2018).

Although nonprofit scholars are increasingly addressing, and attempting to resolve, construct validity concerns related to the use of various definitions of advocacy and lobbying (see Neumayr, Schneider, and Meyer 2015; Prentice 2018), little attention is given to the validity and reliability of nonprofit lobbying data. This article addresses the gap in the literature by examining the primary data source upon which numerous lobbying studies are performed – Internal Revenue Service Form 990 – and comparing them to a new source of publicly available nonprofit lobbying information. An analysis of the legal boundaries and regulatory environment for charitable organizations engaging in lobbying is necessary before such a comparison can be made and understood. Thus, the following two sections examine the federal and state lobbying laws and reporting requirements that establish the foundation for this research.

Federal Lobbying Laws and Regulation

To obtain recognition of tax-exempt status under section 501(c)(3) of the Internal Revenue Code (IRC), nonprofits must pass “organizational” and “operational” tests aimed at evaluating the purpose, financing, and activities of the organization to ensure compliance with prescribed criteria (Fishman and Schwarz 2010). One criterion is the restriction against lobbying constituting a “substantial part” of the organization’s activities. For example, if a nonprofit corporation seeking recognition of tax-exempt status under section 501(c)(3) states in its articles of organization that it will engage in lobbying, then it must also state that its lobbying efforts will be an insubstantial part of its overall activities or face being classified as an “action organization” and denied recognition as a public charity (Hopkins 2011).

In addition to the prohibition against engaging in substantial lobbying, charities are specifically barred from engaging in extensive grassroots lobbying. A charity subject to the expenditure test may only spend 25 % of its total allowable lobbying expenses on grassroots lobbying (see IRC §§501(h) and 4911(c)). To compel compliance with federal lobbying regulations, public charities that engage in substantial lobbying, or exceed lobbying expenditure limits, face excise taxes (IRC § 4911(a)) and possible loss of tax-exempt status (www.irs.gov).

The restrictions on lobbying placed on private foundations, which are more narrowly funded (i. e., financed by fewer, typically private, donors) and more tightly governed (i. e., oftentimes directed by members of a single family or institution, and sometimes by a single trustee) than public charities, are even stricter. Private foundations are not permitted to engage in any lobbying. The prohibition on private foundations engaging in lobbying stems from proscriptions against private inurement and serves to ensure that the organization operates to further public rather than private interests. Private foundations that lobby face sizable excise taxes and possible loss of tax exemption (IRC § 4945(a)). Additionally, foundation managers who approve the lobbying expenditure face excise taxes (IRC § 4945(a)).

Annual Federal Reporting and Lobbying Expenditure Limits

The IRS requires tax-exempt organizations to report annually on their lobbying engagement, activities, and expenditures via Form 990 and its supplement Schedule C. Reporting on these forms varies depending upon whether the public charity takes the 501(h) election, a status that requires additional reporting by the nonprofit in return for clearer legal boundaries. Charities that do not take the 501(h) election are subject to the “substantial part test,” which requires filers to report information about the organization’s lobbying activities and expenses, but does not impose exact limits.² The substantial part test evaluates whether the reported list of activities and expenditures constitute a substantial part of an organization’s work. Given the significant room for interpretation regarding how much lobbying it takes to be considered substantial, and the harsh implications for doing too much lobbying (e. g., loss of tax-exempt status), many organizations opt for the legal bright lines afforded by taking the 501(h) election.

Charities filing Form 5768 and electing the “lobbying expenditure test” under section 501(h), must disclose total direct and grassroots lobbying expenditures.³ To satisfy the lobbying expenditure test, filers calculate their “exempt purpose expenditures” and reference an embedded table in Schedule C to determine the corresponding federal limit on lobbying expenditures – their “lobbying nontaxable amount.” For example, organizations with exempt purpose expenditures equal to or less than \$500,000 are allowed to spend up to 20 % of their outlays tax free (i. e., their lobbying nontaxable amount is \$100,000). As exempt purpose expenditures increase, the limits become more restrictive. For example, an organization with exempt purpose expenditures of \$1.5 million may only spend 15 % of its outlays (i. e., \$225,000) tax free. The IRS imposes a lobbying nontaxable amount cap of \$1 million that is reached when organizations have \$17 million or more in exempt purpose expenditures.

The IRS also requires h-electors to calculate separately their “grassroots nontaxable amount” and disclose their grassroots lobbying expenditures. The grassroots nontaxable amount is calculated as 25 % of the lobbying nontaxable amount. For example, an organization with a lobbying nontaxable amount of \$100,000 has a grassroots nontaxable amount of \$25,000 and may only spend that sum to support grassroots lobbying efforts. Organizations exceeding either lobbying limit – i. e., spending more on lobbying than its lobbying nontaxable amount or grassroots nontaxable amount – are subject to further reporting and taxation. Additionally, organizations exceeding their “lobbying ceiling amount,” 150 % of their lobbying nontaxable amount over a 4-year averaging period, can lose their tax-exempt status.

State Lobbying Laws and Regulation

By contrast to federal regulations, which prohibit public charities from engaging in substantial lobbying and impose strict legal limits for charities taking the 501(h) election, North Carolina statutes do not limit charities in their lobbying expenditures. All NC organizations are subject to state lobbying laws found in General Statutes Chapter 120C (N.C.G.S. § 120C), and no distinctions in the law are made for nonprofit organizations. The statutes contain general provisions defining lobbying, registration procedures and fees, prohibitions and restrictions, reporting requirements, enforcement powers, and punishments for violation. Descriptions of legislation, legislative action, and lobbying provided in the statutes, and through clarifications of the statutes offered by the Secretary of State and the State Ethics Commission are similar to IRS interpretations of federal law. However, some minor differences exist.

The most pronounced difference between NC and federal law relates to how organizations are directed to account for grassroots lobbying and report on such activity. In NC grassroots lobbying is referred to as the “solicitation of others” and is more narrowly construed than at the federal level. Both federal and state authorities provide categories of exempted communication, which allow organizations to engage in certain lobbying-like activities without those activities or associated costs officially counting toward organizational lobbying totals. However, NC exempts all forms of grassroots lobbying communications made by organizations to its “employees, board members, officers, members, subscribers, or other recipients who have affirmatively assented to receive ... regular publications or notices” (N.C.G.S. § 120C-100). Additionally, NC requires only that organizations report grassroots lobbying expenses exceeding an aggregate cost of \$3,000 during any 90-day reporting period. Hence, all else equal, these differences imply that organizations will report fewer grassroots lobbying expenditures to NC authorities than to the IRS.

Annual State Reporting

By contrast to the federal level where the IRS only requires nonprofits to report their lobbying activity once annually in their Form 990, NC policies and practices ensure that nonprofits and their lobbyists report to state authorities multiple times throughout the year. First, organizations and lobbyists must register annually with the NC Secretary of State’s Lobbying Compliance Division. Principal registration entails providing basic information on the organization and the authorized lobbyist, and stating whether the authorized lobbyist is an in-house employee or hired professional. Principal organizations are required to file separate registration statements for each lobbyist they authorize to lobby on their behalf. Similarly, lobbyists must complete distinct registrations for each organization they represent, offering much of the same basic organizational and personal information as principal registrants. Additionally, lobbyists must indicate at registration the “general subjects” on which they intend to lobby on behalf of principals (e. g., education, health service, recreation, transportation, etc.) and the level of government they intend to target (e. g., municipal, county, state, federal).

Subsequently, organizations and lobbyists are required to submit to the Secretary of State’s Lobbying Compliance Division quarterly expense reports detailing reportable expenditures, principal reimbursement of lobbyist expenses, payments to lobbyists, and contractual arrangements or direct business relationships with legislators. Quarterly reports must be filed even when no expenditures or payments are made. Thus, nonprofits and their authorized lobbyists report lobbying engagement to NC authorities a minimum of five times per year (registration plus four quarterly reports), and often more frequently if expense reports are amended. Despite these reporting requirements, nonprofits are not subject to state limits on lobbying, only federal limitations.

Understanding Misreporting

The preceding sections elucidate the federal and state legal boundaries, regulatory environment, and reporting requirements for charitable organizations, and offer a foundation upon which a comparison of federal and state lobbying data may be performed and understood.

Previous research illustrates that nonprofit managers feel pressure from charity watchdog groups (e. g., Charity Navigator, BBB Wise Giving Alliance) and donors (e. g., individual contributors, granting foundations), who use Form 990 information to evaluate nonprofits, to report low overhead costs and high programmatic output (Eckerd 2014; Garven, Hofmann, and McSwain 2016; Parsons, Pryor, and Roberts 2017). Additionally, research demonstrates that nonprofits, perhaps as a result of these pressures, often misreport certain expenses on Form 990, including: program, fundraising, and administrative (Froelich and Knoepfle 1996; Hager 2003; Keating, Parsons, and Roberts 2008; Krishnan, Yetman, and Yetman 2006; Trussel 2003). However, the literature

has not addressed whether nonprofits also misreport lobbying engagement and expenses to the IRS. Given the strict legal federal limits placed on charitable lobbying and the harsh implications for exceeding those limits, it is likely that nonprofit managers also feel pressure to show low lobbying involvement. This study addresses the gap in the literature and extends our understanding of nonprofit reporting to public authorities by comparing federal and state reports of charitable lobbying for a sample of nonprofits.

For the sample of charities examined in this study lobbying expenditures reported to the state should be equal to or lower than lobbying expenditures reported to the IRS. Three points support this assertion. First, NC excludes certain communications to members from lobbying calculations, but the IRS does not (i. e., filers report more categories of lobbying activities and expenditures to the IRS than to NC). Second, the IRS requires filers to account for and disclose all grassroots lobbying activities and expenditures, while NC only asks them to report grassroots expenditures if the total equals or exceeds \$3,000 per reporting period. Third, NC lobbying data capture only lobbying performed within the state. Charities that also lobby in other states (e. g., South Carolina, Virginia, or Washington, D.C.) do not report those activities or expenses to NC, but would report them to the IRS. Given these structural differences, lobbying expenditures reported to NC authorities should be equal to or lower than totals reported to the IRS. The following section introduces the lobbying data and methodologies employed in this study.

Methodology

To assess the accuracy of IRS lobbying information this study compares Form 990 data for a sample of charities to contemporaneous lobbying data from the NC Secretary of State on the organizations and their registered lobbyists. The following paragraphs detail the process by which charitable lobbying data were collected from federal and state authorities and present the methodologies employed in the empirical analysis.

Data

Individuals and organizations that lobby in NC must register annually with the Secretary of State and complete quarterly expense reports. Registration forms and expense reports are made public on the Secretary of State's website. All 828 organizations (for-profit and nonprofit) that registered to lobby in the state in 2010 and 2011 were reviewed in this analysis.⁴ Nonprofit firms ($n = 412$) were separated from for-profit firms ($n = 416$) using data from a repository of state corporate filings. Next, the 2010 IRS Business Master File and the National Center for Charitable Statistics' searchable database were used to identify nonprofits' employer identification numbers and further reduce the sample to include only section 501(c)(3) organizations. Of the 412 nonprofit organizations, 143 were identified as 501(c)(3) public charities and none of the organizations were private foundations. The balance of the nonprofits fell across various other tax-exempt classifications, with the majority ($n = 208$) registered as 501(c)(6) organizations (i. e., member-serving organizations such as business leagues, chambers of commerce, real estate boards, etc.).

Hence, this analysis considers the full population of NC incorporated public charities ($n = 143$) that collectively authorized 288 lobbyists to lobby on their behalf. Fiscal year 2011 Form 990 was accessed for each of the charities and corresponding state-level data were also obtained. Since fiscal years can vary, state lobbying registration forms and quarterly principal and lobbyist expense reports were individually selected to match each organization's stated fiscal year on their Form 990. For example, for organizations with fiscal year July 1, 2010 to June 30, 2011, I selected state-level expense reports for the latter half of 2010 (third and fourth quarter) and the first half of 2011 (first and second quarter) to ensure consistent time intervals and data comparability between the federal and state sources. Information from over 2,100 scanned registration filings and expense reports, including payments to lobbyists and additional lobbying expenses, were manually entered to construct the state-level data utilized in the comparative analysis. Form 990 data on lobbying engagement (Part IV, line 4), lobbying payments to professionals (Part IX, line 11d), and lobbying activities and expenses (Schedule C, Part II-A and Part II-B) were also collated.

Empirical Analysis

The empirical analysis involved three stages: an initial descriptive comparison of the state and federal data, a subsequent statistical analysis comparing organizations that misreported to those that did not misreport across a range of organizational variables, and regression modeling to discern the factors that influence lobbying mis-

reporting. For the descriptive analysis, state and federal lobbying engagement and expense data were compared for the full sample of charities for the fiscal year and differences were noted.

Next, t-tests were conducted to identify the organizational characteristics associated with the incidence of misreporting. Misreporting was operationalized via two methods. The first binary variable captured organizations that reported greater lobbying expenditures to the state than they did to the IRS (evidence of misreporting = 1, no evidence of misreporting = 0). The second binary variable included organizations that reported lobbying expenditures to the state, but did not report any lobbying engagement or expenses to the IRS (evidence of misreporting = 1, no evidence of misreporting = 0). Predictors of fundraising expense misreporting identified in previous studies (Keating, Parsons, and Roberts 2008; Krishnan, Yetman, and Yetman 2006; Trussel 2003) and additional variables were analyzed, including organizational capacity (age, size), professionalization (executive compensation, existence of an audit, accrual accounting practices, number and type of lobbyists), revenue streams (program, government grants, contributions, investment income, membership dues, other), and mission area (environment, arts, education, health, human services, public benefit). Table 1 presents descriptive statistics for all variables.

Table 1: Descriptive statistics.

Variable name	Mean	Std Dev	Range
<i>Misreporting</i>			
Reported greater expenditures to NC than IRS	0.44	0.50	0 – 1
Did not report any engagement to IRS	0.27	0.44	0 – 1
<i>Capacity</i>			
Age (years)	26.88	17.07	2 – 89
Size (total assets)	\$226,943,746	\$968,411,656	\$10,972 – \$9,378,030,720
<i>Professionalization</i>			
Executive compensation	\$924,824	\$2,379,186	\$0 – \$19,570,803
Audit	0.85	0.36	0 – 1
Accrual	0.87	0.34	0 – 1
Signatory	0.31	0.46	0 – 1
In-house lobbyists	1.10	1.23	0 – 7
Professional lobbyists (%)	0.45	0.44	0 – 1
<i>Revenue streams</i>			
Government grants	\$10,917,790	\$56,667,094	\$0 – \$579,002,585
Dues	\$251,815	\$1,990,552	\$0 – \$21,967,052
Program	\$56,622,577	\$171,290,956	\$0 – \$877,653,989
Contributions	\$32,789,012	\$129,064,723	\$0 – \$1,131,249,755
Investment	\$4,566,259	\$24,458,337	-\$8,664,123 – \$259,133,753
Other	\$1,917,747	\$10,414,774	-\$7,984,140 – \$89,696,869
<i>Mission area</i>			
Environment	0.13	0.34	0 – 1
Arts	0.03	0.17	0 – 1
Education	0.12	0.33	0 – 1
Public benefit	0.18	0.38	0 – 1
Health	0.22	0.41	0 – 1
Human services	0.23	0.42	0 – 1

Notes: Raw numbers are reported in this table for ease of interpretability. Age is the number of years since recognition of tax-exempt status; Size is the natural log of total assets at end of year; Executive compensation is the natural log of compensation of current officers, directors, trustees, and key employees; Audit is whether the organization had an audit; Signatory is whether the person signing the return is CFO or Treasurer; In-house lobbyists is the number of lobbyists who are employees; Professional lobbyists is the number of outside hired lobbyists divided by total lobbyists; Government grants is natural log of government grants; Dues is natural log of membership dues; Program is natural log of program service revenue; Contributions is natural log of all other contributions, gifts, grants; Investment is investment income standardized (variable has too many large negative values to perform natural log); Other is other revenue standardized (variable has too many large negative values to perform natural log); mission areas are determined using NTEE codes.

Finally, generalized linear modeling (GZLM) was used to run numerous regressions for each of the binary dependent variables. GZLM uses maximum likelihood estimation for the regression parameters and has less restrictive assumptions with respect to normality, linearity, and constant variance than general linear modeling. Thus, it is preferred for these data. Given the distribution of the variables, a binomial probability distribution and logit link function were specified for the analysis. Initially all predictors with assumed effects were modeled. Then, consistent with commonly accepted practice (Garson 2013), nonsignificant predictors were removed one at a time until the most parsimonious models with the best fit were identified. Multiple robustness checks were performed while monitoring goodness of fit statistics, model effects, and parameter estimates to improve validity and ensure the coefficients are meaningful.

Findings

Results from the comparison of state and federal data suggest numerous charities underreport lobbying engagement and expenses to the IRS. Table 2 shows that of the 143 charitable organizations that filed registration paperwork with the state signaling their intent to lobby, only 100 of them indicated to the IRS that they engaged in lobbying activity on their Form 990 or were an h-elect. It is possible that some of the organizations in the sample intending to lobby registered with the state, but ultimately did not engage in the practice. However, the number of organizations that may have done so is few, since only 7 organizations reported zero lobbying expenses to the state and reported no lobbying engagement to the IRS. Indeed, the Secretary of State expense data show that the great majority of the organizations ($n = 132$; 92.3 %) did engage in lobbying, with charities reporting lobbying expenses ranging from \$87 to \$174,452 per organization for a total \$3,449,100 for fiscal year 2011. Average spending on lobbying for the 132 charities was \$26,130, with a median of \$15,375.

Table 2: Descriptive results of state and federal data.

Sample criteria	<i>n</i>	%
Registered to lobby with NC Secretary of State	143	100
Reported lobbying expenses to NC Secretary of State	132	92.3
Reported lobbying activity to IRS or elected 501(h)	100	69.9
Reported payments to professional lobbyists to NC Secretary of State	72	50.3
Reported payments to professional lobbyists to IRS	44	30.8
Reported higher total lobbying expenses to NC Secretary of State than IRS	63	44.1
Reported lobbying expenses to NC Secretary of State but not to IRS	38	26.6

Notes: Findings in table are presented as proportion of sample meeting criteria.

State data also indicate that 80 charities (55.9 %) authorized a total of 133 outside professionals to lobby on their behalf, with 72 of the organizations (50.3 %) making payments to 127 of them. Notably, however, only 44 organizations (30.8 %) reported payments to professional lobbyists on their Form 990. Thus, 28 charities (19.6 %) reported payments to professional lobbyists totaling \$968,235 to the State of NC, but did not report these payments to the IRS.

Nearly half of the sample (63 charities, 44.1 %) reported greater lobbying expenditures to the state than to the IRS. As a group, these 63 charities reported \$1,368,618 more lobbying expenditures to NC than to the IRS ($M = \$21,724$ and $Mdn = \$10,313$). Further, 38 charities (26.6 %) from this group reported no lobbying to the IRS, but cumulatively reported \$875,511 in lobbying expenditures to the state. Some examples of lobbying expenditures described in the principal expense reports to the state, include: event costs (parking, venue rental, award plaques, catering), printing and merchandise costs (brochures, postcard petitions, flyers, tote bags, fleece blankets), as well as various other costs (rental space for a legislator's law office, call center services, funded international travel for legislators).

T-Tests

T-tests were conducted to explore whether certain organizational characteristics are associated with the incidence of misreporting. Findings in Table 3 show that capacity, professionalization, and certain revenues are associated with lower levels of misreporting, while mission area is less influential. Results show that larger organizations were less likely to misreport lobbying expenses ($t = -3.79$, $p = 0.00$) and engagement ($t = -2.13$, $p = 0.04$) to the IRS. Older organizations were not found to misreport at statistically significant lower rates, as anticipated, however age did seem to exert some downward pressure on expense misreporting ($t = -1.61$, $p = 0.11$). The professionalization variables yield perhaps the most consistent findings. Many of the professionalization variables attain statistical significance, and most of them indicate that higher levels of professionalization yield lower levels of misreporting. Organizations that had an audit during the fiscal year, an accrual system of accounting, a chief financial officer or treasurer (who presumably has greater financial literacy) as the signatory of the return, and higher executive pay were less likely to misreport their lobbying engagement, and, with the exception of the accrual variable, less likely to underreport their lobbying expenses.

Table 3: T-test results.

	Reported greater expenditures to NC than IRS	Did not report any engagement to IRS
<i>Capacity</i>		
Age	-1.61	-1.13
Size	-3.79***†	-2.13**
<i>Professionalization</i>		
Executive compensation	-2.51**†	-4.10***†
Audit	-2.22**†	-2.55**†
Accrual	-0.60	-1.70*†
Signatory	-2.87***†	-2.16**†
In-house lobbyists	0.03	-2.09**
Professional lobbyists (%)	1.67*	2.05**
<i>Revenue streams</i>		
Government grants	-1.08	-1.61
Dues	0.48	0.16
Program	-2.65***	-0.25
Contributions	-2.32**	-2.99***†
Investment	-1.57†	-0.75
Other	-3.48***	-2.46**
<i>Mission area</i>		
Environment	-1.77*†	-1.32†
Arts	1.17†	0.85†
Education	1.24†	0.84
Public benefit	-0.48	-0.34
Health	-0.71	0.32
Human services	0.54	-1.95*†

Notes: Table reports t-test statistic and significance. Two-tailed: * significant at 0.10; ** significant at 0.05; *** significant at 0.01. † denotes that equal variances not assumed.

Organizations with a greater number of in-house lobbyists were less likely to misreport lobbying engagement to the IRS ($t = -2.09$, $p = 0.04$). However, as the ratio of professional lobbyists to total lobbyists rose, the incidence of misreporting increased: Organizations that relied more on professional lobbyists were more likely to underreport lobbying expenditures ($t = 1.67$, $p = 0.10$) and more likely to misreport lobbying engagement ($t = 2.05$, $p = 0.04$) to the IRS.

Increases in revenue tend to exert downward pressure on misreporting, however, not all revenue streams are consequential. Revenue from government grants, membership dues, and investments do not have statistically significant relationships with either misreporting variable. Greater revenue from contributions is associated with lower incidences of misreporting lobbying expenditures ($t = -2.32$, $p = 0.01$) and lobbying engagement ($t = -2.99$, $p = 0.01$). Greater revenue from other sources (e. g., rental income, royalties, fundraising events, sales of inventory, etc.) also influenced reporting, with lower levels of misreporting lobbying expenditures ($t = -3.48$, $p = 0.00$) and lobbying engagement ($t = -2.46$, $p = 0.02$). Greater program revenue yielded lower levels of expense misreporting ($t = -2.65$, $p = 0.01$), but did not have a notable influence on lobbying engagement reporting.

Finally, mission area appears to be less consequential than capacity, professionalization, and revenue in influencing misreporting. Human services organizations were less likely to misreport lobbying engagement ($t = -1.95$, $p = 0.06$) and environmental charities were somewhat less likely to underreport lobbying expenditures ($t = -1.77$, $p = 0.08$). Arts, education, public benefit, and health charities do not appear more or less likely to misreport lobbying engagement or expenses.

Generalized Linear Modeling

Multiple regression models were run to explore the combined effects of the independent variables on the two binary dependent variables. Initial runs included all independent variables with possible influence on the dependent variables, then coefficients were trimmed one at a time until the most parsimonious models were identified. Multiple robustness checks were performed to ensure the appropriate selection of coefficients.

Reported Greater Expenditures to NC than IRS (Dependent Variable #1)

Findings in Table 4 show that, when controlling for the effects for other variables, only a handful of items consistently influence whether charities report greater lobbying expenditures to the NC Secretary of State than to the IRS. The parsimonious model that attained the best fit (i. e., had the lowest Bayesian Information Criterion) shows that organizational capacity, professionalization, and certain revenues all play a role in misreporting.⁵ Larger organizations and nonprofits with greater contributions were far less likely to underreport lobbying expenditures to the IRS ($\chi^2 = 12.30$; $p = 0.00$ and $\chi^2 = 9.35$; $p = 0.00$, respectively). Conversely, organizations with more lobbyists and specifically those that employed outside professionals to lobby at a higher rate were statistically significantly more likely to underreport their lobbying expenditures to the IRS ($\chi^2 = 7.32$; $p = 0.01$ and $\chi^2 = 9.24$; $p = 0.00$, respectively). Charities receiving greater government grants revenue were also somewhat more likely to underreport their lobbying expenditures to federal authorities ($\chi^2 = 2.62$; $p = 0.11$).⁶

Table 4: GZLM results: Reported greater expenditures to NC.

Model	B	Std. error	Hypothesis test Wald Chi-square	Significance
(Intercept)	5.97	1.79	11.12	0.00
Size	−0.35	0.10	12.30	0.00
Contributions	−0.23	0.08	9.35	0.00
Government grants	0.07	0.04	2.62	0.11
In-house lobbyists	0.58	0.21	7.32	0.01
Professional lobbyists (%)	2.02	0.67	9.24	0.00

Notes: Dependent Variable: Reported greater expenditures to NC than IRS. $n = 143$. Trimmed model Bayesian Information Criterion (BIC) = 153.31; full model BIC = 190.75.

Did Not Report Lobbying to IRS (Dependent Variable #2)

Findings from the analysis of the second binary dependent variable (Table 5) are similar to the first. In the fitted model, a mix of organizational capacity, professionalization, and revenue variables attained statistical significance.⁷ Larger organizations were less likely to report lobbying expenses to the state and fail to report lobbying engagement or expenses to the IRS at statistically significant levels ($\chi^2 = 7.00$; $p = 0.01$). Likewise, human services nonprofits and organizations with greater contributions were less likely to misreport their lobbying engagement and expenditures to the IRS ($\chi^2 = 6.32$; $p = 0.01$ and $\chi^2 = 12.06$; $p = 0.00$, respectively). Conversely, organizations that relied more heavily on outside professionals to lobby on their behalf were significantly more likely to report expenditures to the state and fail to report engagement and expenditures to the IRS ($\chi^2 = 3.24$; $p = 0.07$). Finally, although the variable did not achieve statistical significance, the results suggest that organizations with more government grants are somewhat more likely to misreport to the IRS as well ($\chi^2 = 1.79$; $p = 0.18$).

Table 5: GZLM results: Failed to report lobbying to IRS.

Model	B	Std. Error	Hypothesis Test Wald Chi-Square	Significance
(Intercept)	7.07	2.45	8.34	0.00
Human Services	−1.99	0.79	6.32	0.01
Size	−0.34	0.13	7.00	0.01
Contributions	−0.30	0.09	12.06	0.00
Government grants	0.07	0.05	1.79	0.18
Professional lobbyists (%)	1.12	0.62	3.24	0.07

Notes: Dependent Variable: Reported lobbying expenses to the state but did not report any lobbying engagement or expenses to IRS. $n = 143$. Trimmed model BIC = 116.61; full model BIC = 158.21.

Discussion

Previous studies analyzing Form 990 data concede that properly accounting for expenses and reporting on them via Form 990 is complex. According to Froelich, Knoepfle, and Pollak (2000, p. 234), several factors may contribute to Form 990 inaccuracies, including “unclear guidelines for entry calculations,” preparation of returns by “outside accountants with limited knowledge of the organization and its activities,” and “in-house preparation of returns by nonprofit employees with inadequate accounting” proficiency. Although these potential accounting-related issues suggest that human error may contribute to expense misreporting, they do not suggest a directional bias toward over- or underreporting expenses. However, structural differences in reporting between state and federal authorities imply that differences should exist between state and federal lobbying reports.

For the sample of charities under examination, state expenditures should be lower than federal expenditures for three primary reasons. First, lobbying communications encouraging organizational members and newsletter recipients to contact their legislators to voice support or opposition to legislation are exempted from grassroots lobbying expenditure calculations in state law, but not in federal law. Second, grassroots lobbying activities with aggregate costs less than \$3,000 per reporting period (i. e., per quarter) are not subject to reporting requirements in NC but must be reported to the IRS. Finally, and most importantly, the state lobbying expenditures analyzed here only reflect the lobbying activities of organizations within NC. Charities can, and often do, engage in lobbying across state lines. Form 990 requires filers to report all lobbying activities, irrespective of jurisdiction. And yet, despite these factors, nearly half of the charities in this study reported lower levels of lobbying engagement or fewer lobbying expenditures to the IRS than to state authorities. Additionally, recall that for half the sample the results only show that no evidence of misreporting exists, which is different than saying that these charities reported accurately. Thus, the actual number of charities that misreport lobbying engagement and expenditures is likely higher than found here.

Results from the descriptive analysis show substantial differences in reported lobbying engagement, lobbying payments to non-employees, and total lobbying expenditures. Nonprofits in the sample failed to report over \$1.35 million in lobbying expenditures, including nearly \$1 million in payments to professional lobbyists, to the IRS. To demonstrate the scale of misreporting uncovered in this study, records for 2 charities that showed significant variances in reporting were reviewed for additional years. Charity A, for the period of 2007 to 2013, reported no lobbying engagement or expenses to the IRS on their tax returns. Yet, the charity reported lobbying payments and expenses to the NC Secretary of State totaling in excess of \$300,000 for the same period. Charity B reported no lobbying engagement or expenses to the IRS from 2004 to 2014, but records from the NC Secretary of State for five of the years (2010 to 2014) show lobbying expenses totaling in excess of \$550,000. Although larger and more professionalized organizations are generally less likely to misreport, these findings demonstrate that nonprofits of all sizes misreport lobbying engagement and expenses to the IRS.

Group differences analyzed via t-tests offer some interesting bivariate findings, including the apparent influence of capacity, professionalization, and certain revenue streams on reporting accuracy. The regression results offer the most notable findings, particularly the strong effects of contributions and the use of professional lobbyists on reporting accuracy. Charities were significantly less likely to misreport lobbying engagement and expenditures as contributions increased. It is possible for organizations in the sample that contributions were given to support lobbying efforts, thereby reducing incentives to misreport. Managers might be strategically choosing to report accurately their lobbying efforts on Form 990 as a means of demonstrating to their contributors and other stakeholders the organizational commitment to furthering advocacy-related goals. As long as charities steer clear of federal lobbying limits, accurate lobbying disclosure could be fulfilling promises to donors and driving future giving to the organization.

The use of outside professional lobbyists also seems to have consequences for reporting accuracy. Charities were more likely to underreport lobbying engagement and expenses to the IRS as the use of professional lobbyists increased. It is possible that employing professional lobbyists increases opportunities for the loss of information between consultant and organization (for instance, from a communication gap or breakdown), and inconsistencies in state and federal reporting emerge as a product of human error. However, it seems more plausible that organizations are strategically hiring professional lobbyists at a higher rate in an effort to distance themselves from lobbying activities and avoid the possible negative ramifications.

Among the possible reasons to explain the observed disjuncture in state and federal reporting is the uneven regulatory environment. Although definitions of legislation and lobbying enacted by NC mirror respective federal definitions, registration requirements, reporting procedures, and enforcement differ significantly between state and federal authorities. Whereas the IRS requires only that organizations report lobbying activities once annually on their Form 990, NC policies and practices ensure that organizations and lobbyists report lobbying activities to state authorities multiple times throughout the year. Additionally, by requiring both lobbyists and their principal organizations to file quarterly reports consistently, there is a greater likelihood that data are

cross-validated and incentives to misreport to state authorities are reduced. Finally, whereas federal punishments target the public charity as a whole (and not the reporting manager), NC's punishments for misreporting are aimed at the individual. Penalties for violations in North Carolina are severe, and include possible fines (\$5,000 per violation), criminal charges (class 1 misdemeanor), and a 2-year lobbying ban in the State (N.C.G.S. § 120C-602).

Conclusion

The federal prohibition against performing substantial lobbying and gaps in the regulatory environment (with less oversight of nonprofit lobbying by the IRS than in NC) create incentives for nonprofit managers to underreport lobbying engagement and expenses to federal authorities. Previous scholarship demonstrates that nonprofit managers misrepresent certain expenses (e. g., fundraising) on Form 990 to avoid public scrutiny and negative evaluations (Keating, Parsons, and Roberts 2008; Krishnan, Yetman, and Yetman 2006). Thus, it is possible that nonprofit managers also manage lobbying disclosures on Form 990, especially given the strict legal limits and serious consequences for engaging in substantial lobbying (taxation or loss of tax-exempt status).

In an effort to validate the accuracy of lobbying reports this study compared Form 990 data to information from the NC Secretary of State. Findings demonstrate that numerous charities misreport lobbying engagement and expenses on Form 990. Although the absence of legal and accounting sophistication among nonprofit managers and directors potentially plays a role in misreporting, the results show widespread underreporting to federal authorities where charities face lobbying limits and less oversight. This finding suggests lobbying expense misreporting may be less about accounting sophistication and more about managers intentionally manipulating disclosure.

Although this inquiry offers an important first step toward understanding how and why charities report, and misreport, their lobbying activities to state and federal authorities, the study has limitations. Data for this analysis emanate from a single state and at a single time; hence, I caution against drawing inferences too generally. The findings' basis in population data increases confidence in external validity; however, findings may vary in states with differing regulatory conditions and reporting requirements. Future scholarship might conduct longitudinal analysis or consider a broader sample. Additionally, without a qualitative component it is not possible to ascertain the precise causal mechanism to explain the results unearthed in this study. The findings suggest organizational size, level of contributions, and the mix of in-house vs. hired lobbyists play a role. Future research could employ a mixed-methods research design and conduct interviews with nonprofit leaders to explore whether other unexplored factors influence reporting. Despite these limitations, this study offers a strong foundation for further exploration on nonprofit lobbying and charitable expense reporting. More broadly, the findings suggest scholars might consider looking beyond Form 990 data to state-level information where oversight and reporting are presumably more pronounced.

Notes

- 1 For a comprehensive history of lobbying restriction and regulation in the United States, please see Fremont-Smith (2004), Berry and Arons (2005), and Kindell and Reilly (1997).
- 2 Organizations subject to the substantial part test complete Schedule C, Part II-B, a Form 990 supplement that asks filers to provide yes or no responses to questions about who engaged in lobbying on behalf of the organization (e. g., volunteers, paid staff) and how they lobbied (e. g., media advertisements, mailings, publications, rallies, direct contact with legislators, grants to other organizations for lobbying purposes, among other activities). For each "yes" response, filers must specify the amount spent on the lobbying activity and provide a detailed description of the lobbying activity in Schedule C, Part IV.
- 3 An organization that is part of an affiliated group must also check the appropriate boxes in Schedule C, Part II-A, column b, and list the affiliated group members in Part IV.
- 4 Calendar year 2010 was the most recent data available when data collection initiated. Repeated efforts by the author to obtain more recent data from the NC Secretary of State's office were ignored for several months. Eventually several additional years were made available, at which time 2011 data were downloaded and manually added to the author's 2010 dataset. Data from 2012 to 2014 were also used in the longitudinal analysis of two charities selected from the sample.
- 5 The fitted model was statistically significantly better than the intercept-only model ($G = 31.82$; $p = 0.00$) for these data.
- 6 On the recommendation of an anonymous reviewer, I performed bivariate and multivariate tests to explore the relationship between taking the 501(h) election and dependent variable #1 (reported greater expenditures to NC than IRS) and the results were not significant. Bivariate and multivariate tests were not performed for dependent variable #2 (did not report to IRS) because organizations that took the 501(h) election are measured in dependent variable #2. The variable captures organizations that made any reference to lobbying in their 990, including the 501(h) election, even if they did not perform lobbying in the current fiscal year and reported no expenses).
- 7 The fitted model was statistically significantly better than the intercept-only model ($G = 30.19$; $p = 0.00$) for these data.

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