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Incorporated but Not IRS-Registered: Exploring the (Dark) Grey Fringes of the Nonprofit Universe

Kirsten A. Grønbjerg[1], Helen K. Liu[1], and Thomas H. Pollak[2]

Abstract

Listings of Internal Revenue Service (IRS)-registered and state-incorporated nonprofits for the same region may differ for a variety of reasons. Using Indiana as a case study, we first describe the distribution of nonprofits across these two listings. We then present findings from a small telephone survey of incorporated nonprofits that are not registered with the IRS for Indiana to explore whether they are excluded from the IRS-listing for statutory, technical, or compliance reasons. We consider several aspects of state incorporation status: date of incorporation and whether active status has been maintained or not. We conclude that researchers need to pay careful attention to the limitations of the IRS registration system when wishing to examine the dimensions of the nonprofit sector at local, state, or regional levels. Our finding, that some nonprofits fail to maintain active incorporation status, points to significant problems of nonprofit capacity.

Keywords

Nonprofit, IRS registration, state incorporation, regional analyses

A growing number of quantitative studies of the nonprofit sector at both national and regional levels have focused on a subset of Internal Revenue Service (IRS)-registered nonprofits—those registered under subsection 501(c)(3), e.g., "charities" that file IRS

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Form 990s (hereafter referred to as "charitable filers").[1] These data are now available in digitized formats that researchers can efficiently manipulate to develop economic portraits of the nonprofit sector at the national or subnational levels. For recent examples, see Independent Sector and Urban Institute, (2002); the New York City Nonprofits Project (http://www.nycnonprofits.org); Wing, Pollak, and Blackwood (2008); De Vita and Twombly, (2003); and Rafter and Silverman, (2006).

Another stream of research suggests that using charitable filers as the primary source for understanding the nonprofit sector is misleading. More than 25 years ago Salamon and his colleagues used multiple listings to develop comprehensive listings of nonprofits in 16 U.S. communities (Salamon, 1995), revealing substantial gaps in the IRS listings for at least some communities (Grønbjerg, 1989, 1994). A few years later, an effort to develop a census of nonprofits in New York City found that half the organizations did not appear on the IRS rolls (Haycock, 1992). More recently, analysis of a database of Indiana nonprofits drawn from multiple sources revealed that only 23% of the entries appeared on both state corporate and IRS registries (Grønbjerg & Paarlberg, 2002). Using a large (N = 2,206) survey of nonprofits drawn from that database, Grønbjerg and Clerkin (2005) concluded that researchers wishing to generalize their findings to the full nonprofit sector should use state corporate registries as a sampling frame because it includes the majority of churches and captures newer organizations more effectively than IRS registration.

These findings support Smith's argument (1997) that the "dark matter" of the nonprofit sector contains millions of organizations that do not register with the IRS, let alone file Form 990[2] and confirm the importance of understanding the broad array of nonprofit data sources available. But they raise also more substantive questions about the characteristics of the nonprofits not registered with the IRS. Are they small organizations or churches that are not required to be register? If not, what might account for their absence from the IRS listing?

We explore the two latter questions. We first describe key reasons why nonprofits may be incorporated but not registered with the IRS as tax-exempt entities. (We also briefly consider why IRS-registered nonprofits may not be incorporated). We then depict the types of nonprofits included in only one rather than both listings. Next, we report findings from a telephone survey of nonprofits included in the state corporate registry but not in the IRS Business Master File to explore why they are omitted from the latter. We conclude that researches should familiarize themselves with the strengths and weaknesses of all available nonprofit data sources and select the one (or several) that fits best the research questions or focus of the analysis.

Nonprofit Listings: Dual vs. Single Listing Status

Although many nonprofits may operate informally for years, the majority will find it to their advantage to establish some form of formal legal status fairly early in their lifecycle. To do so, the organization may incorporate with state authorities as a not-for-profit incorporation to establish the organization as a legal entity, thereby protecting both the organization's name and the personal liability of individuals affiliated with it. It may also seek federal tax-exempt status with the IRS to avoid liability for federal (and usually state) income taxes and, in the case of those recognized as "charities," to be eligible to receive tax-deductible contributions from individuals, businesses, and foundations.

Figure 1 presents four possible combinations of these two legal statuses in the non-profit universe: (a) organizations recognized as tax-exempt entities with the IRS and incorporated with the state in Cell 1—the "bright matter" in the universe, (b) organizations recognized as tax-exempt entities with the IRS, but NOT incorporated with the state in Cell 2—part of the "grey matter" in the universe, (c) organizations NOT registered with the IRS, but incorporated with the state in Cell 3—also part of the "grey matter" of the universe, but designated "dark grey" because they are invisible to most researchers who focus on only IRS exempt entities, and (d) organizations neither registered with the IRS nor incorporated with the state—the "dark matter" of the nonprofit universe. We turn now to the reasons why nonprofits may be part of the "grey matter"—that is, have secured one type of legal status but not the other.

Omission from the IRS Listing of Tax-Exempt Entities

There are many reasons why incorporated nonprofits may not appear on the IRS Business Master File (BMF) of exempt entities (Cell 3 in Figure 1). We group these into three broad categories: Statutory features of the IRS registration system, technical or methodological issues related to timing or purpose of the listings, and—more troublesome—failure to comply with federal regulations.

Statutory reasons. First, not all nonprofits must register with the IRS. Some entities, such as congregations and their integrated auxiliaries or subordinate units (such as parochial schools), apostolic orders, and conventions or associations of churches do not need to apply for recognition of exemption, unless they desire a ruling. According to the National Center for Charitable Statistics (2008), about half the estimated 350,000 congregations are registered. Other entities that would normally be recognized as tax-exempt also need not register if they have less than US $5,000 in gross receipts. This is also a sizeable omission.[3]

Certain other nonprofits—likely to be quite numerous—also are presumed to be tax-exempt without formally registering: qualified retirement plans, political committees, and homeowners associations (C. M. Watkins, personal communication, February 6, 2006.). Indeed, the IRS code only requires registration explicitly of entities falling under three other 501(c) subsections: (c)(9)—voluntary employees beneficiary associations, (c)(17)—supplementary unemployment benefit trusts, and (c)(20)—legal service organizations. Those not required to register may, of course, nevertheless seek registration for strategic reasons, for example, to confirm legitimacy as exempt organizations and/or signal eligibility for foundation grants or charitable contributions. Others may refrain from registration for other strategic reasons, for example, they lack the resources

		State incorporated	
		YES	NO
IRS registered	YES	Cell 1 “Bright Matter”	Cell 3 “Light Grey Matter” • Statutory reason • Inactive incorporation status • Strategic choice
	NO	Cell 2 “Dark Grey Matter” • Statutory/strategic choice reason • Technical reason • Compliance reasons	Cell 4 “Dark Matter”

Figure 1. Conceptual map of state incorporation and IRS tax-exempt status

and expertise to file the necessary paperwork or they conclude that the initial costs outweigh the benefits. That may be the case if they are small, new, or relatively inactive organizations with minimal need for securing federal income tax exemption or providing their donors with a tax deduction. (Incorporating an organization in Indiana costs only US $30 for the initial registration and US $5 to US $10 each year thereafter, compared to current IRS fees of US $300 to US $700 for processing a Form 1023.)

Technical or methodological reasons. There are also technical issues related to paperwork submissions and processing that may explain other discrepancies. For example, applications for IRS recognition as tax-exempt entities include questions about the legal form of the organization and whether it is incorporated or not.[4] Although the IRS does not require nonprofits to incorporate as a condition of obtaining exempt status, those that indicate on their exempt application that they are incorporated must provide the IRS with a copy of the articles of incorporation showing certification of filing with the appropriate state agency. For these nonprofits, at least, incorporation occurs prior to obtaining exempt status. For others, the sequence may be reversed, or they may secure one type of legal status but not the other. It may then take months, sometimes years, for organizations to obtain a final ruling from the IRS and additional time may pass before the BMF is updated to include the newly recognized entities. Other technical issues include geographic biases.[5] Thus some nonprofits, for example, local subsidiaries or affiliates, may be incorporated in one jurisdiction but use the address of a headquarter organization or a fiscal agent located in another jurisdiction for purposes of reporting to the IRS.

In addition, identifying which nonprofits are both incorporated and IRS-registered is difficult because listings vary in how frequently and completely they are updated. Although incorporated entities must submit annual reports and fees to maintain active incorporation status, only larger IRS-registered nonprofits have been required to file annually (now all must).[6] Also, there are no common identifiers between the two listings to easily identify matches between the two.[7] As a result, one must either look up each incorporated nonprofit (currently some 37,000 in Indiana) against the BMF file (currently about 36,200 for Indiana[8]) or find matches by merging listings and flagging apparent duplicates. Both approaches are time consuming and problematic.

Compliance reasons. Finally, there may be more troublesome reasons why some incorporated nonprofits are missing from the IRS list of exempt entities. Some may not recognize the difference between state and federal regulations and believe that if they are incorporated as nonprofits and/or met other state regulations, they need do no more.[9] The IRS Exempt Organizations Division and most state charity offices are notoriously underequipped for enforcement activities (Jenkins, 2007) and information sharing between the IRS and state corporate or charity offices is limited. As a result, nonprofits may fail to meet their legal obligation to register at the federal level without they or anyone else, including federal and state regulators, recognizing it.

Omissions from Listings of State Nonprofit Incorporations

Although many nonprofits incorporate at the state level before completing their federal tax exempt status[10] that is not a requirement and many do not incorporate at all. Although not our primary focus, we briefly review major reasons why IRS-registered nonprofits may not be incorporated (cell 2 in Figure 1), or at least not in states where they are registered with the IRS. We group also these into three broad categories: Statutory features of the incorporation system, technical and methodological reasons, and strategic choices about where to incorporate.

Statutory reasons. Incorporation allows a nonprofit to obtain standing as a legal entity and as such engage in contracts, safeguard its name, and protect its officers and key employees from personal liability. However, incorporation is voluntary and statutory reasons may therefore explain most omissions from state incorporation listings. Most that incorporate do so in the state where they are headquartered (Jenkins, 2007)[11] although that also is not required.

Technical and methodological reasons. To maintain legal status as a corporation, nonprofits (and other corporations) must pay annual fees and file annual report. Some may forget or delay because they lack adequate staff or resources to file the necessary paperwork. In this case, the organization's incorporation status may be designated as administratively inactive and not included on incorporation listings until reinstated.[12] In addition, as noted above, it is difficult to accurately determine whether organizations are both state-incorporated and IRS-registered, so there may be methodological reasons why nonprofits do not appear to be state incorporated.

Strategic choice reasons. Finally, nonprofits may make strategic decisions about where to incorporate based on differences in state legal environment (Abzug & Mezias, 1993; Abzug & Turnheim, 1998; Edelman, 1990, 1992; Jenkins, 2007). Although federal laws govern the tax treatment of charitable contributions, unrelated business income, and nonprofit lobbying activities, state incorporation laws focus more on governance matters, such as the number of directors required, fiduciary duties, donor standing with respect to lawsuits, liability standards, parliamentary procedures, and so on (Jenkins, 2007; Malamut, 2008a, 2008b, 2008c).[13] States also vary in the extent to which charities are required to file financial reports or report on fundraising activities[14] and in how well staffed they are to enforce regulations.[15] Nonprofits may therefore choose to incorporate in states with lenient requirements or weak enforcement capacity. Alternatively, nonprofits may incorporate in states that help project a particular image as nationally or internationally focused organizations (e.g., by incorporating in New York or the District of Columbia). However, as Jenkins (2007) shows, most of the largest nonprofits incorporate in the state where they are headquartered.

We turn now to our empirical analysis of why some nonprofits are incorporated, but not IRS registered. First, we provide a brief overview of nonprofits included in the comprehensive Indiana database and how they distribute themselves across the various segments of the nonprofit universe as identified in Figure 1. We follow that with a more in-depth look at the "dark grey" matter of the nonprofit universe (Cell 3 in Figure 1)—nonprofits that are invisible at the national level because they are not registered with the IRS, even though they have secured state recognition as not-for-profit corporations.

Findings: Composition of the Nonprofit Universe—Bright and Grey matter

In 2005, the Indiana Nonprofits Sector (INS) project research team completed an update of a comprehensive database of Indiana nonprofits originally developed in 2001. For both the original database and the update, the research team relied primarily on three statewide sources of nonprofit listings: the IRS list of tax-exempt entities, the Secretary of State listing of Indiana incorporated nonprofits, and the yellow page listings of congregations in Indiana.[16]

Analysis of the original 2001 statewide database (Grønbjerg & Paarlberg, 2002) revealed that only 23% of the 54,100 nonprofits in the statewide "three-database" (3DB) listing were included on both lists, that is, constituted the "bright" matter in the nonprofit universe by our definition. By 2005, there were 51,100 nonprofits in the state included in the 3DB listing, down by almost 6% from 2001, of which 33% constituted "bright matter." This reflected an overall decline in the number of IRS registered nonprofits by 7%,[17] whereas state incorporated nonprofits grew by 15%. These differential growth rates suggest that there were notable changes in how well IRS and state incorporation listings covered Indiana nonprofits and in the extent of overlap between the two. Indeed, as Figure 2 shows, the number of dual-listed (bright matter) nonprofits increased by 36%, whereas those found only on the IRS file (light grey matter) was down by 34%; those found only on the state incorporation listing (dark grey matter) declined by almost 1%, and "dark matter" nonprofits (in this case, congregations found only on the yellow pages) declined by 12%.

		State incorporated	
		YES	NO
IRS registered	YES	Cell 1 "Bright Matter" 16,986 (+36%)	Cell 3 "Light Grey Matter" 13,161 (−34%)
	NO	Cell 2 "Dark Grey Matter" 16,819 (−1%)	Cell 4 "Dark Matter" 4,099 (−12%)

Figure 2. Distribution of Indiana Nonprofit Universe in 2005 and percentage change since 2001

The differential growth rates in nonprofit listings for the state of Indiana raise important questions about how patterns of dual and single source listings have changed since 2001. However, because of space limitations we provide here only a brief summary of how single-listed (grey matter) nonprofits compare to dual-listed (bright matter) nonprofits in 2005, recognizing that the analysis is limited by the information available in the two major source listings. For full details and tables, including analysis of how these patterns have changed over the 2001-2005 period, see Grønbjerg, Liu, Pollak and Elliott-Teague (2009).

Of the 59% of Indiana nonprofits that were registered with the IRS in 2005, more than half (56%) were also incorporated in Indiana (up from 38% in 2001). But that percentage varies considerably by subsection, ranging from a high of 97% for subsection 12 (benevolent life-insurance or mutual cooperatives) to a low of 44% for subsection 07 (pleasure, recreation, and social clubs). Not surprisingly, those listed as corporations in the IRS registration file are more likely to be Indiana incorporated (83%) than associations (23%). So are independent nonprofits and central or intermediary organizations (70%-76%) compared to only 27% of the many subordinates registered as parts of a group.

The ratio of bright to light grey matter is also higher for the 10,000 or so IRS-registered Indiana nonprofits that file Form 990 of which more than 70% overall were incorporated in 2005, with percentages increasing with size (whether defined in terms of assets or income). Contrary to expectations, we find that rates of incorporation are highest for newly registered nonprofits, reflecting perhaps growing sophistication among nonprofit managers and entrepreneurs. For nonprofits that are both IRS registered and state incorporated in 2005, the year of state incorporation occurs at an average of 1.2 years prior to the year of IRS registration.

Our ability to compare bright and dark grey matter nonprofits is much more limited because the state incorporation listing contains very little information beyond the year of incorporation. However, we estimate that fully half of organizations obtaining state incorporation alone (no IRS registration) are either congregations or local community associations, compared to only 17% of organizations in the overall IRS Business Master File.

Findings: Exploring the Dark Grey Fringes of the Nonprofit Universe

We turn now to a more in-depth assessment of the subset of Indiana nonprofits, almost 17,000 organizations in 2005, that maintained active state incorporation status, but do not appear on the IRS list of exempt organizations with Indiana reporting addresses (Cell 3 in Figure 1). Many researchers overlook these organizations because they are not aware that such organizations exist or because they assume that those without formal tax-exempt status are unimportant. Indeed, it may be difficult to obtain access to non-registered organizations, but researches should understand why these organizations are not IRS-registered and what their characteristics are before concluding that they can—or should—be ignored.

Nonprofit Survey

We present the results of several small telephone surveys of Indiana nonprofits drawn from the subset of nonprofits included on the 2005 comprehensive Indiana nonprofit database as incorporated nonprofits but not identified as IRS-registered nonprofits with Indiana reporting addresses. Because congregations and similar organizations are exempt from IRS-registration, we exclude some 3,600 organizations that are not IRS-registered but incorporated AND included on yellow page listings of churches, congregations, mosques, and temples.

We drew small random samples of nonprofits from each of three categories of nonprofits with active incorporation status in 2005: those with state incorporation dates prior to 1990 ("older"), those with state incorporation dates between 1990 and 2003 ("middle-aged"), and those with state incorporation dates after 2003 ("younger") to see whether there are systematic differences among those three age groups. In addition, because some nonprofits may fail to maintain active incorporation status,[18] we drew two other samples of those not registered with the IRS: nonprofits listed as inactive on the state incorporation listing in 2001 when the first database was compiled, but which had become active again by 2005 ("resurrected"), and nonprofits listed as administrative inactive on the state incorporation listing in 2005 ("currently inactive"). For the latter two groups of organizations we wanted to understand the conditions under which they became inactive and, in case of the "resurrected" group, resumed active status. In all, we drew random samples of approximately 100 nonprofits from each of the respective pools of eligible nonprofits and interviewed 25 in each pool. For a more complete description of our survey methodology, see the Technical Appendix.

Survey Findings

We focus first on the four groups with active incorporation status with the Indiana Secretary of State in 2005 to discover which of the reasons proposed earlier (statutory, technical/methodological, or compliance) best explains why such nonprofits appear to be absent from the IRS list of exempt organizations. To do so, we draw on questions in the survey that asked respondents to describe the organization's mission, when it was established, its total revenues, and whether it was formally affiliated with another organization or used a fiscal agent.

Omissions for statutory reasons. For nonprofits incorporated in Indiana but not identified as IRS-registered in the 2005 Indiana database, some 76% fit the statutory omission category (see Table 1). They had revenues of less than US $5,000 (48%), were churches (14%), subsumed under the registrations of headquarter organizations or fiscal agents (30%), and/or not required to be registered with the IRS for other reasons (5%; in one case, the organization was denied IRS status).[19] The percentage with statutory reasons ranged between 60% for the "younger" group to 64% for the "resurrected" group, 72% for the "older" group, and 88% for the "middle-aged" group.

Omissions for technical or methodological reasons. Another 12% appear to fit the technical or methodological omission category exclusively (see Table 1).[20] They use fiscal agents outside the state of Indiana (1%) or had recent ruling dates (9%). The latter was primarily the case for the "younger" group, with more than one third (36%) falling into that category. Only two organizations (2%) appear to represent errors by the database research team in correctly identifying the organizations as IRS-registered in 2005.

Omissions for compliance reasons. Finally, we identified nine organizations that seem to fit exclusively the compliance omission category in that they appear to meet requirements for IRS-registration (e.g., do not fit statutory exclusion criteria) but had not done so and did not seem to be excluded for technical reasons (another two also met the technical or methodological reasons). We had too little information from the final three organizations to identify reasons why they were not identified as IRS-registered on the 2005 Indiana nonprofit database.

Validation of formal status. Because we were concerned about errors by the database research team and why those errors might have been made, we asked respondents whether the database team had correctly identified their organization as not registered with the IRS. We then made special efforts to verify the IRS status of the responding organizations, using other information from the survey (e.g., employer identification numbers, alternate names, affiliations). Tables 2 and 3 show that there are some notable differences in the organizational characteristics between those who reported themselves to be IRS-registered (Table 2) and those that said they were not IRS-registered or were not sure (Table 3).

As Table 2 shows, of the 40 organizations that claimed IRS status we confirmed IRS status for more than half (53%), ranging from 33% of old and middle-aged nonprofits to 75% of younger ones. Nearly half of those claiming IRS status have revenues of US$5,000 or more (ranging from 33% for the "old" group to 56% for the "young" group). In addition, 75% said they receive donations from the general public, members, business, or foundations, ranging from half of the "middle-aged" group to all in the "young" group.

Table 3 summarizes characteristics of those not claiming IRS status by incorporation date. In all, 43 organizations said they were not registered with the IRS and another 17 were not sure, for a total of 60 organizations. We were able to confirm that six actually

Table 1. Reasons for Organizations Not on the IRS Listing, Mutually Exclusive: Grouped by Incorporation Date

		Statutory reasons	Technical reasons	Compliance reasons	Don't know	Total	Statutory reasons (%)	Technical reasons (%)	Compliance reasons (%)	Don't know (%)	Total (%)
Old	(N = 25)	20	1	2	2	25	80	4	8	8	100
Middle	(N = 25)	22	0	3	0	25	88	0	12	0	100
Young	(N = 25)	15	9	1	0	25	60	36	4	0	100
Resurrected	(N = 25)	19	2	3	1	25	76	8	12	4	100
Total	(N = 100)	76	12	9	3	100	76	12	9	3	100

Note: Number and percentage reported in this table are mutually exclusive for each category of the reasons why nonprofits are not on the IRS listing. An organization that is classified in the Statutory Reasons will not be classified into the Technical or Compliance Reasons. An organization that is classified in the Technical Reasons will not be in the Statutory or Compliance Reasons.

Table 2. Characteristics of Self-Reported as IRS-Registered Nonprofits: Grouped by Incorporation Date

	Old (1) ($N = 9$)	Middle (2) ($N = 6$)	Young (3) ($N = 16$)	Resurrected (4) ($N = 9$)	Total (5) ($N = 40$)	Old (%) (6) ($N = 9$)	Middle (%) (7) ($N = 6$)	Young (8) ($N = 16$)	Resurrected (%) (9) ($N = 9$)	Total (%) (10) ($N = 40$)
A. Confirmed IRS status										
Organizations with confirmed EIN	3	2	12	4	21	33	33	75	45	53
Organizations with no confirmed EIN	6	4	4	5	19	67	67	25	56	48
B. Nonprofit affiliation status										
Local subsidiary or affiliate of other NP	4	3	0	2	9	44	50	0	22	23
Uses another nonprofit as fiscal agent	1	0	2	0	3	11	0	13	0	8
C. IRS status anticipated										
Plans to seek IRS registration	—	—	—	—	—	—	—	—	—	—
D. IRS subsection status										
Receives donations from the general public, members, business or foundations	6	3	16	5	30	67	50	100	57	75
Church, congregation, or similar organization	2	1	3	1	7	22	17	19	11	18
Membership association (serving own members)	3	1	4	4	12	33	17	25	44	30
E. Annual revenues										
Revenues above US$5,000	3	3	9	4	19	33	50	56	44	48
Revenues less than US$5,000	5	2	6	5	18	56	33	38	56	45
Missing	1	1	1	0	3	11	17	6	0	8
All	9	6	16	9	40	100	100	100	100	100

Note: IRS = Internal Revenue Service; EIN = employer identification number.

Table 3. Characteristics of Self-Reported as Not IRS-Registered Nonprofits: Grouped by Incorporation Date

	Old (1) ($N = 16$)	Middle (2) ($N = 19$)	Young (3) ($N = 9$)	Resurrected (4) ($N = 16$)	Total (5) ($N = 60$)	Old (%) (6) ($N = 16$)	Middle (%) (7) ($N = 19$)	Young (%) (8) ($N = 9$)	Resurrected (9) ($N = 16$)	Total (%) (10) ($N = 60$)
A. Confirmed IRS status										
Organizations with confirmed EIN	1	3	0	2	6	6	16	0	13	10
Organizations with no confirmed EIN	15	16	9	14	54	94	84	100	88	90
B. Nonprofit affiliation status										
Local subsidiary or affiliate of other NP	3	6	6	6	21	19	32	67	38	35
Uses another nonprofit as fiscal agent	1	2	2	1	6	6	10	22	6	10
C. IRS status anticipated										
Plans to seek IRS registration	4	2	4	3	13	25	11	44	19	22
D. IRS subsection status										
Receives donations from the general public, members, business or foundations	9	7	4	8	28	56	37	44	50	47
Church, congregation, or similar organization	2	1	3	1	7	13	5	33	6	12
Membership association (own members)	14	12	1	11	38	88	63	11	69	63
E. Annual revenues										
Revenues above US$5,000	4	1	4	6	15	25	5	44	38	25
Revenues less than US$5,000	8	16	5	6	35	50	84	56	38	58
Missing	4	2	0	4	10	25	11	0	25	17
All	16	19	9	16	60	100	100	100	100	100

Note: IRS = Internal Revenue Service; EIN = employer identification number.

were registered with the IRS. Two registered with the IRS very recently and the rest are affiliated with national organizations outside Indiana. Overall, about a quarter of nonprofit agencies that say they are not registered with the IRS have revenues of US$5,000 or more (ranging from 5% of those in the "middle" group to 44% in the "young" group) and almost half receive donations (ranging from 37% of the "middle-aged" group to 56% of the "old" group. A little more than a fifth said they were planning or at least thinking about seeking IRS status, ranging from 11% of the "middle-aged" group to 44% of the "young" group.

Inactive organizations. Our survey of the 25 "resurrected" and 25 "currently inactive" nonprofits reveals that some nonprofits may be quite fragile. The reasons why many "resurrected" nonprofits failed to maintain active incorporation status include their inability to secure volunteer leadership, failure of expected resources to materialize, problems of keeping organizations going during periods when there are no activities (e.g., between episodic events such as festivals or athletic games), or failure to file the necessary paperwork. Similarly, among the 25 "currently inactive" nonprofits that we were able to reach, six told us that they no longer operate because key leadership or volunteers left the organization and no replacements could be found. Two others explained that expected resources failed to materialize, four merged with other entities, and four stopped operating because there was no demand for or interest in their services.

Discussion

As this analysis shows, it is not a simple matter to sort out the reasons why some well-established nonprofits—at least as indicated by incorporation status—do not appear to be registered with the IRS. In some cases, there are "good" reasons why they are not IRS-registered—they are subsumed under the status of a fiscal agent, churches, or too small to require registration, or membership associations that are not eligible to receive tax deductible contributions and therefore have had few occasions to experience the need for IRS-registration.

Table 4 summarizes our findings. We find that some nonprofits do not know their legal status. When asked whether they were incorporated with the Indiana Secretary of State, almost one fifth was uncertain: 12% didn't know if they were incorporated and 6% thought they were NOT incorporated, even though all were. Moreover, 40% in the four samples with active incorporation status reported themselves to be registered with the IRS even though they were not so identified on the 2005 nonprofit database. In some cases, they are indeed registered but use reporting addresses elsewhere and therefore do not appear when researchers select just those that use reporting addresses in a given region.

The fact that we could only confirm 27 out of 40 nonprofits that claim IRS registration raises important questions for the researcher. We don't know if we could not confirm their the IRS listing because we were given inaccurate registration numbers by respondents, the electronic listings from the IRS contain key-punching errors for the EIN field, or respondents confused IRS exempt registration with exemption from state taxes[21] or

Table 4. Self-Reported as State Incorporation, IRS-Registered, and IRS Status Verification: Grouped by Organizations Incorporated prior to 1990 ("Old"), between 1990 and 2003 ("Middle"), and after 2003 ("Young") and ("Resurrected")

		Self-reported as Indiana Incorporation			Self-reported as IRS registered			Organizations with confirmed EIN	
		Yes	No	Not Sure	Yes	No	Not Sure	Yes	No
Old	(*N* = 25)	23	1	1	9	7	9	4	21
Middle	(*N* = 25)	23	2	0	6	16	3	5	20
Young	(*N* = 25)	19	1	5	16	8	1	12	13
Resurrected	(*N* = 25)	17	2	6	9	12	4	6	19
Total	(*N* = 100)	82	6	12	40	43	17	27	73

Note: IRS = Internal Revenue Service; EIN = employer identification number.

status as a not-for-profit incorporation with the state of Indiana. Possibly, they may have been registered as exempt entities at one point but removed from the IRS listing during one of the occasional purges of the IRS Business Master File because they did not respond to an inquiry from the IRS.

Similarly, our finding that some nonprofits for which we could confirm IRS status are subsidiaries of other nonprofits or use other nonprofits as fiscal agents, also have important research implications. In several cases, headquarter organizations or fiscal agents are located outside the state. Because the Indiana database included only those IRS-registered nonprofits that have Indiana reporting addresses, such "out-of-state" organizations would not have been captured in the database. Not only does this explain why they appear to be not IRS-registered in the database but it also confirms the importance of taking the known geographic bias in the IRS listing into account when seeking to do research on nonprofits at the subnational level.

Finally, we find support for another technical reason why nonprofits may not appear on the IRS registration list. For those in the "younger" group, it is possible that the database research team did not find them on the 2005 IRS registration list simply because of timing issues. Thus IRS regulations specify that as long as an organization files its application within 27 months from the end of the month in which it was created, the exemption (and hence the ruling date) will be retroactive to the founding date. In addition, information on the IRS Web site in July 2008 indicates that applications for exempt status received in February of 2008 were only then (5 months later) being assigned to an Exempt Organizations Specialist,[22] down from nine months several years prior (S. Deja, personal communication, January 14, 2008). It then takes more time for the IRS to process applications, especially if there are problems or questions, and add entities to the BMF.

Indeed, the average number of days from submission to final ruling was 134 days in October 2006 (National Taxpayer Advocate, 2008, p. 213) and an informal survey of legal experts participating in the “Charitylaw” forum (www.CharityChannel.com) suggests that it may take a year or more from when an application is filed to when it is approved (S. D. Smith, personal communication, January 14, 2008). Given such delays, it is possible that the IRS ruling date for at least some “younger” nonprofits could date back to 2003 or even earlier, but not be included on the IRS listing by 2005 when the Indiana segment of the BMF listing was added to the Indiana nonprofit database.

Conclusion

The results of this analysis help advance our understanding of the dimensions of the nonprofit sector and should prove useful for researchers concerned about the grey fringes of the nonprofit universe when assessing the scope of the nonprofit sector at a local, state, or national level. As we show, there appears to be growing overlap between the lists of IRS-registered nonprofits and state incorporated nonprofits, at least in Indiana—up from 23% in 2001 to 33% in 2005. Thus the relative advantages of one list over the other are diminishing (although certainly not eliminated). Moreover, that trend may be accelerating, because nonprofits registered with the IRS since 2000 have the highest incorporation rate. However, limiting the analysis to IRS-registered nonprofits will overlook not only some young organizations, many community associations, and about half of the churches but also a substantial number of nonprofits that are formal enough to have obtained incorporation status

In the second part of our empirical analysis, we sought to get a more in-depth understanding of this latter group—those at the dark grey fringes of the nonprofit universe. We randomly selected nonprofits that differed on when they were incorporated and whether their incorporation status had been declared administratively inactive. Our small survey reveals that statutory reasons characterize about 76% of the omissions, with technical omissions a distant second (12%)—mainly use of fiscal agents or affiliated organizations located elsewhere or recently obtained official IRS rulings. Finally, only 9% appeared to meet the criteria for IRS registration but had failed to obtain such status, or at least had not done so yet.

There are also important policy reasons for considering the “grey” matter of the nonprofit universe, quite apart from regulatory concerns to protect charitable funds (Fremont-Smith, 2004). Those we surveyed serve youth, care for the elderly, represent minority groups, and watch neighborhoods. Other studies of grassroots associations and nonregistered nonprofits suggest they make significant contributions to arts and culture (Toepler, 2003), local advocacy, and promotion of political participation (Smith, 1997). Many are closely aligned with the values of founders and community needs outside of mainstream culture and reflect a diversity of ideologies and communities. Some—relatively few based on our findings—fail to manage the necessary legal processes because of limited capacity—they lack knowledgeable staff or financial resources or simply don’t know what is required—raising important questions about what will happen to those with IRS-registrations now that all exempt entities must report annually.

We hope our analysis assists researchers to make informed decisions about which data sources to use for examining the dimensions of the nonprofit sector at a local, state, or national level. There are not only major advantages to using the IRS list of exempt entities but also important limitations; the same holds for lists of state incorporated nonprofits. Researches should familiarize themselves with the strengths and weaknesses of all available nonprofit data and select the one (or combination of several) that best fits the research questions or focus of the analysis.

Appendix

Sample Selections

Our small telephone survey focused nonprofits drawn from the subset of nonprofits included on the 2005 comprehensive Indiana nonprofit database that were identified as incorporated with the Indiana Secretary of State but which the database research team had not been able to verify as appearing on the list of IRS-registered nonprofits with Indiana reporting addresses. We drew five small random samples of nonprofits from those registered with the IRS, stratified by date of incorporation and inactive status in 2001 and 2005:

1. "Older": nonprofits with state incorporation dates prior to 1990 and active status in both 2001 and 2005;
2. "Middle-aged": nonprofits with state incorporation dates between 1990 and 2003 1990 and active status in both 2001 and 2005;
3. "Younger": nonprofits with state incorporation dates after 2003;
4. "Resurrected": nonprofits listed as administrative inactive on the state incorporation listing in 2001 when the first database was compiled but which had become active again by 2005; and
5. "Currently inactive": nonprofits listed as administrative inactive on the state incorporation listing in 2005.

For each group, we drew a random sample of approximately 100 organizations from the pool of eligible nonprofits (The actual samples were respectively 109 for the "older" group, 99 for the "middle-aged" group, 99 for the "younger" group, 98 for the "resurrected" group, and 108 for the "currently inactive" group).

Phone Interviews

For the sampled organizations, we used information in the database, supplemented by the Web (phone directories, Google, Guidestar, NCCS Dataweb, IRS list of registered charities) and other sources to contact the organizations by phone or email. In all, we contacted 513 organizations at an average of 1.8 times per organization (varying the day of the week and time of day) until we had reached our quota of 25 respondents from each sample. Of the 513 organizations, 32% have disconnected or wrong phone

(continued)

Appendix (continued)

numbers and no other contact information could be located. We attempted to contact, but did not obtain information from another 31% of the organizations for other reasons (never heard back, or we reached our quota), whereas 6% refused to participate. We were able to confirm that 7% of the 513 organizations are no longer in existence (including most of the "currently inactive" group).

We conducted a short telephone survey of those we could locate and who were willing to answer our questions. We explained the purpose of the survey as part of an effort to assess the quality of work undertaken to update the database in 2005 and promised respondents full confidentiality. For those with active incorporation status as of 2005, we first asked each organization to confirm its name and address and its status as incorporated with the Indiana Secretary of State. We then asked whether the research team was correct in listing the organization as not registered with the IRS. If the answer was no, we requested the organization's EIN number and asked whether the organization might be subsumed under the registration of another organization (e.g., a fiscal agent or headquarter organization).

For all active nonprofits we also asked when the organization was established, its total revenues, primary mission, whether it received contributions from the public, and whether it was religiously affiliated to determine whether these factors might provide plausible explanations for why it is not registered with the IRS. For those that no longer had active incorporation status, we focused on the reasons why the organization had allowed its incorporation to become inactive.

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Notes

1. Exempt entities with US$25,000 or more in total revenues are generally required to file IRS Form 990, unless they are included in a group exemption of a headquarter organization or in a Form 990 submitted by a nonprofit that acts as its fiscal agent.
2. The current IRS Business Master File (BMF) contains 1.6 million organizations, including about 1 million charities. However, only about 40% of charities file IRS Form 990, so reliance on charitable filers excludes the majority of registered nonprofits. Moreover, nonfilers are not all small—analysis of all IRS-registered nonprofits in the United States that also participate in the quarterly Covered Employment and Wages Survey of Indiana establishments shows that 292 of 6,304 responding Indiana nonprofit establishments (churches and nonprofits with less than 4 employees are not required to participate in the survey) did not file Form 990 (defined as having zero revenues or zero assets on the BMF). These "non-filer" establishments reported more than 9,200 employees and total annual payroll of more than US$227 million in 2005, or almost 35 employees and US$868,000 payroll on average (about US$24,400 per employee). See Grønbjerg, Lewis, and Campbell (2007, p. 124).
3. Thus a 2002 comprehensive survey of Indiana nonprofits found that 7% of responding organizations (including churches) reported no revenues at all and another 22% had revenues of less than US$5,000—the threshold for IRS registration (Grønbjerg & Allen, 2004).
4. For Form 1023 (application as exempt entity under subsection (c)(3)—for example, charities), question 11 asks for "Date incorporated if a corporation, or formed, if other than a corporation" (the instructions for Form 1023 note that "sole proprietorships, partnerships, or loosely affiliated groups of individuals are not eligible.") For Form 1024 (application as exempt entity under other subsections), question 8 asks whether the organization is a corporation, trust, or association. (See http://www.irs.gov/pub/irs-pdf/k1024.pdf and http://www.irs.gov/pub/irspdf/f1023.pdf, retrieved June 29, 2008). Similarly, IRS guidelines on the "Life Cycle of Exempt Organizations" include under Step 1 "creating an organization under state law" (see http://www.irs.gov/charities/article/0,,id=169727,00.html, retrieved June 29, 2008). However, Hopkins noted (2007, p. 66) that an organization may be deemed a corporation for tax purposes even though it is not formally incorporated.
5. Analysis of IRS-registered nonprofits that participate in the quarterly Indiana Covered Employment and Wages Survey (also known as the ES-202 program) shows that 496 (or about 7%) of the 6,304 nonprofit establishments that participated in the survey in 2005 used IRS filing addresses outside of Indiana. See Grønbjerg, Lewis, and Campbell (2007, p. 124). This may underestimate the geographic bias because churches and charities with less than 4 employees (including presumably many local affiliates or subsidiaries) are not required to participate in the employment survey.
6. The Pension Protection Act of 2006 includes a requirement that as of 2008, all registered exempt entities, excluding congregations, must file a short annual report (Form 990-N e-Postcard) with the IRS confirming their continued existence. Those that fail to do so for 3 consecutive years will lose their exempt status.
7. The organization must request an employer identification number (EIN) from the IRS, usually at the same time (or before) it seeks tax-exempt status. Because this often occurs after nonprofits have obtained incorporation status, incorporation listings usually include only the

state's own incorporation number as an identifier. It is important to note that some nonprofits may obtain an EIN number for banking purposes (see http://www.irs.gov/pub/irspdf/fss4.pdf, retrieved January 4, 2009) without also filing Forms 1023 or 1024 to secure exempt status.

8. See http://nccsdataweb.urban.org/NCCS/Public/ (retrieved December 4, 2008 from National Center for Charitable Statistics, Public Access Web page).
9. Indeed, even nonprofit scholars are not immune from confounding incorporation status with IRS registration as exempt entities (e.g., Abzug & Turnheim, 1998).
10. Part III of the IRS Form 1023 requires those nonprofits that are incorporated to include a state filing certificate; more than three-quarters of the 501(c)(3) organizations in the 2008 IRS Business Master File are identified as corporations.
11. For example, Jenkins (2007, p. 1151) shows that 81% of the Philanthropy 400 (defined by the Chronicle of Philanthropy) are incorporated in the same state as the location of their headquarters, compared to only 30% of Fortune 500 corporations (most of which are incorporated in Delaware).
12. The Indiana Secretary of State requires nonprofits to pay US$10 for the annual registration fee and complete a two-page form (http://www.in.gov/sos/business/forms.html). Nonprofits that fail to file their annul paperwork within 65 days of their anniversary of incorporation risk administrative dissolution although the incorporation status will be reinstated when the fee is paid.
13. See http://www.quickmba.com/law/corporation/state/ for a summary of differences in state incorporation laws; see also http://topics.law.cornell.edu/wex/Non-profit_organizations (retrieved January 21, 2009).
14. For the most recent annual survey of state laws regulating charities, see Giving USA Foundation (2008).
15. Jenkins (2007, p. 1129) reported that 39 out of 49 states for which data are available have two or fewer full-time equivalent lawyers monitoring charities in the States Attorney General office. Indeed, there are few—if any—economic incentives for states to monitor nonprofit incorporation compared to business corporations, because filing fees for nonprofits are usually quite low. Also, because federal law prohibit charities from participating in political campaigns, state policy makers have few political incentives to encourage charities to incorporate in their particular state (Jenkins, 2007).
16. For the 2001 effort, the research team also included nonprofits from several supplementary listings: local listings of nonprofits in 11 communities around the state and nonprofits identified by a telephone survey of Indiana residents. The survey asked respondents to provide name and address for all nonprofits with which they had direct personal engagement during the prior 12 months as paid employees, volunteers, or participants in meetings or events. For more details, see Grønbjerg (2002).
17. There were actually 32,900 IRS registered nonprofits with Indiana reporting addresses in the July 2005 BMF, compared to 32,500 in 2001, but the team removed almost 2,800 IRS registered entities that had either filed corporate dissolution reports with the Indiana Secretary of State or were designated as inactive on the incorporation listing on the assumption that they have ceased to operate and remained on the IRS listing by oversight.
18. For 2005, about 6,800 nonprofits were designated as administratively inactive by the Indiana Secretary of State. They have been excluded from the analysis presented above.
19. The percentages reported in this table are not mutually exclusive for each subcategory of the reasons why nonprofits are not on the IRS listing.

20. Overall, however, 30% actually fit the technical or methodological omission category, but most of these (18 out of 30) also fit the statutory omission category.
21. We have recently received a list of 27,700 organizations exempt from state taxes from the Indiana Department of Revenues, one third of which are not on the current IRS Business Master File.
22. See http://www.irs.gov/charities/article/0,,id=156733,00.html (retrieved July 7, 2008). Experts in exempt tax law report that about half of all applications are "merit closed." This means that the Screener (usually a more experienced agent) spends relatively short time reviewing the application, so that the approval letter goes out in 60 to 90 days (S. Deja, personal communication, January 14, 2008).

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