

# **The Effects of Governance on the Financial Reporting Quality of Nonprofit Organizations**

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*Abstract:* Various stakeholders use nonprofit financial information for investing, contracting, and regulating decisions, and these decisions can be affected by the quality of the underlying financial information. Using multiple measures of financial reporting governance and reporting quality, we find that higher reporting quality is associated with increased governance. We find that our market-based governance measures have a more consistent effect on nonprofit reporting quality than do our regulatory-based measures. Our findings suggest that attempts to enhance the monitoring and oversight of nonprofits can lead to higher quality financial reports, particularly if those efforts involve market participants such as lenders or donors.

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## 1. Introduction

Publicly available financial reports play an important informational role by mitigating the inherent principal-agent conflict within organizations. By utilizing information about the financial condition and performance of an organization, various stakeholders can make more informed investing, contracting, and regulating decisions (Watts and Zimmerman 1986). The appropriateness of stakeholder decisions is at least partly a function of the quality of the financial reports used. Recent well-known accounting related scandals in the for-profit setting suggest that financial reporting quality is not uniformly high.

Failures in financial reporting also occur in the nonprofit sector. One recent example involves an organization whose charitable purpose was to collect and aggregate over \$100 million in donations annually from various donors and distribute the funds to other charities in accordance with the originating donors' wishes (Strom 2004a; Wallack 2003a, 2003b). Since its founding, the charity's financial reports received unqualified opinions from its auditor. When two former employees (who were fired for questioning the charity's accounting methods) tipped off authorities about potential financial fraud, the ensuing investigation revealed that millions of dollars were misallocated towards officer salaries and other operating expenses rather than being passed on to charities.<sup>1</sup> The charity shut its doors, laid off all of its employees, and terminated all employee benefit plans. In response to this and similar events, the Attorney General of California is sponsoring legislation that would enhance nonprofit financial reporting oversight (i.e., The Nonprofit Integrity Act of 2004). In several other states, Attorneys General are

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<sup>1</sup> In order to hide these funds transfers from the eyes of its auditors, the charity wrote checks to recipient charities and recorded those disbursements in its books making it appear that it was properly conducting its purpose of making payments to downstream charities. However, rather than actually mailing the checks the charity voided them, keeping the funds for itself. One former employee stated that the voided checks "were everywhere, lying on the desk, sitting atop filing cabinets, even scattered on the floor" (Wallack 2003b, pg. 2).

considering similar legislation, some of which would impose certain provisions of the Sarbanes-Oxley act on nonprofit organizations (Strom 2004b, Godfrey 2004).

Prior research shows that effective governance can increase the quality of financial reports in the for-profit setting (see Imhoff 2003 for a review). We analyze the effects of governance on the quality of nonprofit organization financial reporting. Because the financial reporting requirements, objective functions, and governance mechanisms of nonprofits are different from those of for-profit firms, it is not clear which, if any, of the existing nonprofit governing mechanisms affect the quality of nonprofit financial reports. By examining the relationship between the existing governance mechanisms and reporting quality, we hope to provide information that is valuable to nonprofit financial statement users as well as to individuals and regulators seeking to enhance nonprofit reporting quality.

We rely on prior research as well as federal and state regulatory reports to identify several measures of reporting quality that are unique to nonprofit organizations. Our governance measures include both market-based and regulatory-based measures. The results of our analysis are consistent with the interpretation that monitoring and oversight increase the quality of nonprofit financial reports. In general, we find that our measures of market-based governance have a more consistent effect on reporting quality than do our regulatory-based measures.

The paper continues as follows. We begin by describing nonprofit financial reports and the governance mechanisms that apply to those reports. We then discuss reporting quality in general and discuss our specific measures. Next, we present our analysis of the association between governance and reporting quality. The final section concludes the paper.

## **2. Nonprofit Financial Reporting Oversight and Monitoring**

### ***2.1. Nonprofit Financial Reports***

The primary source of publicly available nonprofit financial information is the Internal Revenue Service form 990.<sup>2</sup> The 990 contains typical financial statements including a statement of revenues and expenses and a balance sheet, as well as a substantial amount of other information related to the nonprofit's charitable purpose and activities. IRS regulations determine the form and content of the 990 and provide required accounting rules. In most cases the IRS accounting rules mirror Generally Accepted Accounting Principles, although there are several important differences (see Keating and Frumkin 2003 for a reconciliation of these differences).

All nonprofits with revenues over \$25,000 must file the 990 annually. Congressional reports suggest that the intent of the IRS 990 is to provide the public with the necessary information to evaluate the performance of a nonprofit, and that the IRS 990 is the primary source of publicly available nonprofit financial information (Joint Committee on Taxation 2000). To ensure the wide dissemination of 990 information, the IRS Statistics of Income (SOI) division sponsors the Urban Institute to collect and make freely available 990 data for virtually all nonprofits. This data can be found on the Internet at [www.guidestar.org](http://www.guidestar.org) or can be obtained in computer readable form from the National Center for Charitable Statistics at [www.nccs.urban.org](http://www.nccs.urban.org).

Our dataset includes all available continuous years of 990 data (i.e., 1985 to 2000). The most recent year of our sample (2000) contains 15,669 observations, while the oldest (1985) contains 6,168. Because some readers may not be familiar with this database we include specific item number references to the SOI data where applicable. We augment this publicly available data with a smaller hand collected sample that we obtained directly from the nonprofits. To

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<sup>2</sup> Nonprofits are not required to make their financial statements available to the public.

collect this sample we sent a written request to 1,824 nonprofits. From this request we received approximately 1,100 usable observations for 1996. We use this smaller hand collected sample to construct certain variables that otherwise could not be created using the public use databases. In the following sections we describe our financial reporting governance measures.

## ***2.2. Measures of Nonprofit Financial Reporting Governance***

We examine the effects of oversight and monitoring provided by regulators and by market participants. Regulators at the federal and state level are given statutory authority to exercise control over nonprofit organizations. Market-based governance is provided by lenders and investors. Lenders (and related intermediaries) sometimes have legal authority and are frequently given contractual authority to oversee nonprofits. Nonprofits do not have investors in the traditional sense, although prior research suggests that donors act as investors in that they provide funds in exchange for some measure of non-wealth utility that has been described as “warm glow” (Andreoni, J. 1988, 1990). Some types of donors are given contractual authority to oversee their nonprofit recipients. Below we describe these sources of governance in more detail.

### ***2.2.1 Regulators***

The Internal Revenue Service is the primary federal organization charged with overseeing the financial reporting activities of nonprofit organizations. Unfortunately we cannot identify variations in IRS monitoring and enforcement across nonprofits and therefore do not use a federal level governance measure.

Fortunately there is substantial variation in state-level nonprofit legal regulation and reporting requirements. Our measures of legal and reporting governance is from Desai and Yetman (2004) and includes seven measures of a state’s legal powers over nonprofits and nine

measures of state financial reporting requirements for organizations that solicit contributions in a particular state. Both the legal governance metric (*LEGAL*) and the reporting governance metric (*REPORT*) vary across states but do not vary across nonprofits within a state, nor do they vary across time (because they are based on current laws). Because of this, we restrict all analysis using *LEGAL* and *REPORT* to a single year (i.e., the most recent year of our 990 data, which is 2000).

We recognize that having laws on the books is one matter, while enforcement of those laws is another. In addition to including the specific state level legal and reporting rules discussed above, we also include two measures of state-level enforcement. A recent working paper Fremont-Smith and Kosaras (2003) examines court cases involving charities. The authors collect what they believe to be a comprehensive sample of nonprofit court cases from 1995 to 2002. Each case is classified as either criminal or civil. The most common form of criminal misconduct is the misdirection of charitable assets for personal use. The most common forms of civil misconduct are for the breach of fiduciary duty, which includes fraudulent financial reporting. We define *CRIME (CIVIL)* as the number of criminal (civil) trials in a particular state during the period 1995 to 2002 scaled by the number of charities in that same state at the end of the year 2000. We use the year 2000 as it is the most recent year for which we know the number of charities per state.<sup>3</sup> As with all enforcement metrics, ours is subject to at least two problems. First, the relationship between behavior and enforcement is endogenous. If enforcement were perfect there would be no misbehavior, and thus there would be no enforcement necessary. Second, in most instances enforcement actions are settled prior to actual litigation (our database includes completed trials only). Although we recognize these issues, we choose to include these

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<sup>3</sup> Results are robust to alternative definitions including indicator variables equal to one if there was any enforcement action in a particular state from 1995 to 2002 and zero otherwise.

measures of enforcement alongside our measures of legal and reporting governance to calibrate the joint effects of rules and their related enforcement on nonprofit reporting quality. Readers are encouraged to bear in mind the limitations of these measures.

Another source of nonprofit regulation arises from the use of a Certified Public Accountant (CPA) to prepare the IRS 990. Many nonprofits have outside CPAs prepare their IRS Form 990, while others prepare the forms in-house. IRS Circular 230 governs the duties of external CPAs in preparing IRS forms, and failure to follow those guidelines can result in suspension to practice and possible civil or criminal penalties. Unfortunately we cannot identify the preparer of the 990 using the public sample of 990s (it is intentionally erased from all publicly available forms for privacy reasons). However, the majority of respondents to our request for data did not redact the description of the preparer on the 990s they supplied to us, and thus we are able to create a governance variable based on the use of an outside CPA preparer for approximately 1,100 observations from 1996. We test for the effects of using a big or small outside CPA to prepare the IRS 990 (rather than self-preparing the return), though *BIGCPA* (*SMALLCPA*), which is equal to 1 if the nonprofit's 990 was prepared by a Big-4 CPA firm (non-Big-4 CPA firm) and 0 otherwise.

### ***2.2.2. Lenders and Associated Intermediaries***

Because nonprofits do not have access to traditional capital (stock) markets, debt financing through municipal bonds is one way that nonprofits can acquire large amounts of funds for capital projects. Technically nonprofits do not issue municipal bonds directly, but rather receive the proceeds of bond offerings sponsored by various state and city municipalities. Although the issuance is conducted through under the auspices of a governmental agency, the ultimate liability for the bonds resides with the nonprofit (Wedig et al. 1996).

Issuing municipal bonds subjects nonprofits to intensive financial reporting oversight from several sources. The Securities and Exchange Commission enforces the provisions of the Securities and Exchange Act of 1934 rule 15c2-12, which requires that before issuance the firm must file a “final official statement,” which is a comprehensive set of documents prepared by the issuer containing the terms of the issue and extensive financial and operating disclosures. The SEC also enforces the annual reporting requirements of rule 15c2-12, which mandates that all municipal bond issuers file annual financial and operating reports according to rules promulgated by the Municipal Securities Rulemaking Board, which was established in 1975 by Congress. The Board’s purpose is to develop rules regulating securities firms and banks involved in underwriting, trading, and selling municipal securities and is overseen by the SEC. The Board, which is composed of members from the municipal securities dealer community and the public, sets standards for all municipal securities dealers.

The IRS has four oversight functions with respect to municipal bonds. First, the IRS enforces the provisions of the Internal Revenue Code sections 103 and 149, which determine a bond’s taxability both before issuance and while outstanding. Second, the IRS enforces the provisions of the Tax Equity and Fiscal Responsibility Act of 1982, which require specific public hearings and financial reporting disclosures prior to any offering. Third, the IRS enforces the provisions of Internal Revenue Code 149(a) and Treasury Regulation 5f.103(c), which require that all bond issuances be registered annually with the IRS (so that the IRS can determine the bond’s ongoing qualification as tax exempt and match interest payments to those reported on individuals’ tax returns). Finally, the IRS enforces the provisions of Treasury Regulation 1.149(e)-1, which require the filing of form 8030-G and 8038-T (as applicable for arbitrage



bonds).<sup>4</sup> Failure to comply with any of these four oversight requirements will cause the bonds to become immediately taxable to the holders.

Underwriters provide additional financial reporting oversight by acting as financial intermediaries, essentially purchasing the bond offering and re-issuing it to the investing public retaining any spread as profit. Underwriters perform due diligence procedures (including a financial and risk analysis) to gain some level of assurance that sufficient demand will exist for the offering.

One final source of oversight of nonprofits that issue municipal bonds is provided by bond insurance companies. Over one-half of all municipal bond offerings are insured, and most of those are insured by one of the four largest bond insurance companies.<sup>5</sup> The insurance companies sell policies that guarantee the payment of interest and principal to municipal bond purchasers. Nonprofits purchase insurance to secure a lower interest rate than they otherwise would qualify for.

Because the insurance companies are “on the hook” for interest and principal payments, they engage in extremely thorough and ongoing financial oversight of their nonprofit clients. Prior to entering into a contract, the underwriting department conducts an extensive financial investigation to ensure that the risk of loss is remote. Subsequent to the contract, the insurance companies turn the accounts over to their “surveillance” departments, which follow up with periodic financial investigations until the bond issue is fully retired. The standard insurance contract ensures that the insurer has broad access to all nonprofit books, records, or employees

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<sup>4</sup> Arbitrage bonds are bond proceeds that are invested in taxable (to taxable entities) securities prior to being spent on their intended purposes. The spread between the interest payment on the municipal bond and the interest income on the taxable investment is considered to be an “arbitrage profit” which must be remitted to the government (by filing a form 8038-T) every five years.

<sup>5</sup> We are not able to identify which municipal bond issues are insured using our database. Future research could attempt to partition bond offerings into insured and uninsured.

(e.g., the nonprofit's CEO) with short notice. Failure to meet such requests immediately causes the insurance policy to become null.<sup>6</sup> The intense and ongoing monitoring conducted by insurance companies could provide a strong governance mechanism over the quality of nonprofit financial disclosures.

We include a measure of municipal bond governance, *MUNI*, equal to one if the nonprofit had any municipal bonds outstanding at the end of the year (SOI item # e214) and zero otherwise. We recognize that since not all municipal bond offerings are insured, there may be variation in the level of governance across firms with municipal bonds, therefore causing measurement error in our variable. More specifically, nonprofits with uninsured issues are not monitored by insurance companies (although they are still overseen by the SEC, the Municipal Securities Rulemaking Board, the IRS, and underwriters), whereas the nonprofits with insured municipal bond issues are monitored by the insurance companies (in addition to the SEC, the Municipal Securities Rulemaking Board, the IRS, and underwriters). This measurement error should bias us against finding results, and the reader should consider this potential measurement error when interpreting the results.

We do not use a continuous measure for two reasons. First, the underlying distribution is not truly continuous but rather is left-censored (many nonprofits do not have municipal bond debt). Second, the monitoring activities of the insurers are, to a great extent, independent of the amount of debt outstanding as most municipal bond offerings are sufficiently large so as to represent a significant risk of loss to the insurer (the average amount of municipal bond in our

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<sup>6</sup> The insurance contracts are lengthy, but a typical paragraph states “The organization will permit Ambac Assurance to discuss the affairs, finances, and accounts of the organization or any information Ambac Assurance may reasonably request regarding the security for the bonds with appropriate officers. The organization will permit Ambac to have access to and to make copies of all books and records relating to the bonds at any reasonable time.” We thank Peter Poillon, managing director of external relations for Ambac Financial Group, Inc. for explaining some of the complexities involved in municipal bond insurance underwriting.

sample was \$48 million). This variable varies across firms and years (with a “lumpy” distribution across years), but was not available in the IRS database prior to 1993.

### ***2.2.3. Donors (Public, Feeder, and Governmental)***

Donors can be classified as public, feeder, or governmental. Unlike shareholders in for-profit corporations who have the ability to vote their shares, public (i.e., individual and corporate) donors generally have no specific legal right to influence the behavior of the beneficiary nonprofit. Because donations from individuals and businesses tend to be atomistic, no single donor is able to exercise significant control over the nonprofit via a threat to withhold future donations.<sup>7</sup> However, feeder donors and government grantors are frequently given contractual rights to monitor their recipient charities.

Feeder donors are federated fundraising organizations such as The United Way. Feeders do not engage in charitable activities directly, but act as centralized fundraising organizations that aggregate donations from various sources and redirect those donations to nonprofits. Nonprofits receiving feeder funding must meet a stringent set of financial performance criteria as measured by a “volunteer review process,” which involves a detailed examination of various factors including board governance, strategic planning, delivery of charitable services, fundraising activities, and a thorough financial analysis. The financial analysis includes a “proper use of funds” examination of the proportion of expenses consumed by administrative and fundraising activities. In addition to this initial review, most feeders have an annual financial reporting requirement that must be met until all funds are fully disbursed by the donee nonprofit. Finally, nonprofits that are awarded funding must agree to the conditions outlined in a standard

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<sup>7</sup> Exceptions to these generalities no doubt exist, although if a nonprofit receives a large percentage of its donations from a single donor (or related family of donors) it will be classified as a foundation rather than a public charity. We examine only public charities. Some alternative forms of individual donor governance might include legally binding encumbrances on how the donated funds are to be used. Unfortunately we are not able to identify such encumbrances in our data.

“Memorandum of Understanding,” which include submitting to ongoing monitoring activities by the feeder.

Federal and state government agencies provide support to nonprofits through grants. Prior research finds that these agencies play a governance role to recipient nonprofits (O’Regan and Oster 2002). With respect to financial reporting monitoring, governmental agencies apply a stringent set of criteria when selecting recipients (including requiring a stringent “Yellow Book” audit) and engage in post-grant monitoring. Submission to monitoring is a condition of funding. Specific requirements vary by the type of grant and by the granting agency.

We include measures of feeder donations (SOI item # e022) and governmental grants (SOI item # e023), *DONS* and *GRANTS* respectively, equal to one if the nonprofit received any funding in a given year and zero otherwise. We do not use continuous variables for reasons similar to those for municipal bonds. These variables vary across firms and years. Given the nature of these types of funding their distribution across years is “lumpy”.

#### ***2.2.4. Other Sources of Nonprofit Governance***

We recognize that there are several other plausible sources of governance such as boards of directors, the media, and other nonprofits (see Keating and Frumkin 2003 for a discussion of other possible sources of nonprofit oversight). Although some of these alternative measures no doubt have merit, we were not able to obtain reliable and useable data on them.

### **3. Financial Reporting Quality in the Nonprofit Setting**

Although there is no single definition of financial reporting quality there are nonetheless several agreed-upon aspects of quality. In this paper we employ the “decision usefulness” criteria as discussed in Schipper and Vincent (2003). Congressional reports suggest that the

intent of the form 990 is to provide the public with the necessary information to evaluate the performance of a nonprofit (Joint Committee on Taxation 2000), and the Financial Accounting Standards Board (FASB) espouses a similar intent for the financial statements of both for-profit and nonprofit organizations (Concepts Statement No. 1 and 5, FASB 1978, para. 34 et. Seq.). The standards applied by both of these regulators imply a decision usefulness context to financial reporting for both the IRS 990 and nonprofit financial statements.<sup>8</sup>

Having decided on a decision usefulness concept of reporting quality our next task is to select specific measures of decision usefulness. Our first three measures are unique to the nonprofit setting and were identified by regulating agencies as well as prior research. A study by the Governmental Accounting Office (GAO) on nonprofit organization oversight (United States General Accounting Office 2002) identifies three nonprofit financial reporting issues. First, over one-half of all nonprofits that receive donations report zero fundraising expenses. Second, about 10 percent of nonprofits report zero administrative expenses. Third, many nonprofits fail to properly itemize the amounts of their total revenues, expenses, assets, and liabilities but rather report significant proportions of these amounts in the nondescript category “other”. These three nonprofit financial reporting shortcomings are not unique to the GAO study and have been identified and examined by both prior research (Krishnan et al. 2004, Keating and Frumkin 2003) as well as nongovernmental oversight agencies such as the Urban Institute’s cost studies ([www.coststudy.org](http://www.coststudy.org)).

These three reporting issues can decrease the decision usefulness of nonprofit financial reports because they obfuscate the true nature of nonprofits’ activities. By understating the

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<sup>8</sup> Alternative aspects of financial disclosure quality include how well reported net profits correspond with economic profits (Hicks 1939) or how financial disclosures map into stock prices. Because the nonprofit objective function is generally described as welfare maximization (Hansmann 1980) rather than value or profit maximization and because nonprofits do not have an observable stock price, employing either of these alternative aspects of reporting quality is problematic in the nonprofit setting.

amounts of fundraising and administrative expenses a nonprofit necessarily overstates the amount of its charitable expenses. This causes the nonprofit to appear to be more efficient in delivering its charitable output and in raising its donations, potentially misleading donors, grantmakers, and regulators. Prior research shows that donors, grantmakers, and regulators use the proportion of expenses reported in each of these three functional activities (i.e., fundraising, administrative, and charitable) for monitoring and decision making purposes (Weisbrod and Dominguez 1986; Posnett and Sandler 1989; Baber et al. 2002). Various watchdog agencies (such as the Better Business Bureau) and popular press outlets (such as the Wall Street Journal and Money Magazine) rank nonprofits according to the proportion of total expenses that are directed towards charitable causes and make recommendations to readers based on these figures (Barrett 1999). To the extent a nonprofit underreports its fundraising and administrative expenses or makes excessive use of the nondescript “Other” accounts, the quality of its IRS 990 for decision making purposes is compromised. It is interesting to note that the organization discussed in the introductory anecdote regarding nonprofit financial reporting fraud reported zero administrative expenses, zero fundraising expenses, and 24 percent of its total expenses as “other expenses” on its IRS 990. Our fourth measure of reporting quality is based on discretionary disclosures on the IRS 990. In certain places on the 990 an organization is permitted to describe its charitable accomplishments and we use these descriptions as our final reporting quality metric.

We recognize that, in the for-profit setting, the literature on financial reporting quality is vast (see Schipper and Vincent 2003 for a partial review) and uses a multitude of decision usefulness measures. Common examples include abnormal accruals as measured by the Jones (1991) model or one of its many variants, accrual estimation errors derived from the Dechow and

Dichev (2002) model, and accounting metrics' associations with stock returns. These measures do not naturally apply in the nonprofit setting for several reasons. First, unlike for-profit firms, nonprofits do not have an observable stock price. Second, various reporting incentives related to reporting of net income in the for-profit setting make accrual models fitting, but similar incentives related to net income do not naturally apply in the nonprofit setting. In addition, the accounting rules are not the same as those of for-profit firms. Finally, nonprofits have very different overall objective functions than do for-profit firms. Thus we do not apply any of these traditional measures of decision usefulness in our primary analysis. We do, however, test a few of these alternative quality measures as robustness tests and discuss those results later in the paper. In the following sections we discuss the specifics of our reporting quality variables.

### ***3.1. Zero Reported Administrative and Fundraising Expenses***

On the 990, nonprofits are required to partition their itemized expenses (e.g., “wages” or “supplies”) into three functional activities (i.e., charitable outlays, administrative expenses, and fundraising expenses). A particular itemized expense (e.g., “wages”) can be allocated into one or more of the functional activities. As previously noted many organizations report zero fundraising and/or zero administrative expenses. In general one would plausibly expect that at least some amount of administrative activities are required to operate an organization, and at least some amount of fundraising expenses would be incurred to generate donations. However, there are some plausible explanations as to why any particular organization could truthfully and correctly report zero administrative (SOI item # e049) or fundraising expenses (SOI item # e050). We screen our sample to remove all observations with a plausible reason (according to IRS regulations) for reporting zero administrative or fundraising expenses on the IRS 990.

The instructions to the 990 indicate that administrative expenses are those incurred “for overall function and management” of the organization, including “managerial salaries, accounting and billing activities, liability insurance, personnel, office management, and investment expenses”. Given this broad definition of administrative activities it seems unlikely that any nonprofit could operate with zero actual administrative expenses.<sup>9</sup> However, to be conservative in our measure, we exclude observations with less than \$100,000 of total expenses (SOI item # e052). We also exclude organizations that are simply “auxiliaries” or non-operating organizations.

With respect to fundraising expenses we remove all observations that receive less than \$100,000 of donations. IRS regulations are sufficiently broad such that it would be virtually impossible for observations in this remaining sub-sample to have raised substantial donations with zero fundraising expenses. IRS reporting requirements would dictate that at least some modicum of reportable fundraising would be incurred by all donations receiving nonprofits. The IRS requires nonprofits to provide receipts to donors (so that donors have a record for their tax returns) as well as keep internal records of donors (for purposes of matching with individual income tax returns). Expenses related to providing receipts and keeping donor records is properly recorded as fundraising.

*ADMIN (FUND)* is equal to one if the nonprofit reported some administrative (fundraising) expenses, conditional on our screens, and zero otherwise. Each of these variables varies across organization and time.

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<sup>9</sup> It is important to note that the concept of “materiality” which requires audited financial statements to separately disclose a particular type of expense only when it is “materially large”, does not apply to the 990. IRS regulations require any amount of administrative or fundraising expense to be broken out and shown on the 990.



### **3.2. Use of “Other” as an Account Description**

As previously noted the 990 provides a preparer with itemized account categories (e.g., “wages” or “supplies”), and regulations require organizations to use these categories when applicable. In order to capture the majority of activities the IRS 990 provides many broad account descriptions (there are 18 revenue categories and 22 expense categories). If a particular item of revenue, expense, asset, or liability does not fall into one of the many pre-defined categories the nonprofit should report those items as “other” (other revenues are SOI item # e046, other expenses are SOI item # e149, other assets are SOI item # e176, and other liabilities are SOI item # e184). As noted in the GAO report, despite the fact that the provided categories are quite broad and are intended to capture most activities undertaken by nonprofits, many organizations report significant proportions of their total revenues, expenses, assets, or liabilities as “other”. A consistent reporting scheme through time and across nonprofits enhances the decision usefulness of the 990 and incorrect use of the “other” account obfuscates the nonprofits actual operations. The notion that the use of the “other” account reduces the usefulness of IRS forms is not unique to our analysis. Prior research shows that individuals, corporations, and nonprofits use the “other” line on their income tax returns when they are trying to hide information from the tax authorities (Clotfelter 1983; Yetman 2001).

This measure of financial reporting quality, *OTHER*, is the average of four ratios: other revenues / total revenues, other expenses / total expenses, other assets / total assets, and other liabilities / total liabilities. This measure varies across nonprofits and years.

### **3.3. Voluntary Description of Charitable Accomplishments**

Our fourth measure of nonprofit reporting quality is based on discretionary disclosures. Although there is little discretion with respect to the majority of 990 disclosures, nonprofits are

permitted to describe their charitable accomplishments in any way they see fit on parts III and VIII of the 990. The choice of when and how much voluntary disclosure an organization should theoretically supply has been examined in the for-profit setting (Verrecchia 1983). In general an organization should disclose more information about itself and its accomplishments only if it will enhance its advantage over its competitors without disclosing costly private information. By providing the public with additional information about its charitable operations and accomplishments, a nonprofit is able to communicate non-financial qualities to donors and regulators that might not reveal themselves in financial disclosures.

We presume that increased voluntary disclosure enhances the decision usefulness of an organization's 990, although we recognize that the disclosures could be opportunistic and potentially indicative of lower quality. Because it is difficult to judge the "quality" of a voluntary disclosure related to charitable accomplishments, we add up the number of words used in the description of charitable accomplishments in parts III and VIII (*WORDS*) as a parsimonious measure of disclosure quality. We collected this information from the sample of 990s supplied to us by the nonprofits, and therefore we only have data for 1996.

## **4. Empirical Analysis and Results**

### ***4.1. Descriptive Statistics and Correlation Analyses***

The descriptive statistics for our variables are presented in Table 1. The mean (median) value for state legal governance (*LEGAL*) is 5.9 (6) with a minimum value of 3 and a maximum value of 7. The mean (median) value for state reporting governance (*REPORT*) is 5.6 (6) with a minimum value of 0 (some states have no reporting requirements) and a maximum value of 9. The mean value for our criminal enforcement variable (*CRIME*) is 0.007 while the mean for the

breach of fiduciary duty variable (*CIVIL*) is 0.003. This suggests that criminal actions that are brought to trial occur about twice as often as civil actions that are brought to trial. The mean for *MUNI* is 0.26 indicating that 26 percent of our firm-year observations had municipal bonds outstanding. For those organizations that have municipal debt outstanding the mean (median) amount of that debt is \$48 (\$19) million. The sample size for *MUNI* (i.e., 144,916) is less than the full sample because the IRS did not include the amount of municipal bond debt on the public dataset prior to 1993. The mean values for *DONS* (*GRANTS*) is 0.21 (0.34) indicating that 21 (34) percent of our firm-year observations received feeder donations (government grants). For our smaller hand collected sample of 1,191 observations from the year 1996 we find that 39 percent used a “Big-4” CPA to prepare their 990 while 28 percent used a small CPA firm (the remaining 33 percent did not hire an outside CPA to prepare their 990 but rather prepared the form using their internal employees). Turning to our accounting quality variables we find that 54 percent of nonprofits that receive at least \$100,000 in donations report some amount of fundraising expenses. This proportion is higher than that for the population of nonprofits, suggesting that our screens were at least partially successful in removing observations that had a plausible reason for not reporting any fundraising expenses (United States General Accounting Office 2002). Over 91 percent of our sample reports some administrative expenses, a slightly higher proportion than for the population. On average nonprofits in our sample report 11 percent of their revenues, expenses, assets, and liabilities as “other”. The 75<sup>th</sup> percentile of *OTHER* is 16 percent while the (untabulated) 90<sup>th</sup> percentile is over 25 percent. Finally, nonprofits use an average of 227 words to describe their charitable accomplishments on the 990 although the median value is only 98 and the (untabulated) 90<sup>th</sup> percentile value is 616. The standard deviation of *WORDS* is large (3,581). These statistics (along with the skewness statistic) confirm

that our variable *WORDS* is highly skewed. Because of this we use the log of *WORDS* for empirical analysis setting the value equal to zero if the value of *WORDS* is zero.

Although we do not present the correlations between our governance variables, we note that although many of the measures are statistically significantly positively correlated, the only correlations that were above 20 percent are between the state governance variables (i.e., between *LEGAL*, *REPORT*, *CRIME*, and *CIVIL*) in which case the correlations were in the 30 to 35 percent range. In Table 2 we present the correlations between our governance measures and our reporting quality measures, as well as organization size. In most cases the correlations are in line with our hypothesis that reporting quality is increasing in governance. None of the governance variables have a large correlation with firm size (the highest correlation is four percent between *BIGCPA* and firm size) suggesting that the governance variables are not simply proxies for firm size or vice versa.

#### **4.2. General Model Specification**

Although the correlations suggest a relationship between governance and reporting quality a multivariate setting is required in order to control for omitted correlated variables. The general form of our multivariate analysis is:

$$\text{Reporting Quality}_i = \alpha + \beta_1 \text{Governance}_i + \text{Control Variables}_i \Phi + \varepsilon_i \quad (1)$$

We estimate logit models when our reporting quality variables are dichonomous (*ADMIN* and *FUND*) and OLS models when our reporting quality variables are continuous (*OTHER* and *WORDS*).  $\Phi$  is a vector of coefficients on the control variables, which are total assets (SOI item # e178), total revenues (SOI item # e047), and total donations (SOI item # e024). We also

include single digit industrial classifications (known as National Taxonomy of Exempt Entities) as created by the IRS in all models. There are 26 single digit industries in the IRS's National Taxonomy of Exempt Entities. In all analyses we screen for and omit influential observations using Cooks D, Studentized Residual, and/or leverage statistics (Belsley, Kuh, and Welsch 1980). All regression variables are winsorized at the first and 99<sup>th</sup> percentiles prior to entering our regression models.

Although we could employ panel data techniques for some combinations of governance and reporting quality we do not do so because of concerns over intertemporal correlations. Some of our governance variables do not change at all across years (*LEGAL*, *REPORT*, *CRIME*, and *CIVIL*), while others frequently have a single discrete change during our sample period (*MUNI*, *DONS*, and *GRANTS*).<sup>10</sup>

#### ***4.3. Zero Reported Administrative Expenses***

Table 3 contains the regression results for our reporting quality variable *ADMIN*. As previously discussed we use a single year of analysis for the state-level governance variables (i.e., *LEGAL*, *REPORT*, *CRIME*, and *CIVIL*) because they do not vary across years. We present results using the most recent year of *ADMIN* data (2000) although results are generally robust to all other years (i.e., 1985 to 1999) as well.<sup>11</sup> Results show that the coefficient estimate for *ADMIN* is positive and significant for the state governance variables *REPORT* and *CIVIL*, but not for *LEGAL* or *CRIME*. This result suggests that financial reporting requirements at the state level are associated with higher quality financial reporting, but state level laws regulating overall

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<sup>10</sup> We did estimate our models using panel data methods employing clustering techniques. Those results are consistent with those presented in the paper.

<sup>11</sup> We recognize that the *LEGAL* governance variable was constructed using 2003 data whereas our reporting quality variables are only available starting in the year 2000. To gain some comfort that state level legal enforcement and reporting rules did not materially changed between 2000 and 2003 we spoke with several people at various state nonprofit regulating authorities who told us that the laws have not significantly changed during that period.

behavior do not appear to affect reporting quality. With respect to our enforcement variables we do not find an association between states with more relative occurrences of criminal trials and reporting quality, but we do find higher reporting quality in states with more relative occurrences of civil trials. Because financial reporting matters are almost always civil rather than criminal in nature, this particular finding is reasonable.

For our governance variables *DONS* and *GRANTS* we have sixteen years of pooled data (i.e., from 1985 to 2000) available for analysis while for *MUNI* we have eight years of data (the IRS database did not collect municipal bond data at the organization level until 1993). For these three governance variables for which we have multiple years of cross sectional data we estimate separate annual regressions (rather than pooled regressions) and calculate t-statistics based on the distribution of the annual coefficients.<sup>12</sup> Using the summaries of the annual regressions we find that nonprofit reporting quality is increasing in governance measured as *MUNI*, *DONS*, and *GRANTS*. In the annual regressions, the coefficient estimate is significant in every year of the annual regressions for *MUNI* and *DONS*, and is significant in all but one year for *GRANTS*, providing some comfort that the results are stable across time.

In addition to the annual regressions we also present the results of regressions that use the organization-specific mean values (i.e., averaged across time) of the regression variables. Results using the mean values for those governance variables that are available over a period of time (i.e., *MUNI*, *DONS*, and *GRANTS*) are consistent with those of the annual regressions, again suggesting that the results are stable across time and that no single year is unduly influencing the results.

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<sup>12</sup> The corresponding *t*-statistic is calculated as follows: to calculate whether  $\overline{\hat{\gamma}}_j > 0$  we calculate the *t*-statistic as:

$$t(\overline{\hat{\gamma}}_j) = \frac{\overline{\hat{\gamma}}_j}{s(\hat{\gamma}_j)/\sqrt{n-1}}$$
, where  $\overline{\hat{\gamma}}_j$  is the mean coefficient over the years,  $s(\hat{\gamma}_j)$  is the standard deviation of the yearly estimates, and  $n$  is the number of years (Fama and MacBeth 1973).

To test for the incremental effects of our governance variables relative to one another we estimate an additional model that includes multiple governance variables. The combined analysis is performed using the year 2000 data only so that we can include our state level governance metrics. Results of the combined models in table 3 show that *REPORT*, *MUNI*, *DONS*, and *GRANTS* are each independently associated with a higher probability of reporting some administrative expenses at the five percent level, suggesting that these governance measures have independent effects. Although *CIVIL* was statistically associated with reporting quality at the five percent level in the separate state governance model, it is significant only at the ten percent level when included in the combined governance model.

We also estimate a mean regression using the governance variables *MUNI*, *DONS*, or *GRANTS* leaving out the state level governance measures because we cannot calculate a mean value of the state measures as they are available for only a single year. Inferences of the combined mean regression are identical to those from the combined annual regressions.

With respect to our CPA governance variables we are restricted to a single year of analysis because this data was hand collected for 1996 only. We do not find that using a paid CPA to prepare the IRS 990 has any effect on the probability of reporting administrative expenses.

To summarize our tests where reporting quality is defined as reporting at least some amount of administrative expenses, our results suggest that market-based governance is consistently associated with higher quality reporting. Results for regulatory-based governance are mixed. Although state level financial reporting requirements appear to increase reporting quality, none of the other state governance measures appear to have any influence. Oversight provided by CPAs appears to not have any effect on nonprofit reporting quality measured as *ADMIN*.

#### ***4.4. Zero Reported Fundraising Expenses***

Table 4 contains the regression results for our reporting quality variable *FUND*. Consistent with the analysis above for *ADMIN*, we use a single year of analysis for *LEGAL*, *REPORT*, *CRIME*, and *CIVIL* (i.e., 2000), as well as for the CPA governance variables (i.e., 1996). For *DONS*, *GRANTS*, and *MUNI* we estimate separate annual regressions as well as regressions using the organization-specific mean values.

Results in table 4 show that the coefficient estimate for *FUND* is positive and statistically significant at the five percent level for the models where governance is defined as *REPORT* and *CIVIL* and is not significantly significant for the models where governance is defined as *LEGAL* or *CRIME*. This is consistent with state level reporting requirements and civil enforcement positively affecting on reporting quality, but overall legal requirements and criminal enforcement not having a significant affect on reporting quality. With respect to the separate regressions for *MUNI*, *DONS*, and *GRANTS*, each of those models find that the probability of reporting some fundraising expenses is increasing in higher levels of governance. Results using the mean values of *MUNI*, *DONS*, and *GRANTS* are consistent with those for the annual regressions.

Results for the model that combines the governance variables show that *REPORT*, *CIVIL*, *MUNI*, *DONS*, and *GRANTS* are each associated with a higher probability of reporting some administrative expenses, suggesting that these governance measures have independent effects.

Results in table 4 show that the use of a CPA (large or small firm) is associated with a lower probability of reporting fundraising expenses. This finding is inconsistent with our hypothesis and suggests that using an outside CPA firm to prepare the 990 leads to lower reporting quality.

To summarize our tests where reporting quality is defined as reporting at least some amount of fundraising expenses, our results suggest that market-based governance is again consistently



associated with higher quality reporting, while the results for regulatory-based governance are again mixed. Although state level financial reporting requirements and civil enforcement appear to increase reporting quality, neither state laws nor criminal enforcement appear to have any influence. Oversight provided by CPAs appears to reduce, rather than enhance, nonprofit reporting quality measured as *FUND*.

#### **4.5. Use of the “Other” account**

Table 5 contains the regression results for our reporting quality variable *OTHER*. Consistent with the analysis above, we use the year 2000 for the state level governance variables and 1996 for the CPA governance variables. For *DONS*, *GRANTS*, and *MUNI* we estimate separate annual regressions as well as regressions using the organization-specific mean values.

Results of the regressions in table 5 show that the coefficient estimate for *OTHER* is positive and significant at the five percent level for the models where governance is separately defined as *MUNI*, *DONS*, and *GRANTS*, but not where governance is defined as *LEGAL*, *REPORT*, *CRIME*, or *CIVIL*. Results of the mean values of the variables are consistent with those of the annual regressions.

Results of the combined models show that *MUNI*, *DONS*, and *GRANTS* are each associated with reporting fewer items as “other,” while none of the state-level governance measures are similarly associated with reporting quality. We do not find that using a paid CPA to prepare the IRS 990 has any effect on the amount of items reported as “other”.

To summarize our tests where reporting quality is defined as reporting as not excessively using the “other” accounts, our results suggest that market-based governance is effective in reducing use of the “other” account but regulatory-based governance appears to be less effective or perhaps ineffective.

#### ***4.6. Number of Words used to Describe the Charitable Accomplishment***

Table 6 contains the regression results for our reporting quality variable *WORDS*. Because we have only a single year of data for *WORDS* (i.e., 1996) we present the results of a single annual cross sectional regressions only. Results in table 6 show that the coefficient estimate for the natural log of *WORDS* is statistically positively significant for the models where state level regulatory governance is defined *REPORT*, but not where governance is defined as *LEGAL*, *CRIME*, or *CIVIL*. We find that market-based governance measured as *MUNI*, *DONS*, and *GRANTS*, is associated with using more words to describe the charitable accomplishment. When the governance variables are combined into a single regression the results are similar except that *GRANTS* loses its statistical significance.

We find that using a large or small CPA firm to prepare the IRS 990 is associated with fewer words used to describe the nonprofits' charitable accomplishments. This finding is contrary to our hypothesis, but similar to the results we obtained with reporting quality measured as zero reported fundraising expenses. An F-test shows that the coefficients on *BIGCPA* and *SMALLCPA* are different, suggesting that using a small CPA firm to prepare the 990 results in even fewer words being used to describe the charitable accomplishment than does the use of a large CPA firm.

To summarize our tests where reporting quality is defined as the natural log of the number of words used to describe the organization's charitable accomplishments, our results suggest that market-based governance is again consistently associated with higher quality reporting while the results for regulatory-based governance are again mixed. Although state level financial reporting requirements appear to increase reporting quality, neither state laws nor criminal or civil

enforcement appear to have any influence. Oversight provided by CPAs appears to reduce, rather than enhance, nonprofit reporting quality measured as *WORDS*.

Overall we believe our cross sectional results provide support for the notion that both market-based and regulatory-based governance has a positive effect on nonprofit financial reporting quality, but that the market-based metrics have a more consistent effect on reporting quality.

#### ***4.7 Event Analyses***

Because we have time-series data for some of our measures, we can examine the effects of changes in reporting quality across changes in some of our governance variables. This type of test can provide stronger evidence of an association between governance and reporting quality than can a cross-sectional analysis as each firm can act as its own quality control. An event analysis can also mitigate concerns over endogeneity. Specifically, our cross-sectional results are consistent with two interpretations. First (and consistent with our hypothesis), enhanced governance gives rise to enhanced reporting quality. Second, nonprofits with historically higher quality financial reports are more able to qualify for municipal bonds, feeder donations, or government grants. The event analyses can partially address this endogeneity.

To conduct our event analysis we first restrict the sample to those observations that experienced a change in the particular governance variable under examination during our sample period (i.e., they issued municipal bonds, started receiving feeder donations, started receiving government grants, or some combination thereof). We then line up the observations in event time (where  $t_0$  represents the year of the event) and use this sample to estimate the following model:

$$\text{Reporting Quality} = \beta_1 t_{.3} + \beta_2 t_{.2} + \beta_3 t_{.1} + \beta_4 t_0 + \beta_5 t_1 + \Phi \text{ Controls} + \varepsilon. \quad (2)$$

Reporting quality is either *ADMIN*, *FUND*, or *OTHER*, which are the reporting quality variables for which we have time series data. We do not examine the reporting quality variable *WORDS* nor do we examine the state level or CPA governance variables because we only have a single year of data for them. Because *ADMIN* and *FUND* are dichotomous, their respective models using equation (2) are estimated using a logistic function. The models with the quality variable equal to *OTHER* are estimated using ordinary least squares because *OTHER* is a continuous metric. The variables  $t_{.3}$  through  $t_1$  are indicator variables that represent the time period of the observations relative to the change in governance (i.e.,  $t_{.3}$  is equal to one if the observation is from three years prior to the event period of a change in governance and zero otherwise, etc.). Although some nonprofits in our sample had more than one event during our sample period (i.e., they began to receive government grants, then receive no grants for several years, then begin receiving grants again), we examine the first event in our sample period only.<sup>13</sup> We include observations that had different events occur during the sample period (i.e., they issued municipal bonds and started receiving donations or grants) because the effects of these governance changes are included in separate regressions. The control variables include year and industry indicator variables, total revenues, total assets, and total donations.

To test for the effects of the governance event on reporting quality, we conduct F-tests for differences in coefficient estimates at various times around the event period at  $t_0$ . If the event of a change in governance causes a change in reporting quality we would expect to see a change in

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<sup>13</sup> Results are not sensitive to removing these “multiple event” observations from the sample. We attempted to exploit the “multiple event” observations by testing if accounting quality changed back and forth. Because the sample sizes were very small and the time between events was frequently short (often only one year) results of this alternative analysis were not stable.

quality in periods across the event, but not across periods prior to or after the event. Based on this, we hypothesize that the reporting quality variables will not be different across the periods  $t_{-3}$  to  $t_{-2}$  or across the periods  $t_0$  to  $t_1$ , but that they will be different across the periods  $t_{-2}$  to  $t_0$ . We do not test for differences across the periods  $t_{-1}$  to  $t_0$  because the event actually occurs at some point between the time the financial statements are prepared for the periods  $t_{-1}$  and  $t_0$  and the firm may have increased the quality of the financial statement at period  $t_{-1}$  in anticipation of issuing bonds or soliciting feeder donations or government grants.

Results of our event analyses are presented in Table 7. The results of the regression analyses, as well as the F-tests are shown, along with associated  $p$ -values. In all cases, the F-tests show that reporting quality did not change in the periods before (i.e., no significant difference between  $\beta_1$  and  $\beta_2$ ) or after (i.e., no significant difference between  $\beta_4$  and  $\beta_5$ ) a change in governance. However, financial reporting quality did increase across all increases in governance (i.e.,  $\beta_4$  is significantly greater than  $\beta_2$ ), although the change for *FUND* across changes in municipal bond issuances and the receipt of feeder donations are only significant at the 8 percent level. We believe that these results provide particularly strong evidence that nonprofit financial reporting quality is improved by enhanced governance.

#### ***4.8 Summary and Discussion of Results***

Our results are consistent with the hypothesis that increased oversight and monitoring is associated with higher quality financial reporting quality in the nonprofit setting. This in turn suggests that better governance can lead to more efficient resource allocation and regulatory decisions by various nonprofit stakeholders. Our results suggest that pending legislative actions with respect to nonprofit financial reporting governance could increase the quality of nonprofit financial reports. Of particular note is our finding that market-based oversight from donors and

lenders (and related intermediaries) appears to have a more consistent effect on nonprofit reporting quality than does regulatory-based governance measures. This finding suggests that efforts to increase nonprofit reporting quality through regulatory oversight alone will not necessarily produce the intended magnitude of results.

Our results suggest that the governance arising from the receipt of government grants increases the percentage of firms reporting administrative expenses by five percent (see table 3 mean OLS regression). Although this may seem like a relatively small change, our descriptive statistics show that over 90 percent of all organizations report some administrative expenses, so an increase of five percent is relatively large in terms of the residual 10 percent. As another example of the economic significance of our results, we find that the governance arising from the receipt of government grants increases the percentage of firms reporting fundraising expenses by approximately 14 percent (see table 4 mean OLS regression). This figure compares to our sample average where just over 50 percent of organizations reports some fundraising expenses.

#### ***4.9 Alternative Measures of Reporting Quality***

We calibrate the effects of governance on two commonly used measures of earnings quality including discretionary accruals (Jones 1991, Dechow et al. 1995) and accrual estimation errors (Dechow and Dichev 2002). Both of these methods estimate firm-specific deviations from a “normal” or “correct” amounts of accruals. Accruals arise when an organization records a revenue or expense on its books prior to (or sometimes after) the related cash flow occurs. We fail to find any statistically significant associations between these two quality metrics and our governance measures. One plausible reason is that the time series quality metrics presume specific relationships between the accruals process (and permitted discretion in that process) and eventual cash flow realizations. None of these relationships are well defined by prior research

and it is very possible that these models, which were developed for use in the for-profit setting embodying for-profit objective functions, do not apply very well in the nonprofit setting.

## **5. Conclusion**

Financial reports are an important source of information for stakeholders who use them for investing, contracting, and regulating decisions. Low quality reporting can lead to suboptimal decisions and potential misallocation of resources. In this paper we examine the effects of governance on nonprofit organization financial reporting quality and find that in general, nonprofit financial reporting quality is increasing in various forms of oversight and monitoring. We find that market-based governance measures have a more consistent effect on reporting quality than do regulatory-based governance measures. Our findings are not only important for various stakeholders who use nonprofit financial information, but also informs recent legislative debate about the quality of nonprofit financial disclosures and what measures should be taken to improve their quality.

Because the IRS 990 is the primary source of financial information for nonprofits and this form is not subject to routine analysis by independent parties (such as audits by CPAs) it is not well known how useful they are for any particular purpose. Our study finds that, in the absence of routine analysis by some form of regulator, various contracting parties (i.e., lenders, donors, and grant makers) can impose monitoring and oversight of nonprofits' financial reports. Our study represents a preliminary analysis of these important issues. What remains an unanswered question is, even in the presence of existing monitoring, how useful are nonprofit financial reports for investing, contracting, and regulating purposes? Future research addressing this issue would be valuable.

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**Table 1**  
**Descriptive Statistics**

| Variable                     | Varies by | Number of Firm/Year Observations | Mean       | Standard Deviation | 25 <sup>th</sup> Percentile | Median     | 75 <sup>th</sup> Percentile |
|------------------------------|-----------|----------------------------------|------------|--------------------|-----------------------------|------------|-----------------------------|
| <b>Corporate Governance:</b> |           |                                  |            |                    |                             |            |                             |
| <i>LEGAL</i>                 | State     | 15,557                           | 5.93       | 1.27               | 5                           | 6          | 7                           |
| <i>REPORT</i>                | State     | 15,557                           | 5.61       | 2.52               | 5                           | 6          | 7                           |
| <i>CRIME</i>                 | State     | 15,557                           | .007       | .005               | .002                        | .005       | .009                        |
| <i>CIVIL</i>                 | State     | 15,557                           | .003       | .003               | 0                           | .003       | .006                        |
| <i>MUNI</i>                  | Firm/year | 144,916                          | 0.260      | 0.438              | 0                           | 0          | 1                           |
| <i>DONS</i>                  | Firm/year | 176,081                          | 0.215      | 0.410              | 0                           | 0          | 0                           |
| <i>GRANTS</i>                | Firm/year | 176,078                          | 0.335      | 0.472              | 0                           | 0          | 1                           |
| <i>BIGCPA</i>                | Firm      | 1,191                            | 0.385      | 0.487              | 0                           | 0          | 1                           |
| <i>SMALLCPA</i>              | Firm      | 1,191                            | 0.275      | 0.446              | 0                           | 0          | 1                           |
| <b>Accounting Quality:</b>   |           |                                  |            |                    |                             |            |                             |
| <i>ADMIN</i>                 | Firm/year | 165,977                          | 0.911      | 0.284              | 1                           | 1          | 1                           |
| <i>FUND</i>                  | Firm/year | 115,761                          | 0.540      | 0.498              | 0                           | 1          | 1                           |
| <i>OTHER</i>                 | Firm/year | 176,101                          | 0.113      | 0.097              | 0.042                       | 0.082      | 0.161                       |
| <i>WORDS</i>                 | Firm      | 636                              | 227        | 3,581              | 55                          | 98         | 205                         |
| <b>Controls:</b>             |           |                                  |            |                    |                             |            |                             |
| <i>ASSETS</i>                | Firm/year | 176,101                          | 72,194,090 | 802,847,190        | 4,899,353                   | 16,574,425 | 48,634,104                  |
| <i>REVENUES</i>              | Firm/year | 176,101                          | 37,825,277 | 206,805,024        | 1,612,108                   | 7,496,233  | 26,637,665                  |
| <i>DONATIONS</i>             | Firm/year | 176,082                          | 5,086,181  | 27,682,614         | 26,592                      | 416,714    | 2,543,910                   |

Notes: With the exception of *LEGAL*, *REPORT*, *CRIME*, and *CIVIL*, all variables are collected from the IRS Form 990. *LEGAL* and *REPORT* are composites of the state level governance measures as discussed Desai and Yetman (2004) and *CRIME* and *CIVIL* are the number of criminal or civil cases brought against nonprofit organizations in the period 1995 to 2002 by a given state scaled by the number of charities in a state. *MUNI* is an indicator variable equal to 1 if the nonprofit has any municipal bonds outstanding at the end of the year, and 0 otherwise. *DONS* (*GRANTS*) is equal to 1 if the nonprofit received any feeder donations (government grants) during the year, and 0 otherwise. *BIGCPA* (*SMALLCPA*) is equal to 1 if the nonprofit's 990 was prepared by a Big-4 CPA firm (non-Big-4 CPA firm) and 0 otherwise. *ADMIN* (*FUND*) is an indicator variable equal to 1 if the nonprofit reported general and administrative (fundraising) expenses, and 0 otherwise. *OTHER* is equal to the average of ratios of other revenues, expenses, assets, and liabilities to their relative total amounts. *WORDS* is the number of words reported in the "Statement of Program Service Accomplishments" in Parts III and VIII. *ASSETS*, *REVENUES*, AND *DONATIONS* are total assets, revenues, and donations. All variables are winsorized at the 1% and 99% levels.

**Table 2**  
**Pearson Correlation Statistics**

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|                 | <i>ADMIN</i>      | <i>FUND</i>       | <i>OTHER</i>       | <i>WORDS</i>       | <i>SIZE</i>       |
|-----------------|-------------------|-------------------|--------------------|--------------------|-------------------|
| <i>LEGAL</i>    | 0.02<br>(<.0001)  | .039<br>(<.0001)  | .001<br>(.876)     | -.022<br>(0.347)   | 0.012<br>(<.0001) |
| <i>REPORT</i>   | .0167<br>(<.0001) | .0126<br>(<.0001) | -.008<br>(.0005)   | -.017<br>(.474)    | 0.001<br>(0.637)  |
| <i>CRIME</i>    | .017<br>(<.0001)  | .011<br>(<.0001)  | -.002<br>(.427)    | .008<br>(.744)     | 0.009<br>(0.000)  |
| <i>CIVIL</i>    | .033<br>(<.0001)  | .064<br>(<.0001)  | .009<br>(<.0001)   | .009<br>(.717)     | 0.014<br>(<.0001) |
| <i>MUNI</i>     | 0.022<br>(<.0001) | 0.023<br>(<.0001) | -0.068<br>(<.0001) | 0.138<br>(<.0001)  | 0.024<br>(<.0001) |
| <i>DONS</i>     | 0.070<br>(<.0001) | 0.091<br>(<.0001) | -0.069<br>(<.0001) | 0.144<br>(<.0001)  | 0.013<br>(<.0001) |
| <i>GRANTS</i>   | 0.095<br>(<.0001) | 0.229<br>(<.0001) | -0.102<br>(<.0001) | -0.001<br>(0.9602) | 0.016<br>(<.0001) |
| <i>BIGCPA</i>   | 0.022<br>(<.0001) | 0.028<br>(<.0001) | 0.018<br>(<.0001)  | 0.079<br>(<.0001)  | 0.041<br>(<.0001) |
| <i>SMALLCPA</i> | 0.021<br>(<.0001) | 0.031<br>(<.0001) | 0.011<br>(<.0001)  | -.175<br>(<.0001)  | -0.001<br>(0.777) |

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Notes: Variable definitions are in Table 1. p-values are presented below the Pearson correlations.

**Table 3**  
**The Effects of Governance on Zero Reported Administrative Expenses<sup>1</sup>**

| Sample Period:                                 | Annual LOGIT Regressions <sup>2</sup> |                        |                        |                        |                   | Mean OLS Regressions <sup>3</sup> |                   |                   |                   |                   |
|--|---------------------------------------|------------------------|------------------------|------------------------|-------------------|-----------------------------------|-------------------|-------------------|-------------------|-------------------|
|  | 2000                                  | 1993-2000 <sup>2</sup> | 1985-2000 <sup>2</sup> | 1985-2000 <sup>2</sup> | 1996              | 2000                              | 1993-2000         | 1985-2000         | 1985-2000         | 1993-2000         |
| Constant                                       | 2.153<br>(<0.001)                     | 2.555<br>(<0.001)      | 2.251<br>(<0.001)      | 2.180<br>(<0.001)      | 1.928<br>(0.031)  | 1.823<br>(<0.001)                 | 0.909<br>(<0.001) | 0.897<br>(<0.001) | 0.895<br>(<0.001) | 0.886<br>(<0.001) |
| <i>LEGAL</i>                                   | 0.048<br>(0.360)                      |                        |                        |                        |                   | 1.651<br>(0.214)                  |                   |                   |                   |                   |
| <i>REPORT</i>                                  | 0.054<br>(0.023)                      |                        |                        |                        |                   | 0.065<br>(0.035)                  |                   |                   |                   |                   |
| <i>CRIME</i>                                   | 4.158<br>(0.602)                      |                        |                        |                        |                   | 0.049<br>(0.458)                  |                   |                   |                   |                   |
| <i>CIVIL</i>                                   | 35.606<br>(0.081)                     |                        |                        |                        |                   | 0.969<br>(0.091)                  |                   |                   |                   |                   |
| <i>MUNT</i> <sup>4</sup>                       |                                       | 0.750<br>(<0.001)      |                        |                        |                   | 0.947<br>(<0.001)                 | 0.030<br>(<0.001) |                   |                   | 0.026<br>(<0.001) |
| <i>DONS</i> <sup>4</sup>                       |                                       |                        | 0.755<br>(<0.001)      |                        |                   | 0.662<br>(<0.001)                 | 0.056<br>(<0.001) |                   |                   | 0.045<br>(<0.001) |
| <i>GRANTS</i> <sup>4</sup>                     |                                       |                        |                        | 0.667<br>(<0.001)      |                   | 0.723<br>(<0.001)                 |                   | 0.052<br>(<0.001) |                   | 0.043<br>(<0.001) |
| <i>BIGCPA</i> <sup>4</sup>                     |                                       |                        |                        |                        | -0.006<br>(0.992) |                                   |                   |                   |                   |                   |
| <i>SMALLCPA</i> <sup>4</sup>                   |                                       |                        |                        |                        | 0.343<br>(0.617)  |                                   |                   |                   |                   |                   |
| % sig. annual regressions at 0.05 <sup>2</sup> |                                       | 100%                   | 100%                   | 94%                    |                   |                                   |                   |                   |                   |                   |
| Observations                                   | 8,746                                 | 56,314                 | 94,419                 | 94,421                 | 788               | 8,740                             | 19,770            | 19,771            | 19,771            | 19,771            |
| R <sup>2</sup>                                 | 0.01                                  | 0.02                   | 0.03                   | 0.03                   | 0.03              | 0.02                              | 0.03              | 0.03              | 0.03              | 0.04              |

Notes:

1 – Coefficient estimates for control variables and industry dummies are not reported. *P*-values are in parentheses under their respective coefficient estimates. The reporting quality measure is *ADMIN*, which is equal to 1 if the nonprofit reported any amount of administrative expenses and zero otherwise. Variables are winsorized at 1%, and in all analyses we screen for and omit influential observations using Cooks D, Studentized Residual, and leverage statistics (Belsley, Kuh, and Welsch 1980).

2 – In the “annual regressions” with more than one year in the sample period, the annual coefficient estimates and R<sup>2</sup> statistics are the averages of the separate annual regressions. Annual t-statistics are based on the distribution of the annual coefficient estimates (Fama-McBeth 1973). Also reported is the percentage of the separate annual regressions that had statistically significant (at the five percent level) coefficients for the governance variable.

3 – In the “mean regressions,” we use the mean value of the all regression variables for each firm across the sample period.

4 – See Table 1 for the definition of the governance measures

**Table 4**  
**The Effects of Governance on Zero Reported Fundraising Expenses<sup>1</sup>**

| Sample Period:                                 | Annual LOGIT Regressions <sup>2</sup> |                        |                        |                        |                   | Mean OLS Regressions <sup>3</sup> |                   |                   |                   |                   |
|--|---------------------------------------|------------------------|------------------------|------------------------|-------------------|-----------------------------------|-------------------|-------------------|-------------------|-------------------|
|  | 2000                                  | 1993-2000 <sup>2</sup> | 1985-2000 <sup>2</sup> | 1985-2000 <sup>2</sup> | 1996              | 2000                              | 1993-2000         | 1985-2000         | 1985-2000         | 1993-2000         |
| Constant                                       | -0.057<br>(0.629)                     | -0.052<br>(0.535)      | -0.240<br>(<0.001)     | -0.313<br>(<0.001)     | 0.799<br>(0.104)  | -0.292<br>(0.015)                 | 0.603<br>(<0.001) | 0.563<br>(<0.001) | 0.561<br>(<0.001) | 0.535<br>(<0.001) |
| <i>LEGAL</i>                                   | -0.000<br>(0.999)                     |                        |                        |                        |                   | 0.007<br>(0.745)                  |                   |                   |                   |                   |
| <i>REPORT</i>                                  | 0.031<br>(0.003)                      |                        |                        |                        |                   | 0.029<br>(0.006)                  |                   |                   |                   |                   |
| <i>CRIME</i>                                   | 1.722<br>(0.607)                      |                        |                        |                        |                   | 2.467<br>(0.465)                  |                   |                   |                   |                   |
| <i>CIVIL</i>                                   | 35.210<br>(0.001)                     |                        |                        |                        |                   | 34.278<br>(0.001)                 |                   |                   |                   |                   |
| <i>MUNT</i> <sup>4</sup>                       |                                       | 0.263<br>(<0.001)      |                        |                        |                   | 0.198<br>(0.004)                  | 0.052<br>(<0.001) |                   |                   | 0.032<br>(0.014)  |
| <i>DONS</i> <sup>4</sup>                       |                                       |                        | 0.533<br>(<0.001)      |                        |                   | 0.421<br>(<0.001)                 |                   | 0.147<br>(<0.001) |                   | 0.114<br>(<0.001) |
| <i>GRANTS</i> <sup>4</sup>                     |                                       |                        |                        | 0.552<br>(<0.001)      |                   | 0.413<br>(<0.001)                 |                   |                   | 0.144<br>(<0.001) | 0.119<br>(<0.001) |
| <i>BIGCPA</i> <sup>4</sup>                     |                                       |                        |                        |                        | -0.613<br>(0.012) |                                   |                   |                   |                   |                   |
| <i>SMALLCPA</i> <sup>4</sup>                   |                                       |                        |                        |                        | -0.759<br>(0.004) |                                   |                   |                   |                   |                   |
| % sig. annual regressions at 0.05 <sup>2</sup> |                                       | 100%                   | 100%                   | 100%                   |                   |                                   |                   |                   |                   |                   |
| Observations                                   | 8,747                                 | 56,319                 | 94,422                 | 94,424                 | 788               | 8,741                             | 11,966            | 11,966            | 11,966            | 11,966            |
| R <sup>2</sup>                                 | 0.10                                  | 0.12                   | 0.13                   | 0.14                   | 0.31              | 0.12                              | 0.11              | 0.12              | 0.13              | 0.14              |

Notes:

1 – Coefficient estimates for control variables and industry dummies are not reported. *P*-values are in parentheses under their respective coefficient estimates. The reporting quality measure is *FUND*, which is equal to 1 if the nonprofit reported any amount of fundraising expenses and zero otherwise. The analysis sample is restricted to organizations that received over \$100,000 in donations. Variables are winsorized at 1%, and in all analyses we screen for and omit influential observations using Cooks D, Studentized Residual, and leverage statistics (Belsley, Kuh, and Welsch 1980).

2 – In the “annual regressions” with more than one year in the sample period, the annual coefficient estimates and R<sup>2</sup> statistics are the averages of the separate annual regressions. Annual t-statistics are based on the distribution of the annual coefficient estimates (Fama-McBeth 1973). Also reported is the percentage of the separate annual regressions that had significant (at the five percent level) coefficients for the governance variable.

3 – In the “mean regressions,” we use the mean value of the all regression variables for each firm across the sample period.

4 – See Table 1 for the definition of the governance measures

**Table 5**  
**The Effects of Governance on Use of “Other” as an Account Description<sup>1</sup>**

| Sample Period:                                 | Annual OLS Regressions <sup>2</sup> |                        |                        |                        |                   | Mean OLS Regressions <sup>3</sup> |                    |                    |                    |                   |
|--|-------------------------------------|------------------------|------------------------|------------------------|-------------------|-----------------------------------|--------------------|--------------------|--------------------|-------------------|
|  | 2000                                | 1993-2000 <sup>2</sup> | 1985-2000 <sup>2</sup> | 1985-2000 <sup>2</sup> | 1996              | 2000                              | 1993-2000          | 1985-2000          | 1985-2000          | 1993-2000         |
| Constant                                       | 0.109<br>(<0.001)                   | 0.097<br>(<0.001)      | 0.111<br>(<0.001)      | 0.113<br>(<0.001)      | 0.121<br>(<0.001) | 0.114<br>(<0.001)                 | 0.115<br>(<0.001)  | 0.118<br>(<0.001)  | 0.120<br>(<0.001)  | 0.122<br>(<0.001) |
| <i>LEGAL</i>                                   | -0.000<br>(0.473)                   |                        |                        |                        |                   | -0.000<br>(0.383)                 |                    |                    |                    |                   |
| <i>REPORT</i>                                  | -0.00<br>(0.342)                    |                        |                        |                        |                   | 0.000<br>(0.943)                  |                    |                    |                    |                   |
| <i>CRIME</i>                                   | -0.047<br>(0.621)                   |                        |                        |                        |                   | -0.074<br>(0.389)                 |                    |                    |                    |                   |
| <i>CIVIL</i>                                   | 0.430<br>(0.073)                    |                        |                        |                        |                   | 0.383<br>(0.073)                  |                    |                    |                    |                   |
| <i>MUNT</i> <sup>4</sup>                       |                                     | -0.013<br>(<0.001)     |                        |                        |                   | -0.012<br>(<0.001)                | -0.024<br>(<0.001) |                    |                    | -0.023<br><0.001  |
| <i>DONS</i> <sup>4</sup>                       |                                     |                        | -0.009<br>(<0.001)     |                        |                   | -0.004<br>(0.006)                 |                    | -0.016<br>(<0.001) |                    | -0.011<br><0.001  |
| <i>GRANTS</i> <sup>4</sup>                     |                                     |                        |                        | -0.011<br>(<0.001)     |                   | -0.006<br>(<0.001)                |                    |                    | -0.020<br>(<0.001) | -0.017<br><0.001  |
| <i>BIGCPA</i> <sup>4</sup>                     |                                     |                        |                        |                        | 0.006<br>(0.142)  |                                   |                    |                    |                    |                   |
| <i>SMALLCPA</i> <sup>4</sup>                   |                                     |                        |                        |                        | -0.001<br>(0.877) |                                   |                    |                    |                    |                   |
| % sig. annual regressions at 0.05 <sup>2</sup> |                                     | 100%                   | 100%                   | 100%                   |                   |                                   |                    |                    |                    |                   |
| Observations                                   | 14,774                              | 97,080                 | 167,107                | 167,140                | 1,129             | 14,797                            | 21,078             | 21,078             | 21,078             | 21,078            |
| R <sup>2</sup>                                 | 0.04                                | 0.10                   | 0.10                   | 0.10                   | 0.09              | 0.04                              | 0.03               | 0.03               | 0.04               | 0.04              |

Notes:

1 – Coefficient estimates for control variables and industry dummies are not reported. *P*-values are in parentheses under their respective coefficient estimates. The reporting quality measure is *OTHER*, which is the average of the ratios of other assets, liabilities, revenues and expenses to their respective totals. Variables are winsorized at 1%, and in all analyses we screen for and omit influential observations using Cooks D, Studentized Residual, and leverage statistics (Belsley, Kuh, and Welsch 1980).

2 – In the “annual regressions” with more than one year in the sample period, the annual coefficient estimates and R<sup>2</sup> statistics are the averages of the separate annual regressions. Annual t-statistics are based on the distribution of the annual coefficient estimates (Fama-McBeth 1973). Also reported is the percentage of the separate annual regressions that had significant (at the five percent level) coefficients for the governance variable.

3 – In the “mean regressions,” we use the mean value of the all regression variables for each firm across the sample period.

4 – See Table 1 for the definition of the governance measures

**Table 6**  
**The Effects of Governance on Voluntary Description of Charitable Accomplishments<sup>1</sup>**

|   |                  |                  |                  |                  |                  |                  |
|---|------------------|------------------|------------------|------------------|------------------|------------------|
| Constant                                      | 4.42<br>(0.0001) | 4.38<br>(0.0001) | 4.03<br>(0.0001) | 4.30<br>(0.0001) | 4.75<br>(0.0001) | 4.33<br>(0.0001) |
| <i>LEGAL</i>                                  | -0.06<br>(0.147) |                  |                  |                  |                  | -0.06<br>(0.127) |
| <i>REPORT</i>                                 | 0.04<br>(0.033)  |                  |                  |                  |                  | 0.03<br>(0.051)  |
| <i>CRIME</i>                                  | -2.58<br>(0.667) |                  |                  |                  |                  | 3.29<br>(0.645)  |
| <i>CIVIL</i>                                  | 15.91<br>(0.234) |                  |                  |                  |                  | 19.71<br>(0.128) |
| <i>MUNF</i> <sup>2</sup>                      |                  | 0.40<br>(0.0001) |                  |                  |                  | 0.35<br>(0.001)  |
| <i>DONS</i> <sup>2</sup>                      |                  |                  | 0.31<br>(0.004)  |                  |                  | 0.17<br>(0.054)  |
| <i>GRANTS</i> <sup>2</sup>                    |                  |                  |                  | 0.21<br>(0.025)  |                  | 0.07<br>(0.401)  |
| <i>BIGCPA</i> <sup>2</sup>                    |                  |                  |                  |                  | -0.18<br>(0.038) |                  |
| <i>SMALLCPA</i> <sup>2</sup>                  |                  |                  |                  |                  | -0.50<br>(0.001) |                  |
| F-test for <i>BIGCPA</i> =<br><i>SMALLCPA</i> |                  |                  |                  |                  | 11.77<br>(0.001) |                  |
| Observations                                  | 605              | 610              | 608              | 607              | 590              | 591              |
| R <sup>2</sup>                                | 0.09             | 0.09             | 0.08             | 0.07             | 0.14             | 0.12             |

Notes:

1 – Coefficient estimates for control variables and industry dummies are not reported for the single year OLS regressions. *P*-values are in parentheses under their respective coefficient estimates. The reporting quality measure is the natural log of the variable *WORDS*, which is the number of words reported in the “Statement of Program Service Accomplishments” in Parts III and VIII of the IRS form 990 in 1996. The analysis sample is restricted to organizations that reported over \$100,000 in expenses. Variables are winsorized at 1%, and in all analyses we screen for and omit influential observations using Cooks D, Studentized Residual, and leverage statistics (Belsley, Kuh, and Welsch 1980).

2 – See Table 1 for the definition of the governance measures



**Table 7**  
**Event Analysis of Changes in Reporting Quality in response to Changes in Governance**

$$\text{Reporting Quality} = \beta_1 t_{-3} + \beta_2 t_{-2} + \beta_3 t_{-1} + \beta_4 t_0 + \beta_5 t_1 + \Phi \text{ Controls} + \varepsilon$$

|                          | $\beta_1$        | $\beta_2$        | $\beta_3$        | $\beta_4$        | $\beta_5$        | F-test<br>$\beta_1 = \beta_2$ | F-test<br>$\beta_4 = \beta_5$ | F-test<br>$\beta_2 = \beta_4$ | Obs.  | R <sup>2</sup> |
|--------------------------|------------------|------------------|------------------|------------------|------------------|-------------------------------|-------------------------------|-------------------------------|-------|----------------|
| <b>Municipal Bonds</b>   |                  |                  |                  |                  |                  |                               |                               |                               |       |                |
| <i>ADMIN</i>             | 3.90<br>(0.001)  | 4.06<br>(0.001)  | 4.44<br>(0.001)  | 5.11<br>(0.001)  | 5.15<br>(0.001)  | 0.01<br>(0.913)               | 0.33<br>(0.565)               | 8.55<br>(0.003)               | 3,144 | 0.65           |
| <i>FUND</i>              | 0.06<br>(0.885)  | 0.04<br>(0.924)  | 0.17<br>(0.663)  | 0.42<br>(0.295)  | 0.37<br>(0.276)  | 0.05<br>(0.834)               | 0.01<br>(0.923)               | 3.01<br>(0.083)               | 2,077 | 0.38           |
| <i>OTHER</i>             | 0.115<br>(0.001) | 0.005<br>(0.001) | 0.107<br>(0.001) | 0.089<br>(0.001) | 0.088<br>(0.001) | 0.02<br>(0.875)               | 0.02<br>(0.887)               | 26.57<br>(0.001)              | 3,145 | 0.68           |
| <b>Feeder Donations</b>  |                  |                  |                  |                  |                  |                               |                               |                               |       |                |
| <i>ADMIN</i>             | 3.51<br>(.0001)  | 3.58<br>(.0001)  | 3.75<br>(.0001)  | 3.98<br>(.0001)  | 4.09<br>(.0001)  | 0.44<br>(0.513)               | 0.31<br>(0.575)               | 7.71<br>(0.011)               | 7,509 | 0.59           |
| <i>FUND</i>              | 0.61<br>(0.002)  | 0.63<br>(0.001)  | 0.70<br>(0.001)  | 0.83<br>(0.001)  | 0.90<br>(0.001)  | 0.33<br>(0.562)               | 0.04<br>(0.848)               | 2.99<br>(0.083)               | 3,985 | 0.17           |
| <i>OTHER</i>             | 0.115<br>(0.001) | 0.004<br>(0.001) | 0.109<br>(0.001) | 0.105<br>(0.001) | 0.104<br>(0.001) | 0.01<br>(0.927)               | 0.11<br>(0.740)               | 6.73<br>(0.010)               | 7,510 | 0.63           |
| <b>Government Grants</b> |                  |                  |                  |                  |                  |                               |                               |                               |       |                |
| <i>ADMIN</i>             | 2.06<br>(0.001)  | 2.17<br>(0.001)  | 2.32<br>(0.001)  | 2.58<br>(0.001)  | 2.85<br>(0.001)  | 2.65<br>(0.103)               | 0.68<br>(0.408)               | 8.23<br>(0.004)               | 9,060 | 0.55           |
| <i>FUND</i>              | 0.699<br>(0.007) | 0.643<br>(0.014) | 0.876<br>(0.001) | 0.999<br>(0.001) | 0.999<br>(0.001) | 0.185<br>(0.667)              | 0.094<br>(0.759)              | 3.71<br>(0.054)               | 1,620 | 0.27           |
| <i>OTHER</i>             | 0.123<br>(0.001) | 0.119<br>(0.001) | 0.114<br>(0.001) | 0.111<br>(0.001) | 0.111<br>(0.001) | 0.00<br>(0.965)               | 1.69<br>(0.194)               | 5.05<br>(0.025)               | 6,081 | 0.64           |

Notes:

This table presents the results of the OLS regressions for the event analyses of the changes in accounting quality for those firms that experienced a change in governance during our sample period. The variables  $t_{-3}$  through  $t_1$  are indicator variables relative to the event of a change in governance (i.e.,  $t_{-3}$  is equal to one if the observation is from three years prior to the event period of a change in governance and zero otherwise, etc.). Observations are lined up in event time. The three events we consider are the issuance of municipal bonds, the receipt of feeder donations, and the receipt of government grants. Only the first event in our sample period is considered (i.e., the first time an organization receives feeder donations in our sample period). We include year and industry indicator variables, total revenues, total assets, and total donations as control variables. We conduct F-tests for differences in coefficient estimates at various times around the event period at  $t_0$ . We hypothesize that the reporting quality variables are not different immediately before or after the event period (i.e., they do not change from time  $t_{-3}$  to  $t_{-2}$  or from time  $t_0$  to  $t_1$ ), but that they are different across the event period (i.e., they change from time  $t_{-2}$  to  $t_0$ ).