Governance and Tax Avoidance in Nonprofits

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ABSTRACT

The purpose of this study is to evaluate whether increased governance measures in nonprofits are associated with less tax avoidance for unrelated business activities. As nonprofits seek additional revenue sources, they may engage in unrelated business activities, which are taxable. Prior research has indicated that nonprofits sometimes intentionally avoid taxation from these activities. This study addresses if governance, in the form of internal governance or monitoring from capital providers, mitigates this problem through evaluating its relationship with the reporting of positive taxable income. This quantitative study was evaluated through point-serial correlation, Kendall's tau-b, and logistic regression and used 2016-2017 public tax data. The results suggest a positive relationship between reliance on government grants and reporting positive taxable income. Nonprofits with increased reliance on government grants had 4.29 times higher odds to report positive taxable income. These results suggest that reliance on governmental funding may increase transparency compliance and decrease the likelihood that a non-profit will engage in tax avoidance activities. These results may help practitioners, boards, senior managers, and policy makers better understand their role in tax compliance.

Keywords: Governance, Tax Avoidance, Non-profits,

INTRODUCTION

Nonprofit organizations frequently turn to unrelated commercial activities in order to promote their exempt purposes; examples include a church selling its parking spaces to patrons of a nearby baseball stadium or a university's food service catering to non-university individuals. Income generated from these types of unrelated activities is considered Unrelated Business Income (UBI) by the Internal Revenue Service (IRS) and is subject to taxation, less any connected expenses (IRS, 2019). Prior studies have indicated that nonprofits do engage in tax misreporting and avoidance, mainly through tax-incentivized opportunities in expense allocations (Hofmann, 2007; Omer & Yetman, 2007). Some, including the IRS (2008), believe that greater internal governance and monitoring from capital providers reduces tax avoidance related to a nonprofit's unrelated business activity. Yet, an extensive review of the literature suggests that this relationship has not been empirically tested. In response, this study examines the monitoring effect of internal governance and capital providers on a firm's likelihood to engage in tax avoidance. In theory, by strengthening the monitoring of the organization, the nonprofit organization decreases agency issues related to the unrelated activity and reduces the ability of the organization to misallocate expenses due to increased risk of detection. Therefore, the researchers expect increased monitoring costs from internal governance and capital providers to decrease the level of tax avoidance in nonprofit reporting.

As a proxy for tax avoidance, this study uses a binary variable indicating the presence of taxable income. Predictor variables include a governance index (a composite score assessing board independence, audit and tax decisions, and nonprofit policies), and three forms of external capital: government grants, bonds, and restricted donations. Control variables include firm size, firm age, location, financial condition, industry, growth, religious affiliation, year, and charity navigator rating. The study leverages descriptive statistics, point-serial correlation, Kendall's tau-b, and logistic regression. Following Yetman and Yetman (2003), the researchers specifically investigate nonprofits in one of four sectors: 1) arts, cultures, and humanities; (2) education; (3) health; and (4) human services organizations.

The results of this study are mixed. As expected, the results suggest a positive relationship between reliance on government grants and positive taxable income, which implies there is less likelihood of tax avoidance schemes in the presence of grants. Nonprofits with increased reliance on government grants had 4.29 times higher odds to report positive taxable income. However, contrary to expectations, no association was found between the government index, bonds, or restricted assets and tax avoidance.

This study contributes to the literature by clarifying the role internal and external governance mechanisms have in mitigating tax avoidance for non-profit organizations. Specifically, this study extends the research of tax avoidance into the nonprofit sector. The study provides insight into the IRS' decision to revise the Form 990 in 2008; the IRS believed that governance structures would increase tax compliance (IRS, 2008). This study provides some support to this belief. In addition, this study used more available IRS data than past unrelated business income tax studies; prior research included many of its data before the Forms 990-T were made publicly available as a result of the Pension Protection Act of 2006 (Hofmann, 2007; Omer & Yetman, 2007). The governance information was not available until after the 2008 major revision of the Form 990 (IRS, 2008). While data is becoming more accessible, gaps remain in nonprofit research. This study fills the gap by using more accessible information.

The remainder of this paper is organized as follows. The next section provides a review the relevant literature, including the development of our hypothesis. Next, the study describes the methodology, data collection process, and analytics. Finally, after discussing the empirical results, this study indicates limitations, suggests opportunities for future research, and provides a brief conclusion.

LITERATURE REVIEW AND HYPOTHESES DEVELOPMENT

Organizations may engage in activities outside their exempt purpose in order to supplement revenue (Ecer, Magro, & Sarpca, 2017; Knoll, 2007; McArdle & Chene, 2017). To be unrelated, these activities are conducted on a regular basis and are not substantially related to the exempt purpose as indicated when the organization became tax exempt (IRS, 2019). While unrelated activity provides funding for nonprofit organizations, this activity does not significantly relate to the purpose of the organization (IRS, 2019). The IRS (2019) requires that these activities be profit-minded. Otherwise, donations would be used for activities outside of the nonprofit organization's mission.

The intention of UBI was to prevent unfair competition between nonprofits and for-profits (Hofmann, 2007). However, if nonprofits can avoid taxation on unrelated business activities, nonprofits are able to gain a competitive advantage over the for-profit organizations (Knoll, 2007), which decreases the efficiencies within society (Sansing, 1998). Tax avoidance also allows nonprofits to keep funds that belong to the government and the public. The IRS has responded to this issue by increasing the reporting requirements of nonprofits, including additional governance disclosures (Brody, 2012; IRS, 2008). However, compared to other tax arrangements, research on UBI is limited (Omer & Yetman, 2007).

Tax Avoidance

Desai and Dharmapala (2006) developed a theory that managerial rent diversion and tax avoidance may be complementary in nature. Building on that theory, Desai et al (2007) suggested that tax avoidance is generally conducted through complex transactions that hide the true managerial actions from the shareholder. The lack of transparency in financial statements allows a manager to use resources for their personal benefit, which is rent diversion. As managers engage in tax avoidance, managers must hide their transactions from the authorities, which make the company less transparent to shareholders (Desai & Dharmapala, 2006).

Desai and Dharmapala's theory suggested that stronger governance would increase the financial reporting quality and decrease managers using resources for their personal benefit. Tax avoidance increases information asymmetry, which increases agency issues. Stronger governance may lead to less tax avoidance as donors, capital providers would desire greater transparency (Desai & Dharmapala, 2006), and tax avoidance is risky in nature (Armstrong, Blouin, Jagolinzer, & Larcker, 2015). One would expect a negative relationship between governance and tax avoidance as reported on the Form 990-T.

While corporate taxation is a relatively recent accounting research area (Hanlon & Heitzman, 2010), research has suggested that tax avoidance occurs in the for-profit sector (Chen & Chu, 2005; Desai & Dharmapala, 2006; Frank, Lynch, & Rego, 2009; Hanlon & Heitzman, 2010; Kovermann & Velte, 2019; Weisbach, 2002; Wilson, 2009). This study considers the theory of tax avoidance as noted by Desai and Dharmapala (2006) and Desai et al. (2007), which

would predict a negative relationship between governance and tax avoidance on the Form 990-T.

Governance and Tax Avoidance

Prior research studies have considered the relationship of corporate governance to corporate taxation in the for-profit sector (Hanlon & Heitzman, 2010). Desai and Dharmapala (2006) determined that by convoluting the financial statements in order to hide tax shelter transactions, managers provided less transparent financials to the investors, which allowed managers to use resources for their personal benefit. As the incentives for management increased, the tax sheltering levels tended to decrease. Desai et al. (2007) indicated that weak governance leads to greater diversion of funds when tax rates are increased, so overall corporate tax revenues are decreased. Therefore, if tax rates are increased and corporate governance is strong, the overall corporate tax revenues collected by the government increased (Desai et al., 2007).

Other studies continue to connect the importance of corporate governance structures and tax avoidance. Armstrong et al. (2015) studied the relationships between governance, incentives, and tax avoidance. Mulyadi and Anwar (2015) found that corporate governance significantly influenced tax management. They found a positive relationship between the number of board members and tax management. In addition, they found a negative relationship between both board independence and board compensation and tax management. When studying the relationship of corporate governance and tax aggressiveness, Halioui, Neifar, & Abdelaziz (2016) found a negative relationship for board size and CEO salary.

To our knowledge, this line of research has not been applied to the nonprofit sector. Nonprofits are often organized as corporations (IRS, 2017), and the existence of two principals in nonprofits increases information asymmetry, which magnifies agency issues (Kitching, 2009). Nonprofits also avoid taxation through misreporting expenses on the Form 990-T (Omer & Yetman, 2007; Hoffmann, 2007). This study intends to fill this gap by conducting governance and tax avoidance research in the nonprofit sector.

Hypothesis Development

Dependent Variable

In order to evaluate the presence of tax avoidance, the study includes a dichotomous variable that indicates if the entity reported taxable income is either positive or nonpositive. Positive taxable income was noted by a 1 with nonpositive as 0. A dichotomous variable has been used in other tax-avoidance nonprofit studies (Omer & Yetman, 2003).

Independent Variables

First, the study considers internal governance. In the case of nonprofits, strong internal governance should not allow a nonprofit organization to engage in an unrelated business activity that did not bring a profit that could be used to further the exempt purpose. The strength of internal governance is generally measured through an index (Harris, Petrovits, & Yetman, 2015, Harris, Petrovits, & Yetman, 2017; Newton, 2015; Yetman & Yetman, 2012) based on questions answered on the Form 990. By including data concerning each nonprofit's board independence

(Harris et al, 2015, Harris et al., 2017, Newton, 2015), audit and tax decisions (Harris et al., 2017, Neuman, Omer, & Thompson, 2015, Newton, 2015) and governing policies (Harris et al, 2015, Harris et al., 2017, Newton, 2015, Yetman & Yetman, 2012), this study will establish a governance index, which is described in Table 1. The relationship between governance structures and tax avoidance remains difficult to predict due to differences from the classical principal-agent theory and the more recent theory posed by Desai and Dharmapala (2006). Therefore, the researchers defer to the null hypothesis.

Hypothesis 1: Internal governance measures have no relationship to tax avoidance for unrelated business activity as reported on the Form 990-T.

Table 1: Governance Index

Governance Index (Average of 3 Sections)	
Board Independence (Ratio of Points/Potential Points)	
INDEPENDENCE	Ratio of independent board members
OUT MGT	Outsourced management
INS BUS REL	Inside business relationship
MEMBERS	Oversight from members or stockholders
Audit and Tax Decisions (Ratio of Points/Potential Points)	
AUDIT	Audited or review/compilation
AUDIT COMM	Presence of audit committee
990 TAX	Tax preparer - 990
990-T TAX	Tax preparer – 990-T
WEBSITE	Availability of tax returns
Nonprofit Policies (Ratio of Points/Potential Points)	
990 REVIEW	Form 990 review policy
CEO COMP	CEO compensation policy
NON-CEO COMP	Non-CEO compensation policy
WHISTLE	Whistleblower policy
CONF INT	Conflict of interest policy
DOC RENT	Document retention policy

Second, this study considers governance from capital providers external to the nonprofit. Additional oversight from capital providers could influence the propensity to misreport unrelated business income tax. For example, oversight from the source of capital could affect tax avoidance due to the additional monitoring required to receive that capital (Nikolova, 2014). Additional monitoring and reporting are required when nonprofits receive government grants and contracts (Boris, De Leon, Roeger, & Nikolova, 2010), which is like requirements from Sarbanes-Oxley to public companies (Ostrower, 2007). A higher level of governmental reporting requirements should decrease the extent of agency issues (Nikolova, 2014). In addition, lenders of long-term debt have the right to monitor nonprofit organizations; this debt is primarily in the form of municipal bonds (Harris et al., 2017). Many of those that provide capital have the legal right for oversight of managerial actions (Harris et al., 2017). The level of restricted donations

also indicates the level of oversight from donors and reduces the flexibility related to using that funding (Shon, Hamidullah, & McDougle, 2019). Donors requiring restrictions tend to monitor the nonprofit more closely (Harris et al., 2017). Here, the researchers hypothesize:

Hypothesis 2: There is no relationship between the level of funding from capital providers and tax avoidance.

Hypothesis 2a: Capital provided from governments has no relationship to tax avoidance.

Hypothesis 2b: Capital raised through bond issues has no relationship to tax avoidance.

Hypothesis 2c: The level of restricted donations has no relationship to tax avoidance.

Overall, one should expect that greater governance results in less tax avoidance because the financials would require increased transparency (Desai & Dharmapala, 2006) and less risky behavior (Armstrong et al., 2015). Researchers have indicated that board monitoring is positively related to financial reporting accuracy on the Form 990 concerning the program ratio (Yetman & Yetman, 2012) as well as negatively related to asset diversions (Harris et al., 2017). One would similarly expect that additional board monitoring is positively related to financial reporting concerning unrelated business activities on the Form 990-T. Therefore, one would expect a nonprofit with greater governance to avoid less taxation and report positive taxable income.

While several nonprofit studies have discussed the issue of corporate governance (Harris et al., 2017; Yetman & Yetman, 2012), no study to our knowledge has yet considered the relationship between corporate governance and the avoidance of unrelated business income taxes. While the relationship is difficult to predict, stronger governance should have an impact on tax avoidance measures (Kovermann & Velte, 2019). This study intends to fill the gap from prior research and consider the relationship between governance and tax avoidance.

METHODOLOGY

The purpose of this study is to examine the relationship between governance mechanisms and tax avoidance. This goal is accomplished through descriptive statistics, point-serial correlation, Kendall's tau-b, and logistic regression, where the latter is common in nonprofit studies (Harris et al., 2017; Omer & Yetman, 2003, 2007; Yetman & Yetman, 2012).

Since the dependent variable is dichotomous, the researchers employed logistic regression. In general, logistic regression will require a larger sample size than multiple linear regression (Hair, Black, Babin, & Anderson, 2015). For binomial logistic regression, one assumption is that a minimum of 15 cases should be included in the sample size per each independent variable (Laerd Statistics, 2015). As the study has four predictor variables and nine control variables, the sample size must equal at least 195 returns. Van der Ploeg, Austin, and Steyerberg (2014) found that logistic regression reached a stable conclusion based on 20-50 events per variable. Hosmer and Lemeshow (2000) recommended a sample size that was at least 400. Therefore, this study uses a sample size of 400, which is 31 samples per variable and meets the assumptions noted by Laerd Statistics (2015) and Van der Ploeg et al. (2014). Much information needs to be compiled from the Forms 990 and 990-T, so a sample is necessary to evaluate the question.

Sample and Data Collection

The population for this study includes nonprofit organizations with unrelated business income activity that filed both a Form 990 and Form 990-T in the tax years 2016-2017. The sample frame includes nonprofit organizations with returns that are available through the IRS Annual Extract (IRS, n.d.-a). The Forms 990 and 990-T are available on the Tax-Exempt Organization Search website beginning with the 2016 tax year (IRS, n.d.-b). Since nonprofit information starting in 2016 is readily accessible, this study will include tax returns from 2016 and 2017. From these forms, one can see the amounts filed on the tax return (IRS, n.d.–c), which allows an accurate assessment of data.

In this study, data was primarily collected from the IRS website, Nonprofit Explorer, and Charity Navigator. For sample selection, the study used a stratified, random sample. The following industries were to be evaluated in the study: (1) arts, cultures, and humanities; (2) education; (3) health; and (4) human services organizations. The total required sample size under logistic regression was 400 returns, so 100 returns were included from each industry.

If the nonprofit was missing information for both years, then the next nonprofit was selected according to the random numbers established in Excel. The final data set includes pooled data that is cross-sectional and time-series data. Missing reports are possible because nonprofits may select that they filed a Form 990-T but did not actually file the Form in the current tax year.

Model

Complete Empirical Model

This section includes the procedures for each hypothesis and discusses the model used in this study. Data analysis is completed within SPSS. An increase in internal and external governance measures is expected to decrease the level of tax avoidance as indicated on the nonprofits' tax returns.

With a dichotomous dependent variable, one would need to use logistic regression in order to generate a model to test the null hypothesis. In addition, binomial logistic regression would include only nominal or continuous variables. The governance index is continuous in nature. Both *Hypothesis 1* and *Hypotheses 2* are made up of continuous independent variables and a dichotomous dependent variable. For each hypothesis (*1, 2a, 2b, 2c*), this study will test the correlation through point-biserial correlation. This correlation analysis assumes that one variable is continuous, and the other variable is dichotomous (Laerd Statistics, 2015). The correlation analysis will be testing for the null and alternative hypotheses as noted below (Laerd Statistics, 2015).

H_0: $\rho_{pb} = 0$; the population correlation coefficient is equal to zero.

H_A: $\rho_{pb} \neq 0$; the population correlation coefficient is not equal to zero.

After incorporating correlation analysis, this study will incorporate the full model into the logistic regression for *Hypotheses 1 and 2*. The logistic regression equation is noted below.

$$P(AVOID) = \alpha + b1\ (GovIndex_i) + b2\ (GovGrants_i) + b3\ (MuniBonds_i) + b4\ (RestrAssets_i) + b5\ (Age_i) + b6\ (EconCond_i) + b7\ (Location_i) + b8\ (Size_i) + b9\ (Growth_i) + b10\ (Industry_i) + b11\ (Religion_i) + b12\ (Year_i) + b13\ (Rated_i) + \varepsilon i$$

DATA ANALYSIS

With the removal of one extreme outlier, the sample included 399 tax returns. The sample of the governance index had a mean (median) of 0.688 (0.729). The governance index indicates the level of internal governance within a nonprofit based on answers to questions about board independence, policies, and audit and tax decisions. A nonprofit with a governance index of zero would have no governance measures in place; meanwhile, a nonprofit with a score of 1 would have perfect governance. Though the data was not normally distributed, the governance index could be transformed through Templeton's (2011) two-step process.

The percentage of revenue from government grants had a sample mean (median) of 7.35% (0.00%). The percentage of assets with restrictions reported a sample mean (median) of 18.07% (1.75%). Both the government grants and restricted asset variables indicated non-normal distribution; both were skewed with high kurtosis. The distribution was expected due to the number of nonprofits reporting no government grants or no restricted assets.

The sample mean (median) for the percentage of revenue from municipal bonds was 0.02% (0.00%). Overall, only 13 nonprofits indicated any revenue from municipal bonds. In this sample, only one nonprofit reported a percent of revenue exceeding 1% for municipal bond revenue. Therefore, the variable for municipal bond revenues is not normally distributed. Table 2 notes the descriptive statistics for the sample.

Table 2: Descriptive Statistics

Variable	*n*	*M*	*SD*	Min. Value	Median	Max. Value	Skewness	Kurtosis
Avoidance	399	0.296	0.457	0	0	1	0.899	-1.199
Governance Index	399	0.688	0.161	0.104	0.729	0.938	-1.353	1.441
Government Grants	399	7.35%	0.175	0.00%	0.00%	96.33%	3.108	9.658
Municipal Bonds	399	0.02%	0.005	0.00%	0.00%	9.32%	19.973	398.936
Restricted Assets	399	18.07%	0.359	-284.70%	1.75%	353.82%	1.292	30.902

The relationship between the governance index and the tax avoidance measure was evaluated through point-serial correlation and Kendall's tau-b. The governance index was slightly higher for firms with positive taxable income (M = .692, SD = .01) than firms with nonpositive taxable income (M = .686, SD = .01). A statistically significant correlation did not exist (r_{pb} (399) .02, p = .71). Based on Kendall's tau-b, there was a weak positive association between the governance index and tax avoidance, τ_b = .011. However, this relationship was not statistically significant, p = .798.

The relationship between each capital provider measure (government grants, municipal bonds, and restricted assets) were evaluated through Kendall's tau-b. Based on Kendall's tau-b, there was a weak positive association between the level of government grants and tax avoidance, τ_b = .071, though the relationship was not statistically significant, p = .108. Looking at municipal

bonds, there was a weak negative association between the level of municipal bonds and tax avoidance, τ_b = -.03. However, this relationship was not statistically significant, p = .6. Finally, there was a weak negative association between the level of restricted assets and tax avoidance, τ_b = -.03, but the relationship was not statistically significant, p = .557. Overall, no relationships were supported in the correlation analysis.

The entire model was evaluated through logistic regression for governance and the dichotomous tax avoidance measure. This analysis included all four independent variables and nine control variables. As the dependent variable is dichotomous, logistic regression will be used. In order to evaluate the data, a t-test with an independent sample was conducted between the two groups (nonpositive taxable income and positive taxable income). The results are shown in Table 3. Based on these results, significant differences were found between the groups for the government grants, industry, and tax year variables. All other variables did not have significant differences between the groups.

Table 3: Differences between Groups

	Nonpositive Taxable Income			Positive Taxable Income			*t-test*	
Variable	*n*	*M*	*SD*	*n*	*M*	*SD*	*t*	*Sig*
Governance Index	281	0.688	0.160	118	0.689	0.164	-0.036	0.971
Government Grants	281	5.882%	15.096%	118	10.845%	21.976%	-2.241	0.026*
Municipal Bonds	281	0.034%	0.033%	118	0.000%	0.002%	0.654	0.514
Restricted Assets	281	19.309%	39.249%	118	15.123%	26.356%	1.242	0.215
Age	281	55.300	40.489	118	51.500	36.771	0.879	0.380
Economic Condition	281	8,355,664.669	63,425,554.600	118	7,915,559.191	21,759,166.890	0.074	0.941
Location	281	6.774%	2.849%	118	6.943%	2.767%	-0.546	0.586
Size	281	7.160	1.175	118	7.270	1.194	-0.885	0.377
Growth	281	33.104%	604.017%	118	30.136%	19.223%	0.541	0.589
Industry	281	2.420	1.122	118	2.700	1.088	-2.323	0.021*
Religion	281	0.100	0.334	118	0.080	0.267	0.675	0.500
Tax Year	281	0.590	0.493	118	0.690	0.462	-2.082	0.038*
Rated	281	0.120	0.327	118	0.090	0.292	0.799	0.425

* $p < 0.05$

In SPSS, the Box-Tidwell (1962) can analyze linearity of the continuous variables with respect to the logit of the dependent variable. A Bonferroni correction was applied using all 26 terms of the model resulting in a statistical significance being accepted when $p < 0.002$ (Laerd Statistics, 2015). Based on this assessment, all continuous independent variables were found to be linearly related to the logit of the dependent variable. Once linearity was confirmed, logistic regression could be conducted. Outliers were noted. There was one standardized residual with a value of 2.657 standard deviations, which was removed from the analysis. The data point was more than 2.5 standard deviations.

The model was statistically significant, with the regression results indicating p = .047. The Hosmer and Lemeshow test indicated that the model is not a poor fit because p = .934.

According to the Cox and Snell R^2 and the Nagelkerke R^2 values, the explained variation in the tax avoidance measure in the model ranges from 6.4% to 9.2%. The model correctly classified 70.1% of the cases. The classification matrix can be found in Table 4. This classification percentage is higher than other unrelated business income tax studies; Omer and Yetman (2003) reported a model that correctly classified 62.0% of the cases. In addition, 7.7% of nonprofits with positive taxable income were predicted by the model to have positive taxable income, which indicated the level of sensitivity. For specificity, 96.1% of nonprofits with nonpositive taxable income were correctly predicted. The model therefore strongly predicted the firms reporting nonpositive taxable income but predicted the firms reporting positive income poorly. The positive predictive value was 45%, and the negative predictive value was 71.4%. In order to assess multicollinearity, the dependent variable was treated as continuous since the variable is dichotomous. In this regression, the tolerance for the independent variables were greater than 0.1. The VIF values were less than 3. The results indicated that a collinearity problem does not exist in this regression.

Table 4: Classification Matrix

	Predicted		
	Avoidance		Percentage correct
Observed	Nonpositive taxable income	Positive taxable income	
Nonpositive taxable income	270	11	96.10%
Positive taxable income	108	9	7.70%
Overall percentage			70.10%

RESULTS

Overall, a binomial logistic regression was performed to ascertain the effects of governance on the likelihood that the nonprofits reported taxable income related to unrelated business activities. The results are shown in Table 5. Of the variables, only government grants and the tax year was statistically significant. Nonprofits with increased reliance on government grants had 4.29 times higher odds to report positive taxable income. Therefore, the evidence indicates some support for a positive relationship between the percentage of revenue from government grants and reporting positive taxable income on the Form 990-T. The implication of the results suggests that firms that are funded by government grants are less likely to engage in tax avoidance strategies.

The only control variable that had a significant relationship was tax year. Nonprofit returns completed in 2016 had 0.57 times odds to report positive taxable income. The 2017 TCJA, though not enacted until the 2018 tax year, may have adjusted behaviors in the 2017 tax year.

Table 5: *Logistic Regression Predicting Likelihood of Positive Taxable Income based on Governance Measures.*

	B	*SE*	*Wald*	*df*	*p*	*Odds Ratio*	*95% CI for Odds Ratio*	
							Lower	*Upper*
Governance Index	-0.663	0.957	0.480	1	0.488	0.515	0.079	3.362
Government Grants	1.457	0.640	5.180	1	0.023*	4.293	1.224	15.053
Municipal Bonds	-3305.392	4,485.772	0.543	1	0.461	-	-	
Restricted Assets	-0.150	0.355	0.178	1	0.673	0.861	0.430	1.725
Age	-0.002	0.004	0.276	1	0.599	0.998	0.991	1.005
Economic Condition	0.000	0.000	0.137	1	0.711	1.000	1.000	1.000
Location	2.967	4.278	0.481	1	0.488	19.428	0.004	85,142.383
Size	0.253	0.157	2.583	1	0.108	1.287	0.946	1.752
Growth	-0.021	0.039	0.282	1	0.595	0.980	0.908	1.057
Industry			4.167	3	0.244			
Arts	-0.503	0.336	2.237	1	0.135	0.605	0.313	1.169
Education	-0.460	0.367	1.567	1	0.211	0.632	0.308	1.297
Health	0.054	0.359	0.022	1	0.881	1.055	0.522	2.135
Religion			0.000	2	1.000			
None	20.515	22,793.658	0.000	1	0.999	811,917,042.949	-	
Christian	20.510	22,793.658	0.000	1	0.999	807,987,531.200	-	
Tax Year - 2016	-0.558	0.244	5.221	1	0.022*	0.572	0.355	0.924
Rated - Not Rated	0.187	0.412	0.205	1	0.651	1.205	0.537	2.704
Constant	-22.670	22,793.658	0.000	1	0.999	0.000		

Note: Response Event = 1 (positive taxable income); Response Event = 0 (nonpositive taxable income)
* p < .05

DISCUSSION OF RESULTS

This study considered the relationship between governance and tax avoidance related to unrelated business activities in nonprofit organizations. To our knowledge, no other study has researched this relationship in a nonprofit setting. The most significant outcome from this study is the evidence supporting a relationship between government grants and tax avoidance. With government grants, a nonprofit organization often must follow requirements like Sarbanes-Oxley for public companies (Ostrower, 2007). Ostrower (2007) suggested that the nonprofits that receive government funding may have a higher culture of accountability and reporting as compared to other nonprofits. In addition, nonprofits with government grants may also have greater participation from beneficiaries, which provides greater feedback to the organization

(Mandel & Qazilbash, 2005). With this additional required transparency, one would expect nonprofits with greater reliance on government funding to have less tax avoidance.

The results suggested that firms with greater reliance on government grants experience some significantly different outcomes related to unrelated business taxable income. With logistic regression, the relationship between government grants and tax avoidance was statistically significant (p = .023); nonprofits with increased reliance on government grants had 4.29 times higher odds to report positive taxable income. Therefore, the reliance from government grants is negatively related to tax avoidance for unrelated business activities. These results suggest that funding from governmental sources in nonprofit organizations may increase transparency and tax compliance. This finding supports the theory of corporate tax avoidance that greater transparency increases tax compliance (Desai & Dharmapala, 2006; Desai et al., 2007).

As a nonprofit organization increases its percentage of revenue from government grants, the nonprofit may benefit from increased tax compliance. Current nonprofit rules generally require public charities to maintain at least one-third of their donations from the general public or exempt functions (IRS, n.d.-e). If the most important goal is to increase tax compliance, the IRS may consider adding government assistance to the calculation. The government may consider increased funding to nonprofit organizations in order to achieve higher tax compliance when lacking.

Contrary to expectations, no relationship was found between the governance index, bonds, or restricted assets and tax avoidance. Regarding the governance index, unlike other studies that found that stronger governance decreased tax avoidance in other for-profit arenas (Armstrong et al., 2015; Mulyadi & Anwar, 2015), this study did not arrive at the same conclusion. The researchers suspect our government index was too aggregated to find any relationship with tax avoidance. In for-profit studies, different elements of the governance index were tested separately. For example, Armstrong et al. (2015) considered only board independence and board financial sophistication. Mulyadi and Anwar (2015) found a positive relationship between the number of board members and tax management; they also found a negative relationship between board independence and tax management. Halioui et al. (2016) considered various independent variables for governance, including, board size, board independence, CEO salary, CEO compensation, CEO age, CEO tenure, and other variables. In their study, they only discovered a negative relationship between board size and CEO salary with tax aggressiveness. Instead of using an index, one may consider the different measures separately to discover any relationships between internal governance and tax avoidance.

The researchers also surmise that the revenue from municipal bonds may not be large enough to warrant any power for the oversight from municipal bondholders. Likewise, donors with restrictions may be focused on their specific donations instead of the unrelated business activity and tax compliance.

LIMITATIONS AND FUTURE RESEARCH

In this study, several limitations exist. First, the distribution of the independent and dependent variables violate normality. Non-parametric tests were used to evaluate the data in several calculations, but we accepted some violations when employing the regression analysis. As the sample size was 399 returns, the data from regression does tend to become more trustworthy even as normality is lacking due to the central limit theorem (Williams, Grajales, & Kurkiewicz, 2013). However, the results from the regression analysis may be considered biased.

Second, this study was limited to the data on the IRS website, which covered the tax years 2016 and 2017. Considering other returns in different years may provide better estimations for some variables. Third, we must assume that all information presented on the Form 990 for governance disclosures is accurate. Fourth, this study assumes that the board members have the financial sophistication to carry out tasks as disclosed. Finally, this is a correlation study, which does not consider causation but only the relationships between the variables presented.

While this study extended the nonprofit literature, some questions remain unanswered. In addition, new changes due to the current climate and the Form 990-T create questions. These questions present future research opportunities. Future research should consider some of the components of the governance index separately, the impact of the Tax Cuts and Job Act enacted in 2018, different subsets of nonprofits, and other variables, like the program ratio.

CONCLUSION

Evidence from this study indicates that reliance on government grants is related to less tax avoidance. An implication is that firms with governmental funding tend to be more transparent and comply with tax laws. Moreover, if this finding was the result of additional oversight required with governmental funding, policy makers should consider if that additional oversight should be required of other nonprofit organizations. In addition, policy makers should consider the Form 990 disclosure requirements to better pinpoint the disclosures that may increase tax compliance.

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