Tax Expenditure Analysis and Constitutional Decisions

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Articles

Tax Expenditure Analysis and Constitutional Decisions

by
LINDA SUGIN*

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Introduction

In his 1996 State of the Union Address, President Clinton declared: "The era of big Government is over."¹ By that, he meant that the government would no longer implement its policy goals through massive federal spending programs. What he did not say was that, as a result, federal policy would be increasingly dependent on indirect funding.²

The Internal Revenue Code (hereinafter "Code"), at least in the eyes of the President and Congress, has apparently become the vehicle of choice for disbursing government funds.³ Congressionally imposed restrictions on direct government expenditures, in particular the pay-as-you-go provisions in the Budget Enforcement Act of 1990, have significantly contributed to this trend.⁴ In 1998, the federal government spent more money through the Code than through the discretionary appropriations process.⁵ The tax law’s traditional revenue-raising function is being eclipsed as it becomes a principal tool of federal policy.

Policymakers and scholars have long recognized that direct spending programs and tax subsidies can be economically equivalent.⁶ The Code can provide a subsidy by authorizing taxpayers to keep part

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¹ President’s State of the Union Address, 1996-1 PUB. PAPERS 79 (Jan. 23, 1996).
² Many of the government’s goals are now accomplished by encouraging private citizens and corporations to engage in particular activities and support certain causes in exchange for substantial tax reductions. Indirect funding of federal policies also comes from sources outside the federal government, for example, in the form of unfunded mandates and regulation of private activity.
⁵ The Office of Management and Budget (hereinafter “OMB”) estimated that the federal government spent approximately $553 billion in appropriations and $566 billion by foregoing tax revenue. These numbers do not include amounts that the government spent on social security, Medicare, Medicaid and interest on the national debt. The estimated total outlay for 1998, including discretionary and mandatory spending was $1,693.4 billion. See ANALYTICAL PERSPECTIVES, BUDGET OF THE UNITED STATES GOVERNMENT, FISCAL YEAR 1998, at 249 [hereinafter ANALYTICAL PERSPECTIVES]. Five hundred sixty-six billion dollars was the total in the revenue loss portion of the OMB’s Tax Expenditure Budget. See id. at 73-75.
of the tax they would otherwise owe to the government. The mechanisms for tax-based subsidies are exclusions, deductions, and credits. Exclusions operate as subsidies to the extent of the foregone tax, equal to the taxpayer's marginal rate applied to the excluded amounts. Examples of such exclusions are the exclusion from gross income of housing allowances received by ministers, the exclusion from employee income of the cost of employer-provided health insurance, and the exclusion of de minimis fringe benefits. Like exclusions, deductions operate as subsidies to the extent of the foregone tax, equal to the taxpayer's marginal rate applied to the deductible amount. An example of a deduction that operates as a subsidy to the extent of the taxpayer's marginal rate is the deduction allowed for home mortgage interest, I.R.C. §163(h). Unlike exclusions and deductions, tax credits operate as subsidies to the full extent of the dollar amount of the credit. An example of a credit that operates as a subsidy is the HOPE educational credit, which allows taxpayers to offset their tax liability by a portion of their educational expenses. While these three mechanisms operate differently, each one allows the taxpayer to reduce the tax liability she would have had in the absence of the provision.

Every year the government publishes a "tax expenditure budget," which, like the official federal budget, quantifies government funds "spent" (according to tax expenditure theory) as a result of exclusions, deductions and credits contained in the Code. The tax expenditure budget identifies only certain provisions of the Code as equivalent to spending programs; it excludes so-called "structural" tax provisions. A provision is structural, the theory holds, if it exists to accurately measure "income." Structural provisions are not "tax expenditures," and are not considered

10. I.R.C. § 25A.
11. In fact, it publishes two. The OMB publishes one and the Joint Committee on Taxation publishes the other. See ANALYTICAL PERSPECTIVES, supra note 5, at 71-98; JOINT COMMITTEE ON TAXATION, ESTIMATES OF FEDERAL TAX EXPENDITURES FOR FISCAL YEARS 1998-2002, TAX NOTES TODAY, Dec. 15, 1997, available in WESTLAW, 97 TNT 241-44 [hereinafter JOINT COMMITTEE BUDGET]. The Joint Committee's tax expenditure list is similar, but not identical to the list prepared by the President's office. See JOINT COMMITTEE BUDGET, supra, paras. 56-60 (describing differences between OMB and Joint Committee budgets).
12. For example, the deduction allowed for ordinary and necessary business expenses under Code section 162 is a structural provision because it allows taxpayers to deduct the costs of producing income in determining net income subject to tax. It would be possible to quantify the revenue that could be raised from repealing structural provisions of the Code.
equivalent to spending programs under tax expenditure theory.\textsuperscript{13} However, as will be discussed, distinguishing structural provisions from tax expenditures has been the source of considerable controversy.\textsuperscript{14}

The basic insight of tax expenditure analysis is very simple: there is no economic distinction between the government's direct subsidy of an activity or institution and its grant of an equivalent tax break for that activity or institution. When the government fails to tax, it is expending resources just as surely as when it sends a check. Proponents of tax expenditure analysis maintain that the economic equivalence of tax expenditures and direct expenditures requires that there should not be any legal distinction between them.\textsuperscript{15} They would subject tax expenditures to the full panoply of constitutional and statutory restrictions on government spending. I will refer to this approach as the "strong version" of tax expenditure analysis. Proponents of this view ask: From a constitutional standpoint, why should it matter whether the government directly funds religious schools or gives a tax break to parents for tuition to such schools? Put this way, the argument is appealingly simple. Opponents have claimed that the tax expenditure concept is not useful. Some have argued that it lacks a normative foundation,\textsuperscript{16} others that the impossibility of determining precisely what should be included in the tax expenditure budget undermines its value,\textsuperscript{17} and still others that it relies on the absurd notion that the government is entitled to all of a taxpayer's money.\textsuperscript{18}

\begin{itemize}
  \item \textsuperscript{13} See \textsc{Stanley S. Surrey, Pathways to Tax Reform} 17 (1973) [hereinafter \textsc{Surrey, Pathways}]; \textsc{Stanley S. Surrey \& Paul R. McDaniel, Tax Expenditures} 3 (1985) [hereinafter \textsc{Surrey \& McDaniel, Tax Expenditures}].
  \item \textsuperscript{14} See Part I.B. infra.
  \item \textsuperscript{15} See \textsc{Surrey \& McDaniel, Tax Expenditures}, supra note 13, at 118-19; Donna D. Adler, \textit{The Internal Revenue Code, the Constitution, and the Courts: The Use of Tax Expenditure Analysis in Judicial Decision Making}, 28 \textsc{Wake Forest L. Rev.} 855 (1993).
  \item \textsuperscript{17} See Boris I. Bittker, \textit{Accounting for Federal "Tax Subsidies" in the National Budget}, 22 \textsc{Nat'L Tax J.} 244 (1969) [hereinafter Bittker, \textit{Tax Subsidies}]. The debate over the tax expenditure concept has pitted two of the greatest tax scholars against one another, Stanley Surrey in favor, see \textsc{Surrey, Pathways}, supra note 13; \textsc{Surrey \& McDaniel, Tax Expenditures}, supra note 13; Stanley S. Surrey \& William F. Hellmuth, \textit{The Tax Expenditure Budget—Response to Professor Bittker}, 22 \textsc{Nat'L Tax J.} 528 (1969), and Boris Bittker against, see Bittker, \textit{Tax Subsidies}, supra; Boris I. Bittker, \textit{The Tax Expenditure Budget—A Reply to Professors Surrey \& Hellmuth}, 22 \textsc{Nat'L Tax J.} 538, (1969) [hereinafter Surrey \& Hellmuth]. Undoubtedly they are both right.
\end{itemize}
The Supreme Court rekindled interest\textsuperscript{19} in the constitutionalization of tax expenditure analysis\textsuperscript{20} with its 1996 decision in \textit{United States v. Virginia (VMI)}.\textsuperscript{21} VMI raises the very question at the heart of the tax expenditure debate: Should economically equivalent government support be treated as legally equivalent? In \textit{VMI}, the Supreme Court decided that Virginia's policy of admitting only men to the Virginia Military Institute—a state-operated and state-funded institution—violated the equal protection clause of the Constitution.\textsuperscript{22} The implications of the \textit{VMI} decision depend upon how one views government support for private single-sex education. If \textit{VMI} means that the government is barred from participating in any way in single-sex education, then the public support—including tax-based support—that flows to private single-sex schools would be constitutionally suspect.\textsuperscript{23} Proponents of tax expenditure analysis argue that tax-based support is functionally equivalent to direct government spending, and should therefore be constitutionally equivalent.\textsuperscript{24} Indeed, they believe that this conclusion is a "matter of logical necessity."\textsuperscript{25} Judicial adoption of tax


\textsuperscript{20} The Supreme Court has been reticent to adopt tax expenditure analysis as a basis for constitutional decisionmaking, despite repeated invitations. The Court has shown that it clearly understands the economic equivalence of tax subsidies and direct subsidies. See Committee for Public Educ. & Religious Liberty v. Regan, 444 U.S. 646 (1980); Committee for Public Educ. & Religious Liberty v. Nyquist, 413 U.S. 756 (1973); Walz v. Tax Comm'n, 397 U.S. 664, 690 (1970) (Brennan, J., concurring).

\textsuperscript{21} 518 U.S. 515 (1996).

\textsuperscript{22} \textit{Id.} at 534. The majority declared that the state would be required to furnish an "exceedingly persuasive justification" for government action that differentiates on the basis of gender. \textit{Id.} at 531.

\textsuperscript{23} Government support flows to private schools in many ways, including, for example, funds under Title IX, Civil Rights Act of 1972, § 901, 20 U.S.C. § 1681 et seq. (1994) (requiring a "sex blind" approach to funding and decisions in educational institutions), government guaranteed loans to pay student tuition, and tax benefits in various forms. The exemption from tax allowed to gender-segregated institutions under Code section 501(c)(3) does not clearly provide an economic benefit to those schools because even without the exemption, they might not have any taxable income.

\textsuperscript{24} See SURREY, PATHWAYS, \textit{ supra} note 13, at 40; SURREY & MCDANIEL, TAX EXPENDITURES, \textit{ supra} note 13, at 118-19.

\textsuperscript{25} Bernard Wolfsman, \textit{Tax Expenditures: From Idea to Ideology}, 99 HARV. L. REV.
expenditure analysis could mean that the VMI decision directly dictates the treatment of tax-based support to private single-gender institutions. If state financial support (not just state operation of the university) made VMI vulnerable, then the deductibility of contributions to such single-sex schools as Smith and Wellesley would also be unconstitutional.

This Article reveals the complexity underlying judicial application of tax expenditure analysis. It adopts what I call a "qualified version" of tax expenditure analysis: it applauds the important lessons of tax expenditure analysis for policymaking and accepts the economic equivalence of certain tax provisions and direct spending programs and the analytic prescriptions for legislatures that flow from that equivalence; however, it finds that the strong version of tax expenditure analysis gives economic equivalence too much normative force, and that courts have only limited use for the tax expenditure budget in legal analysis.

My critique of the strong version of tax expenditure analysis is based on two points: (1) it imposes inappropriate restraints on adjudication and improperly reduces judicial scrutiny of provisions that are not classified as tax expenditures, and (2) it gives tax

491, 495 (1985) (reviewing SURREY & MCDANIEL, TAX EXPENDITURES).

26. Justice Rehnquist's opinion in VMI provides some support for the argument that the fact of economic support is itself of constitutional importance. He considered the state's role in funding VMI to be a key element of the constitutional violation and believed that the state's substantial underfunding of the proposed parallel women's institution prevented Virginia's suggested remedy from satisfying constitutional requirements. United States v. Virginia, 518 U.S. 515, 566 (1996) (Rehnquist, C.J., concurring in the judgment).

27. Of course, in order to conclude that deductions for contributions to Smith and Wellesley are unconstitutional after VMI, one must equate tax-based economic support not merely with financial support but with public operation of a large and complex institution. Only if the tax laws place the federal government in the same position vis-à-vis private sex-segregated schools as was the state of Virginia with respect to public single-sex education would VMI's precedent directly control the tax benefits. Nevertheless, tax expenditure analysis places tax provisions on a par with direct government operation such that their constitutionality depends on the distinction between funding and operation. If this distinction is the source of VMI's constitutional defect, Virginia could cure the defect by transferring formal control to a private group while continuing full state funding. The courts have never held that tax-based support is equivalent to direct government operation of an institution, and as discussed more fully below, evidence of government intent to discriminate differs greatly for tax-based support compared to direct government operation. Government intent to discriminate is necessary for a violation of the equal protection clause. See infra Part II.B.

28. By "economic equivalence," I mean that a recipient receives the same monetary benefit from a tax program and a direct spending program. I do not mean that the tax and spending programs are identical in every respect. If they are, then they could not have different legal statuses under the analysis I propose. I am concerned with programs that have the same economic effect, but are carried out differently.
expenditures the same legal consequences as economically equivalent direct-spending programs, even where the legal standard does not depend on economic equivalence. Part I identifies the drawbacks of separating structural, income-defining provisions of the Code from tax expenditure provisions for purposes of judicial review. Part II explains why tax expenditures should not always be constitutionally equivalent to direct-spending programs with the same economic effect. Economic equivalence is only one factor in the evaluation of a tax provision; other factors may be more important to the constitutional standard.

This Article looks at the significance of the similarities and differences between tax benefits and direct spending for purposes of the equal protection and establishment clauses, with a particular focus on the charitable contribution deduction. Because economic equivalence is not critical under these constitutional provisions, tax expenditure analysis is not relevant to the legal analysis. While this Article deals only briefly with numerous provisions of the Code and analyzes only two constitutional provisions, it provides a model for considering the constitutionality of any tax provision.

The Article begins by defending the qualified version of tax expenditure analysis, explaining how tax expenditure analysis is well suited to legislatures but not to courts. The definitional difficulties inherent in the tax expenditure concept, and the political manipulability of the tax expenditure budget make tax expenditure analysis too unreliable for constitutional adjudication, even while it provides relevant information to legislatures. The strong version of tax expenditure analysis would constitutionalize the definition of income and thereby reduce judicial scrutiny of income-defining tax provisions. Structural provisions, as well as tax expenditures, may violate constitutional norms, a possibility ignored in most discussions of the constitutionality of tax provisions. In addition, the hybrid nature of the federal income tax presents an external challenge to the theoretical underpinnings of the tax expenditure concept.

30. Proponents of the strong version of tax expenditure analysis believe that allowing tax expenditures where economically equivalent direct spending programs would be constitutionally prohibited elevates form over substance and allows the government to achieve indirectly what it may not achieve directly. However, these proponents are correct only if the fact of economic support is constitutionally decisive, which it is not under the constitutional provisions examined in this Article.
31. Two constitutional provisions are more than enough for one tax professor.
32. See, e.g., SURREY & MCDANIEL, TAX EXPENDITURES, supra note 13; Adler, supra note 15; Victor Thuronyi, Tax Expenditures: A Reassessment, 1988 DUKE L.J. 1155; Zelinsky, supra note 19.
33. Our federal income tax contains many elements of a consumption tax. See infra
Turning from the institutional drawbacks of wholesale judicial adoption of the strong version of tax expenditure analysis, Part II describes my proposed methodology for examining the constitutionality of tax benefits. Because of the importance of government intent under the equal protection and establishment clauses, the Article describes a model for determining government intent in tax provisions, explains how to classify and evaluate different types of tax provisions, and considers the separability of government intent from taxpayer intent. Because the equal protection analysis centers on the intent question and tax-based aid to discriminatory private organizations is accomplished by means of broad, entitlement-like provisions, I conclude that tax-based aid that flows to discriminatory private organizations under the charitable contribution deduction is constitutional. Consequently, VMI does not jeopardize the deductibility of contributions to Smith College. Unfortunately, the tax-deductibility of contributions to racially discriminatory organizations such as Bob Jones University may be no more constitutionally suspect than those to Smith.35

To address the possible absence of a constitutional impediment to tax-based support for an organization that racially discriminates, the Article considers how the analysis of tax provisions might differ under interpretations of the equal protection clause that have not been embraced by the Supreme Court. It concludes that any understanding of the equal protection clause that focuses on the effects of tax-based support, rather than government intent, would require that courts treat tax benefits and economically equivalent direct spending programs the same, along the lines advocated by proponents of the strong version of tax expenditure analysis. Comparing the analysis of tax-based aid under the Supreme Court’s current interpretation of the equal protection clause with competing interpretations illustrates my basic thesis about the applicability of tax expenditure analysis to constitutional adjudication: the substantive interests embodied in the constitutional provision determine the

Part I.D.

34. The IRS revoked Bob Jones University’s tax exemption because it discriminated on the basis of race. The Supreme Court upheld the IRS’s determination on statutory grounds. See Bob Jones Univ. v. United States, 461 U.S. 574 (1983).

35. Different consequences for Bob Jones University and Smith College could arise under current law if the constitutional analysis gets past the prima facie case, and the court applies the different standards of strict and intermediate scrutiny to the government’s justification of the Code’s provision. For the charitable deduction, the constitutional case fails at the intent question, so the different standards for race and gender-based discrimination are likely to be irrelevant. Different results for Bob Jones and Smith could follow if the Supreme Court decides that race-based distinctions require a unique analysis. Cf. Shelly v. Kraemer, 334 U.S. 1 (1948).
relevance of economic equivalence to constitutional adjudication. Tax expenditure analysis is helpful only when economic equivalence is central.

The Article then analyzes tax-based aid to religious organizations by applying the same methodology and examining the substantive interests embodied in the establishment clause. In addition to prohibiting government intent to favor religion, the Supreme Court has identified other interests protected by the establishment clause that are absent in equal protection analysis. Therefore, the Article considers the problem of state entanglement with religion through the tax law, and whether tax-based support may be considered constitutionally incidental to the government's secular purpose. It concludes that taxpayer choice, taxpayer cost, and indirectness of government support may provide grounds for finding that tax-based aid to religion would be constitutional where equivalent direct aid would not. By drawing upon the Supreme Court's decision in Rosenberger v. University of Virginia,\textsuperscript{36} I argue that the Court's formalism indicates that most of the Justices are unlikely to be sympathetic to the strong version of tax expenditure analysis in establishment clause cases. Nevertheless, the Article raises some constitutional questions about the charitable contribution deduction's tax-based aid to religion.

The final section of the Article looks beyond the constitutionality of tax provisions and considers what tax policy can learn from constitutional scholarship. It questions the narrow limits of the equality norm that has traditionally been applied in tax policy discussions and suggests that the tax law offers significant untapped opportunities to advance constitutional norms.

\section*{I. Tax Expenditure Analysis, Legislatures, and Courts}

In this section, I argue that the tax expenditure budget suits Congress’ institutional needs, but is problematic if applied unreflectively as a basis for constitutional adjudication.

\subsection*{A. Institutional Needs of Legislatures and Courts}

Tax expenditure analysis has been an immensely important policymaking tool. It has invited lawmakers and citizens to look at tax provisions more fully, allowing greater understanding of the effects of the Code on the behavior of taxpayers, and the options that the legislature has when choosing to subsidize certain activities. It has given the government greater control by identifying the non-revenue raising functions that the tax law serves, and has illuminated the

\textsuperscript{36} 515 U.S. 819 (1995).
richness of the tax law by identifying the Code's central position in defining the nature of the relationship between government and citizen in both the collection and disbursement of revenue.

The tax expenditure budget has produced a taxonomy that allows us to distinguish different functions fulfilled by tax provisions, encouraging us to compare tax provisions with spending provisions. It has given a fuller accounting of how the government spends money, potentially improving government's accountability to the people, and it has been a model of analysis for many other countries.

The central lesson of tax expenditure analysis—that tax provisions perform the same function as spending provisions and should be analyzed in the same way—is a crucial lesson for legislators. For example, tax expenditure analysis challenges us to analyze the home mortgage deduction as a government spending program that subsidizes taxpayers' mortgage payments, the child tax credit as a direct government payment to families with children, and the earned income tax credit as a government-financed wage subsidy. Because one of Congress' principal functions is appropriation of funds, the economic equivalence that tax expenditure analysis highlights is central to the legislature's performance of its task. The problems with tax expenditure analysis and the difficulties of compiling the tax expenditure budget do not significantly undermine their utility in the legislative arena. The tax expenditure budget is generally and broadly accurate as a list of tax provisions that function as

37. The Congressional Budget Act of 1974, Pub. L. No. 93-344, 88 Stat. 297 (codified as amended in scattered sections of 2 & 31 U.S.C.), required that a list of tax expenditures be included in the budget every year. The tax expenditure budget quantifies the cost of tax expenditure provisions and details their allocations among the various government agencies. It estimates the revenue losses associated with individual tax provisions, and describes the provisions included in the budget. For example, the tax expenditure budget has a category for "health" provisions, under which it quantifies the revenue loss on account of the exclusion of employer contributions for medical insurance premiums and the deductibility of medical expenses, among others. See Analytical Perspectives, supra note 5, at 71-98. The OMB quantifies the cost in two ways, which produce different totals for tax expenditures: the revenue cost method quantifies the amount of revenue that would have been collected had tax been collected without the tax expenditures. The outlay equivalent method quantifies the amount of revenue that would have been necessary if tax had been collected and the government transferred sufficient funds to the taxpayer to cover the tax liability. Where they differ, the outlay equivalent method generally results in a higher amount. For a description of the economic assumptions used in determining the numbers, see id. at 84-87. The Joint Committee only uses the revenue cost method. See Joint Committee Budget, supra note 11, para. 61.


41. I.R.C. § 32.
government spending, even though it would be impossible to prove that it is truly accurate in every detail.\textsuperscript{42} Its failure to achieve complete accuracy is not critical to the legislators who can use it to identify the type and magnitude of tax provisions that could be reenacted as spending programs.\textsuperscript{43}

For courts, however, the occasional haziness inherent in tax expenditure analysis is much more problematic. The equivocal definition of income and the debatable question of whether particular items should be included in the tax expenditure budget make tax expenditure analysis an inadequate guide for deciding individual lawsuits. The theory is also of limited use in drawing lines between taxpayers, a task that courts engage in regularly, but that Congress rarely performs.\textsuperscript{44} The general accuracy that makes the concept and the list helpful to legislators in determining broad questions of policy would be small consolation to courts attempting to apply those policies in specific cases. Additionally, in reviewing legislation, courts do not get to pick and choose from among a variety of policy alternatives; they cannot decide to modify the legislative program or implement it in a different way. Rather, courts are called upon to uphold or strike down the legislation involved in a particular case or the government’s application of it.\textsuperscript{45}

Tax expenditure analysis calls on Congress to do the functional equivalent of reappropriating tax expenditures by identifying those sections of the Code that should be evaluated like spending provisions. Provisions omitted from the list of tax expenditures are properly analyzed as “tax” provisions, according to tax expenditure analysis. Thus tax expenditures have become easier targets for reform than structural provisions,\textsuperscript{46} and lobbyists try to characterize their cherished provisions as income-defining in order to keep them

\textsuperscript{42} Most people who care enough to consider the question would agree on most provisions in the tax expenditure budget. The OMB and the Joint Committee only differ on 17 provisions. See Joint Committee Budget, supra note 11, para. 60.

\textsuperscript{43} Of course, legislators can misuse the tax expenditure budget, as well as the rhetoric of tax expenditure analysis, for political reasons. See infra notes 79-91 and accompanying text.

\textsuperscript{44} When Congress singles out a particular taxpayer, it often does so obscurely. The most famous example is the “Louis B. Mayer” provision, which provided a special pension benefit for him alone without mentioning him by name in the Code. See Internal Revenue Code of 1954 \textsection 1240. See generally Lawrence Zelenak, Are Rifle Shot Transition Rules and Other Ad Hoc Tax Legislation Constitutional?, 44 Tax L. Rev. 563 (1989).

\textsuperscript{45} Though courts have undertaken significant remedial measures in certain contexts, they do not rewrite federal statutes and have limited discretion that might be informed by tax expenditure analysis.

off the tax-expenditure hit list.\textsuperscript{47} Making tax expenditures easier targets for reform might be defensible from a legislative perspective either because the structural provisions are contributing to some ideal, such as a comprehensive income tax base, that Congress is slowly striving towards by reviewing and repealing tax expenditures,\textsuperscript{48} or because there are simply too many provisions for the legislature to identify areas in which legislative attention is warranted, so that the list of tax expenditures assists the legislature in focusing its attention to where changes are warranted.

Unlike the legislature, the judiciary is never in the position of having the entire Code before it, and never has the opportunity to change any provision it dislikes. Courts are only called upon to consider cases and controversies, and therefore, no second-order screening device, such as the tax expenditure budget, is necessary to guide the courts to provisions that they should review. Once a tax provision is challenged, the courts can turn directly to the legal standards to determine the nature of the scrutiny that is appropriate.

The ambiguities of tax expenditure analysis are not the only reason why courts have wisely resisted embracing it.\textsuperscript{49} Their hesitancy is justified because judicial adoption of tax expenditure analysis could constitutionalize the definition of income and, as a by-product, reduce judicial scrutiny of income-defining provisions. It could also make constitutional consequences more vulnerable to political maneuvering, and set Congress and the courts on conflicting paths in shaping the tax law. The remainder of Part I explores these problems.


One of the problems with tax expenditure analysis’s insistence that economically equivalent tax and spending programs be analyzed consistently, even in constitutional cases, is that it gives the definition of a tax expenditure constitutional importance. This section argues that treating tax expenditures and direct expenditures identically would impose an unreasonable burden on the definition of a tax

\textsuperscript{47} See JEFFREY H. BIRNBAUM & ALAN S. MURRAY, SHOWDOWN AT GUCCI GULCH 196-97 (1988). See also PAUL MCDANIEL, TAX AND SPEND 5 (Spring 1998) (arguing against using the tax expenditure budget as a “hit list”) (manuscript on file with author).

\textsuperscript{48} While Professor Surrey clearly linked tax expenditures and tax reform, Professor McDaniel has rejected that connection.

Tax expenditure analysis presumes an ability to distinguish tax expenditures and structural provisions; identification as a tax expenditure is the first step in analyzing a tax provision according to the criteria applied to spending programs. But distinguishing tax expenditures from the structural components of the federal income tax has always been a problem. At one time, scholars debated whether such a distinction was even possible, and although no consensus emerged from that controversy, commentators seem to have lost interest in discussing the question of whether any tax expenditure budget is defensible. Instead, discussion has turned to the proper categorization of individual provisions, and it is not unusual for current analyses of tax expenditures to ignore altogether the theoretical impossibility of their identification.

While definitional uncertainty is manageable in the legislative arena, such ambiguity is very troublesome if constitutional implications flow from it. Incomplete resolution of the myriad definitional problems that arise at the edges of the tax expenditure concept could lead to undesirable results in difficult cases. If categorization of a provision as a structural tax provision causes it to be upheld by a court despite constitutional infirmities, then it provides a windfall to those who benefit from it. The definitional uncertainty of the tax may allow taxpayers to reap benefits that a court would not allow if the provision were not categorized as income-defining. On the other hand, if a tax provision is mistakenly equated with a direct spending provision so that the tax provision is invalidated, then certain programs that Congress has found desirable

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will be foreclosed as unconstitutional.\textsuperscript{53} In a case involving definitional uncertainty, the constitutional question turns on a contested distinction between a structural provision and an expenditure—a distinction that may be no less arbitrary than the one between direct and indirect government expenditure.

Connected with the problem of satisfactorily distinguishing tax expenditures from structural tax provisions is the tendency of tax expenditure \textit{rhetoric}, apart from its actual content, to emphasize the undesirability of tax expenditure provisions\textsuperscript{54} and consequently to imply that structural tax provisions are permanent. The nomenclature choices are revealing: some provisions are "structural," implying that the tax system might collapse without them, even though the decision about the particular structure is not a product of tax expenditure analysis. Courts may be led to believe that striking down a "structural" provision would be of greater consequence than striking down an "expenditure" that has made its way by stealth or accident into the Code.\textsuperscript{55} The special constitutional scrutiny that the strong version of tax expenditure analysis would impose on tax expenditures may yield a lack of scrutiny for tax provisions that make up the normal structure of an income tax. Although courts could subject items not on the tax expenditure list to the same treatment as those on the list,\textsuperscript{56} items left off the list benefit from the presumption that they are pure tax provisions, or simply revenue raising devices.\textsuperscript{57}

\textsuperscript{53} Surrey and McDaniel have suggested that judges look to the tax expenditure budget to determine whether an item should be evaluated as a spending program, rather than evaluating themselves whether a tax provision functions like a spending program. See \textit{Surrey \& McDaniel, Tax Expenditures}, \textit{supra} note 13 at 119. While the political concerns would be more substantial if judges adopt the tax expenditure budget compiled by either the administration or the Joint Committee, definitional uncertainty and mistakes can occur whether judges, politician, or bureaucrats make the determination.


\textsuperscript{55} When Professor Surrey appeared before the Senate Finance Committee, Chairman Harry Byrd accused him of insinuating that tax incentives were adopted without the knowledge of many congressmen. See \textit{Birnbaum \& Murray}, \textit{supra} note 47, at 14. See also Griffith, \textit{supra} note 16, at 359 (arguing that the 1986 Act proves that Congress chooses the distribution of the tax burden using a combination of tax preferences and rates).

\textsuperscript{56} \textit{See Surrey \& McDaniel, Tax Expenditures}, \textit{supra} note 13 at 144 (arguing that it would be impossible to claim that items on the list should not be analyzed like direct spending since Congress put them on the list, but that items not on the list could be treated like those on the list by courts considering such provisions).

\textsuperscript{57} It has been noted that even pure revenue raising provisions promote certain
Thus, wholesale adoption of tax expenditure analysis into judicial decisionmaking threatens to constitutionalize the definition of income by making income-defining provisions less vulnerable to constitutional attack than tax expenditures.

For example, Congress might adopt a provision that allows taxpayers to deduct the costs of private school tuition on the ground that parents of private school students are double-taxed when taxed for the support of public schools and then required to use after-tax dollars to pay for private school. The double-tax explanation provides a structural justification for the deduction that depends on arguments about how to measure income. Alternatively, Congress might adopt the deduction because private schools reduce the burdens on government by alleviating the government’s need to provide educational services. Individuals who reduce the government’s burden while increasing their own financial obligations have reduced their own ability to pay taxes at the same time that they benefit the fisc. Ability-to-pay arguments explain the deduction’s role as part of the structure of an income tax.


Congress recently considered a provision that approximates such a deduction. See H.R. 2646, 105th Cong. § 2 (1998) (allowing parents to use untaxed build-up in investment accounts to pay for private school tuition).

This theory was suggested by the Supreme Court in *Mueller v. Allen*, 463 U.S. 388, 396 (1983): “[T]he Minnesota Legislature’s judgment that a deduction for educational expenses fairly equalizes the tax burden of its citizens... is entitled to substantial deference.” The Court considered the deduction for educational expenses a “genuine tax deduction.” *Id.* at 397 n.6 (distinguishing *Committee for Public Education v. Nyquist*, 413 U.S. 756 (1973)).

An income tax must measure income accurately in order to tax every dollar once and only once.


*Cf.* David F. Bradford et al., *Blueprints for Basic Tax Reform* 83-84 (2d ed. 1984) (including a deduction for state and local income taxes in the Model Tax Based on Income because these payments reduce the resources available to the payor for consumption or accumulation).

This type of approach has been explored by Professor Victor Thuronyi. See Thuronyi, *supra* note 32. He suggests that we replace the tax expenditure concept with the concept of “substitutable” tax provisions. A substitutable provision is any “tax law provision whose purposes a non-tax-based federal program can achieve at least as effectively.” *Id.* at 1156. If the purpose of the provision is to relieve the tax burden on income, then the provision is not substitutable. See *id.* at 1186-88. In evaluating the constitutionality of tax provisions, Thuronyi considers whether a provision is a true taxing provision, i.e., one relating to tax burden allocation. He compares *Mueller v. Allen*, 463 U.S. 388 (1983), in which the Supreme Court upheld a tax deduction for school tuition and supplies available to all taxpayers, with *Committee for Public Education and Religious Liberty v. Nyquist*, 413 U.S. 756 (1973), in which the Court struck down a tax credit for...
inaccurately when an item is double-taxed.

Another example of too little scrutiny for normative elements of the tax might be the exemption from tax for certain types of organizations.\textsuperscript{64} The tax exemption for religious, educational and charitable organizations\textsuperscript{65} is not listed as a tax expenditure.\textsuperscript{66} There are various justifications for why the exemption is not a tax expenditure. Some commentators have argued that the organization's income is not income at all in the accretion sense, but rather the pooling of the separate income of individuals,\textsuperscript{67} and that nonprofit organizations do not benefit individual taxpayers and are therefore inappropriate objects of taxation.\textsuperscript{68}

But why should the structural arguments matter if the schools or organizations discriminate on the basis of race? In that case, courts should investigate whether the deduction or exemption amounts to government discrimination. This approach would certainly be preferable to a policy of overlooking constitutional claims because the challenged code sections are "structural." Whether the state

private school tuition. Thuronyi rationalizes the Supreme Court's holdings in those cases on the grounds that "the Minnesota deduction [upheld in \textit{Mueller}] was motivated at least in part by tax-policy considerations unrelated to the goal of providing aid to private schools." \textit{Id.} at 1204. Because nobody made an ability-to-pay type argument in \textit{Nyquist}, which appears to be the sine qua non of a tax policy justification, Thuronyi concludes that it was reasonable for the Court to strike down the tax credits in that case for providing aid to sectarian schools. Thus, Thuronyi bases his distinction between \textit{Mueller} and \textit{Nyquist} on the essential tax nature of the provision in \textit{Mueller} and the absence of that nature in \textit{Nyquist}. \textit{See id.} at 1204-05.

While Thuronyi tries to erase the unworkable distinction that tax expenditure analysis creates by separating taxing provisions from spending provisions, he introduces an analogous distinction between substitutable and non-substitutable provisions, inviting increased scrutiny only for substitutable provisions. Thus, Thuronyi's categorization gives non-substitutable provisions a special status equivalent to Surrey's structural tax provisions, making his proposal quite similar to the tax expenditure analysis in this respect. While Thuronyi rejects the normal income tax, his proposal is dependent upon "tax structure issues," as is tax expenditure analysis. Just like that analysis, his proposal seems to rely upon identifying whether a provision really is a "tax" provision or not, but without defining the theoretical parameters for what counts as a tax. In elevating tax structure without presenting a normative tax, Thuronyi's tax structure is empty. Thus, Thuronyi's alternative to tax expenditure analysis shares tax expenditure analysis' flaw in overprotecting the structure of the tax, but without the benefits of the comprehensive base that provides the normative underpinning for tax expenditure analysis.

64. For greater discussion of exempt organizations and the charitable contribution deduction, \textit{see infra} part II.

65. I.R.C. § 501(c)(3).

66. \textit{See \textit{Analytical Perspectives}}, \textit{supra} note 5, at 73-75.


68. \textit{See Bittker, Tax Subsidies}, \textit{supra} note 17, at 256; Bittker & Rahdert, \textit{supra} note 67, at 314-316.
discriminates on the basis of race cannot possibly depend on the definition of income.

It is easy to make arguments for why a provision is part of the structure of an income tax, and it is easy to see that even normative provisions defended on income-definition grounds might in fact promote certain kinds of schools or particular classes of taxpayers. This definitional slipperiness underscores the problem with applying exacting constitutional scrutiny only to tax expenditures and never to structural provisions. Characterizing a provision as a structural component of the tax could protect its possibly unconstitutional effects.

The problems of a two-tier system of judicial review can be illustrated by a recent real-life example. During the debates over the Taxpayer Relief Act of 1997, Representative Archer, chairman of the House Ways and Means Committee, opposed the Administration’s efforts to make the child tax credit refundable and stated that he would consider refundability of the credit to be a welfare (i.e. spending) provision, rather than a tax provision. In the legislation that was eventually adopted, the child credit is refundable, but only to the extent that the taxpayer has paid FICA that is not refunded through the earned income credit. If Chairman Archer’s view of the refundability provision—as a welfare program—were to prevail, then the refundability feature would be part of the tax expenditure budget, and thereby treated somewhat like a spending provision. On the other hand, if the entire provision were included

70. The Ways and Means Committee is responsible for tax legislation in the House.
73. FICA is the combined Social Security and Medicare tax paid on a wage base, not according to income. See I.R.C. §§ 3101, 3111.
74. I.R.C. § 32.
75. Some would argue that the child credit should be included in the tax expenditure budget, regardless of the refundability provision, but others would argue that the child credit is a normative tax provision because it adjusts for the taxpaying ability of families depending on their size. See infra note 77. Neither OMB nor the Joint Committee analyzes the different components of the child credit in their explanations. See ANALYTICAL PERSPECTIVES, BUDGET OF THE UNITED STATES GOVERNMENT, FISCAL YEAR 1999, at 92 [hereinafter 1999 ANALYTICAL PERSPECTIVES]; JOINT COMMITTEE BUDGET, supra note 11, para. 32. However, OMB includes payments made in excess of the tax liability (i.e. the refundable portion) in the direct spending budget for both the earned income tax credit and the child credit. See 1999 ANALYTICAL PERSPECTIVES, supra, at 515-16. Thus, the amounts included in the tax expenditure budget are apparently limited to the nonrefundable portion.
76. It is not clear how Representative Archer would characterize the part of the credit that offsets tax liability but is not refundable.
as a normative tax provision because it helps measure the ability of families of different sizes to pay tax,\(^77\) or achieves progressivity in rates, it would not be treated as a spending provision but would be part of the structure of the tax. This structure-fulfilling function would identify the provision as one necessary to define income.

For purposes of analysis, let us assume that nonrefundability would allocate greater benefits to white families, while refundability would allocate greater benefits to minority families. What if Congress chose to design the refundability provision in order to provide tax benefits primarily to families of a particular race?\(^78\) Whether this provision should be subject to an equal protection challenge should have nothing to do with the provision's categorization as a tax expenditure or structural provision. If Congress designs a provision for the express purpose of providing an economic benefit to white families and denying the same benefit to minority families, then it should be subject to an equal protection challenge. A provision's distributional consequences and the intent behind them are not determined by its characterization as a tax expenditure.

C. Politicization of Tax Expenditure Concept

Another reason why wholesale judicial adoption of tax expenditure analysis is undesirable is that the constitutional consequences that flow from defining the normal tax would be vulnerable to political manipulation. The tax expenditure budget can be a forceful political weapon because items included in that budget are quantified federal spending, while excluded items are largely invisible. Surrey dramatized this point by explaining that the home mortgage deduction means that the federal government sends richer taxpayers large checks to subsidize their mortgages, middle-income taxpayers medium checks, and refuses to subsidize the poorest

\(^77\) Along the lines of the dependency exemption. See I.R.C. § 151(c). The definitional question for the child credit is similar to the definitional question for the dependency deduction. For a discussion that treats the dependency deduction as a tax expenditure, see Lawrence Zelenak, *Children and the Income Tax*, 49 TAX L. REV. 349 (1994) (discussing welfarist and externalities arguments). See also HENRY C. SIMONS, *PERSONAL INCOME TAXATION* 140 (1938) (arguing that child support is voluntary consumption). For a defense of the dependency exemption as a structural provision because child support is involuntary consumption, see Boris I. Bittker, *Federal Income Taxation and the Family*, 27 STAN. L. REV. 1389, 1444-56 (1975).

\(^78\) I propose this hypothetical because it presents an egregious example of legislative intent to discriminate on the basis of race, which suggests serious equal protection problems under a standard of strict scrutiny. See infra, Part II. It is necessary to use hypothetical provisions in this discussion because there is no income-defining provision of current law that would meet the high standard of intent necessary for a violation of the equal protection clause.
mortgagors at all. The inherent flexibility in the tax expenditure definition was manipulated by the Reagan Treasury to change the baseline tax against which tax expenditures are identified and measured. Whereas Surrey used a modified version of an economic ideal, the Reagan Treasury dispensed with the normative foundation and adopted a reference tax law baseline that resembled existing law. Consequently, departures from the base were defined so that the tax expenditure budget became increasingly skewed in favor of social spending, and business incentives were etched into the tax's normal structure. The Reagan Treasury's redefinition of the tax expenditure reflects not only the continuing problem of defining the normal tax, which I have already argued should give one pause before attaching legal consequences to that definition, but also the ability of those in control of the official definition to alter it to serve political goals. If courts place too much importance on the list, then those who assemble the list—tax specialists in the Treasury and Joint Committee who are not accountable in the political process and who necessarily bring their own views to the task of categorization—have very significant power.

The rhetoric of tax expenditure analysis transforms "tax cuts" into "spending programs" (and vice versa), with the political consequences that follow from those characterizations. The politician who cuts taxes in the 1990s is favored over the one who increases spending. The debate over refundability of the child credit is an

79. See Surrey, Pathways, supra note 13, at 234-35.
81. See 1999 Analytical Perspectives, supra note 75, at 104.
82. The Reagan Treasury included the reduced rate for capital gains and accelerated depreciation as part of the normal tax. See Analytical Perspectives, supra note 5. Even Surrey's model can be considered biased towards business in its departures from the Haig-Simons income definition. If Haig-Simons were used as the normal tax, then unrealized appreciation would significantly change the distribution of tax expenditures.
83. See supra Part I.B.
84. Professor Surrey had great confidence in the tax experts who would prepare the tax expenditure budget. See Surrey, Pathways, supra note 13, at 19-21. Professor Surrey may have been too trusting.
85. The text assumes that the courts would accept the categorization of tax expenditures that has been prepared by OMB or the Joint Committee. However, it would be possible for the courts themselves to undertake an initial determination of whether a provision should be categorized as a tax expenditure. This approach would reduce the problems of politicization of the constitutional determination, but would not address the other problems described in the text.
86. See supra notes 70-77 and accompanying text.
example of the use of tax expenditure rhetoric in this politicized manner. When Chairman Archer argued that he considers refundability of the credit to constitute a welfare program, rather than a tax program,\textsuperscript{87} he managed to harness public hostility to welfare and disassociate the provision from the popular support that tax cuts enjoy.

The political right has been quite successful in using the tax expenditure budget to attack programs it dislikes.\textsuperscript{88} Opponents of government spending have succeeded in targeting tax expenditures for elimination, without proposing that they be replaced with direct spending programs. The tax expenditure budget has become a target for proponents of smaller government, a knee-jerk hit list,\textsuperscript{89} with "reformers" ignoring the implication inherent in tax expenditure analysis that tax expenditures should be evaluated as direct spending programs to determine if they should be administered through the tax law. One commentator has claimed that tax expenditure analysis has proved to be unsuccessful precisely because it has made provisions listed in the tax expenditure budget easy targets for repeal without increasing actual scrutiny of the policies represented by those provisions, and without fostering analysis of the best way to achieve governmental objectives.\textsuperscript{90}

Adopting the tax expenditure concept into judicial decisionmaking threatens to compound the malleability of the normal tax structure and its susceptibility to politicization. If a provision's inclusion in the tax expenditure budget carries implications for how a court must analyze it when faced with constitutional questions, then whoever compiles the list has the power to affect the extent of the courts' examination of Code provisions.\textsuperscript{91}

An additional drawback to the constitutionalization of tax expenditure analysis could be the increased isolation of tax policy that it could engender. If the courts constitutionalize distinctions that are the product of the internal structure and coherence of the tax law, then the tax law will become more self-contained and independent of non-tax government policies. Tax expenditure analysis would reduce the number of provisions that should be analyzed as "tax policy" by identifying only certain Code sections as part of the "tax" law. It

\begin{itemize}
  \item \textsuperscript{87} See Stevenson, supra note 72.
  \item \textsuperscript{88} Left-leaning organizations have also assailed many of the items listed in the tax expenditure budget, but their denunciation of "corporate welfare" has not enjoyed the political momentum of the right's attack on social welfare. See CITIZENS FOR TAX JUSTICE, supra note 52.
  \item \textsuperscript{89} See MCDANIEL, supra note 47 (manuscript at p. 5).
  \item \textsuperscript{90} Thuronyi, supra note 32, at 1181.
  \item \textsuperscript{91} This problem does not exist if the courts engage in tax expenditure analysis without adopting any official version of the tax expenditure budget.
\end{itemize}
would consequently perpetuate the separation of what remains within tax policy apart from broader government policies. Only by increasing scrutiny of tax provisions generally, and making them subject to review for consistency with policies reflected outside the Code, can tax policy become more sensitive to the broader social policies that it increasingly reflects. Without constitutionalizing the structural components of the income tax, every tax provision can be reviewed on its own merits. Because tax expenditure analysis, on balance, may do more to isolate tax policy from social policy than to integrate it, it is crucial that its application be confined to the legislature, where it is most constructive.

D. Hybrid Income-Consumption Tax

There is a final reason why tax expenditure analysis should not constitutionalize the structure of the income tax: the increasingly hybrid nature of the federal income tax, as more consumption tax elements are incorporated. A hybrid base defies the ideal of a "normal" tax. While the normal tax does not have to be an income tax, there can be no tax expenditures where the underlying tax is simply a hodgepodge of excises that are not based on any structural tax components. A complete embrace of the hybrid tax model fully rejects tax expenditure analysis. But even a tentative acceptance of the hybrid tax raises doubts regarding constitutionalization of tax expenditure analysis.

When Surrey advocated for adoption of the tax expenditure budget, he stopped short of arguing in favor of income as the basic structure, and instead accepted that the United States had chosen income as the tax base. By reason of that choice, Surrey concluded that the list of tax expenditures should consist of those provisions that are not necessary to the accurate measurement of income. The list of

92. For example, the treatment of employer-provided pension plans, individual retirement accounts, and qualified state tuition programs all effectively exempt investment yield from tax.

93. A tax expenditure is simply the absence of a tax that we would otherwise expect to find according to a particular theory of taxation. This standard against which expenditures are measured is sometimes called a "normal" or "normative" tax. See ANALYTICAL PERSPECTIVES, supra note 5, at 71 (using the "normal" tax method); JOINT COMMITTEE BUDGET, supra note 11, at para. 8 ("tax expenditures are to be defined with reference to a normal tax structure"). See also SURREY, PATHWAYS supra note 13, at 7 (discussing a "normative" model of an income tax).

94. See SURREY & MCDANIEL, TAX EXPENDITURES, supra note 13, at 233.

95. He has been criticized for failing to defend the income base. See, e.g., Griffith, supra note 16, at 364.

96. See SURREY, PATHWAYS, supra note 13, at 15-21; SURREY & MCDANIEL, TAX EXPENDITURES, supra note 13, at 5. Professor McDaniel continues to hold this view. See MCDANIEL, supra note 47, at 7.
tax expenditures that he proffered, as well as the lists compiled by the Joint Committee on Taxation and the Office of Management and Budget today, was composed of items that escape tax despite their characterization as income under a distant cousin of the Haig-Simons definition of income.97

It may have been reasonable for Surrey to have assumed the income base when he first developed the tax expenditure budget, since he wrote against the backdrop of considerable scholarly and governmental excitement about a comprehensive income tax base.98 Congressional interest in a comprehensive income tax seems to have peaked around the time that Tax Expenditures was published in 1985, culminating in the Tax Reform Act of 1986.99

But the post-1986 mood seems to have changed, and this decade has seen a clear legislative and popular move away from a comprehensive income tax.100 Professor Shaviro has described the cyclical nature of tax legislation—a move toward purification of the tax base (tax reform) followed by a move away from such reform and toward the use of the tax law as a social tool.101 Consistent with that change in ideal, tax legislation in the 1990s has increased the Code's

97. Strict adherence to the Haig-Simons definition of income would require taxation of imputed income, for example, which was not part of Surrey's normal tax base. See Surrey, Pathways, supra note 13, at 12-13. Professor McDaniel's Tax and Spend seems to have moved closer to a Haig-Simons ideal than did his previous work with Professor Surrey. Compare McDaniel, supra note 47, at 6-1 ("My own view is that if an item is excluded from the tax base but would fall within the S-H-S definition of income, there is a rather strong presumption created that the item is a tax expenditure.") with Surrey & McDaniel, Tax Expenditures, supra note 13, at 4 (accepting the exclusion of unrealized appreciation and imputed income from the normative tax).

98. See Boris I. Bittker, A "Comprehensive Tax Base" as a Goal of Income Tax Reform, 80 Harv. L. Rev. 925, 925 (1967) ("It is no exaggeration to say that a 'comprehensive tax base' . . . has come to be the major organizing concept in most serious discussions of our federal income tax structure."). See also Comprehensive Income Taxation (Joseph A. Pechman ed., 1977); Bradford, supra note 62; Department of the Treasury, Tax Reform for Fairness, Simplicity and Economic Growth ch. 1 (1984) [hereinafter Tax Reform for Fairness, Simplicity and Economic Growth].


departures from a comprehensive tax on income. Recent amendments to the Code move the federal income tax one step further from an ideal income tax and one step closer to a consumption tax. Many scholars have recognized, and accepted, the "hybrid" nature of our income-consumption tax.

Notwithstanding changes in the underlying definition of the tax base and a greater acceptance of the consumption-tax model, the tax expenditure budget continues to identify departures from an income ideal. A glance at the tax expenditure budget reveals that many of the provisions included therein would be structural in a tax based on consumption. Acceptance of the hybrid income-consumption tax as an independent and legitimate policy choice undermines the normative foundation on which the tax expenditure budget rests. In other words, the hybrid income-consumption tax that we have—and that we seem satisfied to develop further—threatens the very existence of the tax expenditure.

If recent legislation is any indication, it is likely that Congress will continue to adopt consumption-type provisions to further economic and social goals. If so, judicial adoption of tax expenditure analysis (and implicitly its income-based model) could set the two branches of government working at cross-purposes. If the courts analyze consumption-based provisions as exceptions from an income tax, they will subject those provisions to restrictions based on an

102. Professor McDaniel interprets this history as a desire for greater use of tax expenditures, without signaling any change in policy ideal concerning the basic structure of the tax. The continued official preparation of the tax expenditure budget certainly supports this perspective.

103. The Taxpayer Relief Act of 1997 is replete with provisions that reduce the effective rate of tax on accumulated income. See, e.g., Taxpayer Relief Act of 1997, Pub. L. No. 105-34, §§ 302 (Roth IRAs), 311 (capital gains), 312 (gain on sale of principal residence), 111 Stat. 788.


105. For example, the exclusion of contributions to and earnings in pension plans, the exclusion for interest on state and local bonds, the expensing of business costs, accelerated depreciation, and the deferral of gains for certain transactions.

106. The tax expenditure concept could be modified to accommodate the hybrid tax. For example, the tax expenditure list could exclude all items that would be normal in either a pure income tax or a pure consumption tax. But recognizing the compromise in the tax base weakens the structure of the normal tax, perhaps to the point at which departures from it have no normative significance.
income model that Congress has chosen to reject. Congress’ taxing power would thus be compromised, creating unnecessary inter-branch conflict and thwarting Congress’s efforts to achieve legitimate legislative goals.

II. Tax Expenditure Analysis in Constitutional Decisionmaking

In the last Part, I explained why wholesale importation of the strong version of tax expenditure analysis into judicial decisionmaking is undesirable. In this Part, I explain my more qualified version by describing the approach that courts should follow in considering the constitutionality of tax benefits and the significance they should attach to the economic equivalence of tax benefits and direct spending. This part begins with a brief discussion of state action, a predicate for constitutional review by courts, and explains why tax benefits should always be subject to constitutional scrutiny as state action. Then it discusses how to evaluate government intent in tax policy because government intent is a crucial element of the substantive constitutional analysis that I argue must be applied to tax provisions. After setting up a general approach, I separately explore the constitutionality of tax benefits that flow to private organizations under the equal protection and establishment clauses, applying the doctrine developed in each of those areas and discussing the recent Supreme Court cases that raise these issues. Because the Supreme Court’s current equal protection and establishment clause jurisprudence does not lead to the conclusion that economic equivalence is crucial for those constitutional provisions, I conclude that tax provisions and direct spending programs having the same economic effect could have different constitutional statuses. I also consider alternative interpretations of the equal protection clause to illustrate how the analysis of tax-based aid would differ pursuant to those interpretations, and how economic equivalence could be central to constitutional analysis.

A. State Action

One might argue that tax benefits do not involve sufficient state action to trigger constitutional scrutiny. After all, it is the taxpayer

107. It would be possible to limit the tax expenditure budget to any provision that fit neither an income nor a consumption base, and treat the federal tax like a combination of two comprehensive tax bases. However, that would be inconsistent with reality as well because the tax that Congress has chosen picks provisions from both ideal bases, but refuses to adopt either one purely and totally. For an explanation of why we have the hybrid we have, see Kornhauser, supra note 104.

108. It is well settled that the Constitution only prohibits discrimination by the government, not by private parties. The Equal Protection Clause states: “No State
who decides to take advantage of the charitable deduction by writing a check to a religious institution or single-sex school. It is the taxpayer, not the state, that makes the funding decision, and it is the institution that carries out its own private policies.

The lack of government control inherent in the provision of tax benefits supports the argument that such benefits cannot constitute state action. The level of government involvement necessary to make a private party into a state actor is substantial. Unlike direct government funding and operation, tax benefits are generally characterized by a minimal level of government control and a significant level of taxpayer cost. The Supreme Court has been reticent to find that state action exists where the wrong was under the control of a private party—even where that party had significant involvement with the state. Because tax benefits generally create

shall . . . deny to any person within its jurisdiction the equal protection of the laws." U.S. CONST. amend. XIV, § 1. Through the Fifth Amendment, the strictures of the Fourteenth Amendment also apply to the actions of the federal government. See Bolling v. Sharpe, 347 U.S. 497 (1954). It has been argued that at the time the Fourteenth Amendment was adopted, the common law was assumed to protect people from private discrimination, and therefore, the Constitutional provision was necessary to stop government action, completing the individual's right not to be discriminated against. See Erwin Chemerinsky, Rethinking State Action, 80 NW. U. L. REV. 503 (1985) [hereinafter, Chemerinsky, Rethinking].

109. The Supreme Court has found state action to exist in the actions of private parties where those private parties exercise governmental power by executing a traditional public function. See, e.g., Terry v. Adams, 345 U.S. 461, reh'g denied, 345 U.S. 1003 (1953) (state action found where private party managed elections for public office); Marsh v. Alabama, 326 U.S. 501 (1946) (state action found where company operated a "company town").

110. This follows from the entitlement nature of tax benefits. See JOINT COMMITTEE BUDGET, supra note 11, para. 6 ("Tax expenditures are most similar to those direct spending programs that have no spending limits, and that are available as entitlements to those who meet the statutory criteria established for the programs.") Once the Code includes a provision, any taxpayer can arrange her affairs so as to benefit from it. Occasionally, the government's revenue estimates will miscalculate the number of taxpayers who will avail themselves of a benefit. For example, when Congress adopted the deduction for IRA contributions, taxpayers saved themselves $32 billion over three years, even though the government had predicted that the provision would only cost $5.5 billion. See BIRNBAUM & MURRAY, supra note 47, at 86.

111. Taxpayer cost is reflected in the non-subsidized portion of an expenditure that receives preferential tax treatment. For example, a taxpayer in a 30% bracket is entitled to a deduction for contributions that she makes to charity, but the government only subsidizes her contributions to the extent of her tax rate, so that the taxpayer must fund the other 70% of the gifts herself.

112. See, e.g., San Francisco Arts & Athletics, Inc. v. Unites States Olympic Comm., 483 U.S. 522, 542-47 (1987) (holding that the Committee was not bound by the Constitution, even though it had been chartered by federal law and received federal funds); Blum v. Yaretsky, 457 U.S. 991, 1002-12 (1982) (finding that physicians who made decisions to move patients out of nursing homes, thereby denying them Medicaid benefits, were not state actors); Rendell-Baker v. Kohn, 457 U.S. 830, 839-43 (1982) (refusing to apply First
entitlements, taxpayers control their own receipt of them. Entitlements do not preclude anyone who can satisfy their terms. Therefore, tax-based support is not well-suited to singling out particular individuals or organizations. The cases suggest that the government's considerable involvement with the private actor, even where there is a significant financial subsidy, does not necessarily turn that actor's decision into action of the state.

Amendment limitations to school's decision to fire teacher for her views on school policy, even though school was funded and heavily regulated by the state); Flagg Bros., Inc. v. Brooks, 436 U.S. 149, 157-64 (1979) (holding that no state action existed where a statute authorized self-help by parties seeking to repossess property).

113. But see supra note 44.

114. Even if a government subsidy may sometimes be a significant factor in finding state action, tax-based support is always limited as a percentage of a private actor's budget; tax benefits cannot constitute substantially all of a private organization's support. The nature of tax benefits provided in the form of either an exemption, an exclusion, or a deduction is such that the level of government support is limited to the tax rate that the private actor would otherwise have paid. Unlike direct governmental spending programs, the provision of tax benefits can never provide the majority of any private party's support. For example, if an organization is funded entirely by private contributions from individuals who are allowed deductions for their contributions, then the government may be considered to subsidize those contributions at the value of the tax deductions—let us assume 40%, which is approximately the highest individual rate under current law. This means that 60% of the funding provided comes out of the pockets of the contributors, limiting the government's share of funding to 40%. The 40% rate for contributors provides a ceiling on the government's funding through this mechanism. If, in addition to private contributions, the organization earns income on its investments, the government's total support may increase, but its share of support will never go above 40% because the exemption for the organization's earned income can be no greater than the highest corporate tax rate, or 35%. Thus, if an organization receives $100 from contributors in the highest bracket and earns $100, which would be taxed at the highest corporate rate if not for an exemption (this assumption is generous to the government's share), then the government's subsidy can be assumed to be $70, out of a total budget of $200. This calculation assumes that contributions would not be included as part of a nonprofit's taxable income, if the organization were subject to tax, and is consistent with current law treatment for capital contributions to corporations. See I.R.C. § 118(a).

115. The only support for the argument that tax benefits imply state action by private persons who discriminate is Burton v. Wilmington Parking Authority, 365 U.S. 715 (1961). In that case, the Supreme Court held that there was state action in a restaurant's decision to exclude blacks because the restaurant was a tenant of the city-owned parking garage, even though the city had no control over the operations of the restaurant. This lessor-lessee relationship was a sufficient nexus between the state and the restaurant for the Court to hold the state responsible for the restaurant's activities. On this reasoning, tax benefits might constitute enough support or nexus necessary for state action. However, Burton has never been extended to apply to tax benefits, and although it has not been overruled, its continuing validity, even on its own terms, is questionable. See LAURENCE H. TRIBE, AMERICAN CONSTITUTIONAL LAW § 18-3, at 1701 n.13 (2d ed. 1988), [hereinafter TRIBE, CONSTITUTIONAL LAW] at 1701 n.13; Adams v. Vandemark, 855 F.2d 312 (6th Cir. 1988). But see Lebron v. National R.R. Passenger Corp., 513 U.S. 374 (1995) (Scalia, J., citing Burton in support of decision).
Notwithstanding these arguments, tax benefits clearly implicate both private action and government action. The issue, therefore, is the constitutional status of this joint public and private decisionmaking regarding the allocation of tax benefits. The requirement of both taxpayer and government action should not operate to privatize the government's role. Neither must it subject the private actor to constitutional scrutiny. It is not necessary to attribute the private action to the state to find that state action exists. Rather, the government's role in providing tax benefits should always be evaluated as state action, even though the ultimate beneficiaries of those benefits may be private actors beyond the reach of the Constitution's constraints. Where the government action is in passing legislation, the legislation must be subject to review; where the action is in regulation or administrative practice, those must comply with constitutional standards as well. Thus, when considering tax benefits, courts should approach the state action issue by separating the question of whether the government should be prohibited from providing a tax benefit from the question of whether a private party should be prohibited from engaging in an activity facilitated by those benefits.

Professor Tribe has explained the Court's state action doctrine by focusing on state acts separately from state actors. He explains the cases in which challenges to private actions are allowed by describing them as challenges to state acts—a government's delegation of authority to churches, a state's common law of libel that raises First Amendment concerns, a state's rule of tort immunity. Based on these cases, Professor Tribe argues that there can be state action even where the private parties are not deemed to be state actors—the state action may be in the state's law that allows one private person to sue another, the state's granting of government-like authority to a private party, the state's placing of monopoly power in a private party, and the state's immunization of private

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116. The argument that tax benefits fail, by their nature, to constitute state action, hangs on the fact that those benefits, standing alone, will never transform a private actor into a state actor. If the state action question always requires the private actor to be an agent of the government, it creates an unnecessarily high threshold for state action, and allows more private discrimination than is necessary to ensure that the private realm is not obliterated. Cf. Henry J. Friendly, The Dartmouth College Case and the Public-Private Penumbra, TEX. Q. Summer 1969, supp., at 1.


118. See LAURENCE TRIBE, CONSTITUTIONAL CHOICES 246-266 (1985) [hereinafter, TRIBE, CHOICES].


people from consequences of their actions.\textsuperscript{122}

Professor Tribe's perspective helps to illuminate the state action issue for tax benefits by focusing on the legal regime. The creation of the legal regime itself—the statutes, regulations, and administrative practice that authorize taxpayers to direct public funds as they wish—is undeniably state action. Whether that action violates the substantive protections of the Constitution is a separate question. But it is not necessary to find that any private party is a state actor in order to attack the state itself for providing that party with benefits.\textsuperscript{123}

B. Evaluating Government Intent in Tax Policy

Identifying the creation of the tax benefit as state action does not resolve the more difficult question of government intent. When the funding of a religious or discriminatory institution requires a combination of government and private action, how should courts evaluate the intent underlying that action? This section offers a framework for such analysis.

If the government intends to discriminate on the basis of race or gender, then its decision is subject to heightened scrutiny under the equal protection clause. If its purpose is to favor religion, then its actions violate the establishment clause. Given that these constitutional provisions place great importance on government intent or purpose, how does the nature of government intent reflected in tax provisions compare to the nature of government intent apparent in direct spending provisions? Taxpayer choice—the taxpayer's power to determine how government funds are allocated—is a hallmark of tax benefits.\textsuperscript{124} This is because the taxpayer can

\textsuperscript{122} See Tribe, Choices, supra note 118, at 264-65.

\textsuperscript{123} It is possible to prohibit the government from providing tax benefits without prohibiting private action by allowing a constitutional challenge to proceed against the government, but precluding an action for injunctive relief against the private party. See Green v. Connally, 330 F. Supp 1150 (D.D.C. 1971); McGlotten v. Connally, 338 F. Supp. 448 (D.D.C. 1972). Professor Tribe has suggested that the plaintiffs in Moose Lodge No. 107 v. Irvis, 407 U.S. 163 (1972) and Jackson v. Metropolitan Edison Co., 419 U.S. 345 (1974) should have sued the government authority granting benefits rather than the private party engaged in the discriminatory behavior. See Tribe, Constitutional Law, supra note 115, at 1717-18. To the extent that the state action requirement prevents intrusive remedies that disrupt private operations, see Erwin Chemerinsky, Constitutional Law: Principles and Policies 390 (1997) [hereinafter Chemerinsky, Principles], these concerns are absent in a suit of this type against the government, which would simply require a revocation of tax benefits. As long as the government's participation is severable from the private action, as it always is in the case of tax benefits, the state action doctrine should never operate to preclude review of the government's action in supporting the private party.

\textsuperscript{124} If individual choice is of constitutional importance with respect to tax-based programs, then it should be significant for non-tax based programs as well. Professors
choose to avail herself of a generally available provision by fitting within its contours. For example, taxpayers can require the government to contribute to the cost of their education by claiming an allowable credit or deduction for that education. They can require the government to help support their favorite charities by making deductible contributions to those charities. Regardless of whether individual choice is socially desirable, it is constitutionally significant because it can separate the government's intent from the ultimate recipient of tax benefits.

State support of private institutions falls along a spectrum of government involvement. At one end is VMI, operated and supported by the state. In that case, it was clear to the Supreme Court that the state was responsible for the sex-based discrimination of the institution. The other end of the spectrum is represented by the

Surrey and McDaniel have long pointed out that direct spending programs could give discretion to individuals in allocating government funds. See Paul R. McDaniel, Federal Matching Grants for Charitable Contributions: A Substitute for the Income Tax Deduction, 27 TAX L. REV. 377 (1972) (dispensing with the charitable deduction, but retaining individual choice precisely as it operates under the deduction); Surrey & McDaniel, Tax Expenditures, supra note 13, at 100. Individual choice is only a factor affecting the treatment of tax-based programs because it currently happens to be a hallmark of such programs, not because it must be a characteristic nor because only tax-based programs can allow for individual choice. Nevertheless, as long as tax-based programs have different characteristics than direct spending programs, it is worth considering the implications of those differences, even if those differences do not have to exist.

125. As with many tax provisions, the government's contribution in these cases depends on the taxpayer having sufficient tax liability to absorb the government benefit. In the case of the charitable contribution deduction, the taxpayer must also be an itemizer. See I.R.C. § 62 (stating that the charitable deduction is not allowed in determining adjusted gross income).

126. Before considering whether individual choice should have any constitutional significance, it is worth asking whether individual choice is desirable—whether individuals, rather than government and its processes, should be empowered to determine how government funds are spent. In the context of charitable giving, individual choice has been championed on pluralist grounds: government should not have the power to choose what is valuable in art or culture and that individual choice insures toleration for fringe groups and support for developing ideas. See, e.g. Donald L. Sharpe, Unfair Business Competition and the Tax on Income Destined for Charity: Forty-Six Years Later, 3 FLA. TAX REV. 367, 378-79 (1996). But see, Mark P. Gergen, The Case for a Charitable Contributions Deduction, 74 VA. L. REV. 1393, 1410 (1988) (stating that managers of artistic enterprises claim that private support requires them to cater to conventional tastes). However, individual choice raises questions for representative democracy. In an age of dwindling discretionary spending, whose discretion is best? Some might argue that democratically elected representatives are a better choice for determining how government money is spent than are the wealthy donors to charitable organizations. I have argued elsewhere that corporate managers are an undesirable choice in determining where corporate philanthropy goes because they represent a concentration of power outside the democratic process. See Linda Sugin, Theories of the Corporation and the Tax Treatment of Corporate Philanthropy, 41 N.Y.L. SCH. L. REV. 853 (1997).
example of police and fire protection—general services provided by
the state to everyone. By providing the same benefits to everyone,
the government support is tangential to the sphere of private activity
and the state does not discriminate on any basis. The greater the
government involvement in a particular activity, the easier it is to
equate institutional purpose with governmental purpose.

Government support through tax benefits, in particular the
Code's charitable contribution deduction allowed to donors, falls
somewhere in between the state-operated paradigm and the general-
services paradigm. The government clearly makes more choices in
the tax-benefits context than it does in the general-services context,
but at the same time, is less involved in the discrimination than it is in
the publicly operated single-sex school. In the provision of tax
benefits, there is always both decisionmaking by the government and
private decisionmaking. If tax benefits flow to discriminatory or
religious organizations, it is the government's decisionmaking that is
relevant to the constitutional analysis.

Tax benefits share the intermediate range of the spectrum with
numerous other types of government support of private institutions,
such as federally guaranteed student loans that help individual
students pay for tuition at single-sex schools and government-
backed bonds that support the construction of private schools. The
theory underlying the strong version of tax expenditure analysis
seems to have much to say about those programs as well as tax
benefits.

Tax benefits are not the same as police and fire protection—
though they are wide-ranging, they are not available for all purposes.
While they are allowed significant leeway in allocating government
funds, individuals cannot choose anybody they wish to receive tax
benefits. Any program under which individuals can choose to direct
government funds, as tax benefits do, must be limited by some criteria
predetermined by the government.

In designing tax benefits, Congress makes a determination to
fund certain categories of activities. By complying with the restraints
imposed by the statutory language, the taxpayer claims an entitlement

127. This was the paradigm in Walz v. Tax Commission of New York, 397 U.S. 664
(1970), the seminal case in which the Supreme Court upheld the property tax exemption
of religious institutions.
(1973)).
130. This reasoning suggests that there can be no allocation of government funds that is
independent of the government's message. Cf. Regan v. Taxation Without
to the benefit. The central issue in the constitutional analysis of tax benefits depends on determining the government’s intent in these intermediate contexts—where the government chooses to fund some general category of recipients, but not others. Because of the economic equivalence of direct funding and tax-based support, the strong version of tax expenditure analysis would equate taxpayer and government purpose with respect to the funding of a discriminatory or religious organization. In so doing, tax expenditure analysis fails to identify the similarities and differences between taxing and spending programs that are important for constitutional analysis.

Tax benefits and direct spending programs will often differ from a constitutional perspective because they reveal different levels of government intent: tax benefits can result from taxpayer compliance with an entitlement based on a nondiscriminatory standard, while direct spending programs (and state operation) are more likely to require affirmative inclusion by the government of a discriminatory private organization in a funding scheme. It is the requirement of both taxpayer and government action in the provision of tax benefits that allows the government to insulate its decisions from the decisions of the private organization. Because the Constitution imposes no affirmative obligation on the government to exclude private discriminatory or religious organizations from receipt of generally available government benefits, broad provision of such benefits seems to ensure their constitutional acceptability.

Under current doctrine, therefore, courts should find unconstitutional government intent in tax policy where there is evidence of a purpose to provide or specifically deny benefits to a group that cannot be constitutionally favored or disfavored. That determination, moreover, should focus on the level of government policy, not the determination to fund made by the individual taxpayer. Under this analysis, the more targeted a tax provision, the more vulnerable it would be to constitutional attack. The more general a provision, the less vulnerable it would be to constitutional attack, but the less effective it would be in achieving narrow social policy goals.

Theoretically, a tax provision could reflect the same level of government intent as direct operation or support. The following

131. These constraints can be considerable, as they are for qualified retirement plans governed by ERISA, or minimal, as they are for the home mortgage deduction.
132. There are, of course, many exceptions. There are government matching grant programs that operate very much like tax deductions, in addition to the well-known direct entitlement programs. A matching grant program could be designed in a way that minimized the government intent behind a particular grant and the analysis presented here could apply to that program as well.
A hypothetical tax provision would thus clearly violate the equal protection clause: "There shall be allowed as a deduction any contribution or gift to any educational institution that admits only white students." The statute itself indicates government intent to discriminate on the basis of race in the provision of tax benefits. Separate rate schedules for minorities and whites, or deductions, credits or exemptions explicitly tied to race would also be facially discriminatory and therefore, unconstitutional. At the other end of the spectrum, a deduction allowed for contributions to all educational institutions would be acceptable. The broad generality of such a provision negates any implication of intent to discriminate on the basis of race, even though racially discriminatory organizations could claim benefits pursuant to the provision.

Government intent, or purpose, is crucial in establishment clause analysis as well as equal protection analysis because the state is not allowed to prefer any particular religion, or to favor religion over non-religion. If a tax statute evidences such an intent, then it would run afoul of establishment clause principles. Thus, if the Code were amended to provide that deductions are only allowed to Christian organizations, but not other religious organizations, that provision would be unconstitutional. At the other end of the spectrum, a provision that allows deductions for contributions to all membership or not-for-profit organizations would be general enough to be constitutionally acceptable, even though it would, in fact, include religious organizations. I will call this latter type a "general-principle" provision.

Many tax provisions discriminate among taxpayers on some

133. Professor McCaffery has raised an interesting equal protection question by suggesting that we adopt a different rate schedule for married women and married men. See Edward J. McCaffery, Taxing Women (1997) [hereinafter McCaffery, Women]; Edward J. McCaffery, Taxation and the Family: A Fresh Look At Behavioral Gender Biases in the Code, 40 UCLA L. Rev. 983 (1993) [hereinafter McCaffery, Family]; and Edward J. McCaffery, Slouching Towards Equality: Gender Discrimination, Market Efficiency and Social Change, 103 YALE L.J. 595 (1993). His recommendation is based on application of the optimal tax model and empirical evidence about the elasticity of the labor supply of married women and married men. Because married women are more responsive to the tax costs of working, and therefore more likely to stop working if taxes diminish their take-home pay, McCaffery argues that married women should be taxed less so that the tax does not alter their behavior. Because discrimination on the basis of gender has been subject to an intermediate level of scrutiny, rather than the strict scrutiny applied to race-based classifications, McCaffrey's proposal might (or might not) pass muster under current equal protection doctrine. A similar race-based classification would certainly violate equal protection.

134. While the literature on statutory interpretation distinguishes intent from purpose, the courts do not seem to have picked up on this distinction. See generally, Ronald Dworkin, Laws Empire (1986); William Eskridge, Dynamic Statutory Interpretation (1994).
basis, most often the sources or uses of income, and it is worth considering two types of tax provisions to decide what level of government intent they exhibit. The first type is what I will refer to as laundry-list provisions, and they should be closely scrutinized for government intent behind every item individually. The second kind discriminates on the basis of non-suspect characteristics, often relating to ability to pay, but benefits certain defined groups. These provisions should be closely scrutinized for evidence of government intent that is not on the face of the statute.

In adopting laundry-list provisions, the government can indicate an intent to discriminate, even though it can bury that intent in the list. For example, if Congress passes a provision that allows deductions for contributions to Bob Jones University and the alma mater of each of Congress' current members, with each school individually named in the statute, the fact that Congress affirmatively chooses to include Bob Jones University may indicate an intent to provide benefits to an organization that discriminates on the basis of race, despite the company it keeps in a long list of other schools that do not so discriminate. Thus, intent to discriminate is not negated by laundry-list provisions in the same way that it is negated by general-principle provisions that happen to benefit organizations that discriminate.

Section 501(c)(3) is, of course, a laundry-list provision. It provides that the organizations described as follows shall be exempt from tax:

Corporations, and any community chest, fund, or foundation, organized and operated exclusively for religious, charitable, scientific, testing for public safety, literary, or educational purposes, or to foster national or international amateur sports competition..., or for the prevention of cruelty to children or animals, no part of the net earnings of which inures to the benefit of any private shareholder or individual, no substantial part of the activities of which is carrying on propaganda, or otherwise attempting, to influence legislation... and which does not participate in or intervene in... any political campaign on behalf of (or in opposition to) any candidate for public office.

Section 170 piggybacks on the exemptions in section 501(c)(3) and authorizes a deduction for contributions to such organizations. The clause in the middle of the section is the general-principle type of provision referred to earlier—the allowance of an exemption for all not-for-profit organizations. But the code section does not allow such

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135. For example, preferential rates for capital gains, I.R.C. § 1(h); tax-free fringe benefits, I.R.C. § 132; the home mortgage deduction, I.R.C. § 163(h).

136. I.R.C. § 501(a) operates to provide the exemption, I.R.C. § 501(c)(3) describes the organizations.
a broad-based application. Rather, an organization must also fit within one of the specific-purpose categories at the beginning of the section. While the categories do not indicate any intent to discriminate in violation of the equal protection clause, they may indicate intent to favor religion in violation of the establishment clause.

On the one hand, this statutory language reflects a government preference for religion because religious organizations automatically qualify for the exemption (and donations to them are tax-deductible), while secular organizations must fit into one of the other enumerated categories in order to qualify for exemption. Section 501(c)(3) does not make tax-based support generally available to a broadly defined class of which religious organizations incidentally happen to be members. Rather than describing a general principle, the list in section 501(c)(3) is a hodgepodge of organizations with varying purposes.\textsuperscript{137} The support of religious organizations is explicit.

On the other hand, the breadth of section 501(c)(3) may be sufficient to remove the government’s imprimatur of support from any particular organization claiming the exemption.\textsuperscript{138} It can be argued that a long enough laundry-list provision negates any suggestion of special treatment for one group. This would be an argument for treating laundry-list provisions like general-principle provisions for purposes of determining government intent, rather than like facially discriminatory provisions. Some have argued that the variety of organizations and the cross-purposes to which they aspire prove that the government does not favor any particular message by the exemptions allowed in section 501. While that may be true in the narrow sense, a broader perspective reveals that the government supports religious, charitable and educational organizations, as opposed to the broad categories of, say, political or economic organizations. Most of these distinctions are constitutionally irrelevant, but the inclusion of religious organizations is troublesome.

The laundry-list approach to the charitable deduction presents an additional question about government intent to favor religion, due to the rationale for the existence of the deduction. The establishment clause’s requirement of neutrality toward religion is inconsistent with the rationale for the charitable deduction. The dominant theory

\textsuperscript{137} It is unlike the statute that provides support to all visually handicapped students, see \textit{Witters v. Washington Dep’t of Services for the Blind}, 474 U.S. 481 (1986), or all students who need remedial help, see \textit{Agostini v. Felton}, 117 S. Ct. 1997 (1997).

supporting the existence of sections 501(c)(3) and 170, the subsidy theory, is explicitly value-laden. The theory explains the exemption and the corresponding deduction as a means by which the government increases the financial support for organizations that it wants to subsidize, usually because they produce social goods. The subsidy theory implies that Congress approves of the organizations listed in the statute. Thus, the inclusion of religious organizations in the list may indicate Congressional intent to favor religion.

Other explanations for the charitable deduction, aside from the subsidy theory, could indicate a lower level of government intent to support religion. For example, the theory that explains the charitable deduction as encompassing organizations that reduce the burdens of government might not imply anything about the social value of organizations described in the section. The analysis under this theory is more of a functional analysis—what do governments do? Any organization that performs government functions, whether they are good or bad, would be eligible for the deduction, so the statute would not necessarily indicate government intent to favor religion. The individual choice at the funding level would essentially allow citizens to decide which functions of government are important enough to be funded. The problem with employing this theory to decide an establishment clause issue is that the inclusion of religious organizations among the allowable recipients is impossible to explain.

Turning to the second type of provision, the Code often

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140. Even if the statute indicates that the government favors religion, it may not be unconstitutional if it reduces government entanglement with religion or if it is required by the free exercise clause. For a discussion of other factors, aside from intent, that are important in establishment clause doctrine, see infra notes 258-295 and accompanying text.

141. See Walz, 397 U.S. at 687 (Brennan, J., concurring) (stating that "these organizations... bear burdens that would otherwise either have to be met by general taxation or be left undone."). It has been argued that the origins of the deduction could not have been explained on this theory. See Lars G. Gustafsson, 'Lessening the Burdens of Government': Formulating a Test for Uniformity and Rational Federal Income Tax Subsidies, 45 KAN. L. REV. 787, 801 (1997).

142. Under any reading of the establishment clause to date, government is not permitted to operate a church itself, so there is no explanation for how religious organizations, apart from their non-religious activities, come to fulfill the functions of government. Empirical evidence reveals that the public benefits functions of religious organizations are minimal compared to their other activities. See Jeff E. Biddle, Religious Organizations, in WHO BENEFITS FROM THE NONPROFIT SECTOR 92, 98 (Charles T. Clotfelter ed., 1992) [hereinafter WHO BENEFITS] (public benefit expenditures constitute 3% of total expenditures of religious congregations, sacramental expenditures constitute over 60%).
discriminates either on the basis of some notion of ability-to-pay, or because Congress wants to encourage certain economic activity. Thus, the Code allows deductions for extraordinary medical expenses and contributions to retirement savings accounts. It often discriminates on the basis of income, phasing out benefits for high-income taxpayers and providing refundable credits targeted to low-income taxpayers. As a by-product of the joint filing system, it gives some couples a "marriage bonus" and others a "marriage penalty." To the amusement of many law students, the "nondiscrimination" provisions in the Code have nothing to do with equal protection, but rather refer to high-income and low-income taxpayers.

Congress might include an apparently benign distinction in the Code precisely because it is linked, in fact, to a racial classification. Thus, if Congress designs the joint filing system with the intent to discriminate against minority couples or with the intent to tax women at a higher rate than men, then the provision should be subject to an equal protection challenge, and under current law, it would be. However, the problem of proving discriminatory intent in such a case is likely to be overwhelming.

143. The meaning of taxation based on ability to pay is not self-evident, and I leave for another day the discussion of whether the law's sensitivity to ability to pay tax is distinct from its encouragement of economic activity.

144. See I.R.C. § 213.

145. See I.R.C. § 219(a).

146. See, e.g., I.R.C. § 151(d)(3) (personal exemptions); I.R.C. § 219(g) (IRA deduction); I.R.C. § 68 (itemized deductions); I.R.C. § 25A(c) (Hope and Lifetime Learning credits).

147. See I.R.C. § 32 (EITC); I.R.C. § 24 (child credit).


149. See I.R.C. § 132(j)(1) (allowing classification for fringe benefits that do not "discriminate in favor of highly compensated employees"); I.R.C. § 401(a)(4)(qualified pension plans may not "discriminate in favor of highly compensated employees").

150. Under the joint filing system, the secondary earner—the spouse who earns less—is taxed at the primary earner's marginal rate on the first dollar of income. Because the primary earner can be said to earn the first family dollars, the primary earner enjoys the benefit of the progressive rate schedule and the family's exemptions, and the secondary earner is subject to a higher average rate of tax. Thus, some have argued for individual filing. See, e.g., Grace Blumberg, Sexism in the Code: A Comparative Study of Income Taxation of Working Wives and Mothers, 21 BUFF. L. REV. 49 (1971); Pamela B. Gann, Abandoning Marital Status as a Factor in Allocating Income Tax Burdens, 59 TEX. L. REV. 1 (1980).

151. See infra notes 189-194 and accompanying text. A discussion of standing to challenge the constitutionality of tax provisions is beyond of the scope of this Article. Nevertheless, it is important to keep in mind that there are significant standing hurdles that prevent taxpayers from challenging provisions that they believe contrary to constitutional norms. See Allen v. Wright, 468 U.S. 737 (1984); Simon v. Eastern Ky.
The most likely source of evidence of discriminatory intent behind tax provisions is legislative history, which is plentiful and readily accessible for federal tax legislation, particularly for recently enacted changes in the Code. However, drafters of relevant contextual materials, knowing the constitutional standard, would be foolish to include any indicia of discriminatory intent, particularly if a nondiscriminatory explanation is available to provide a plausible interpretation of the statute. Because this type of statute often has an income-related distinction, it is easy to explain it on the basis of ability to pay or consistency and coherence within the Code. Any distinction based on income is presumptively neutral because it is relevant to the revenue-raising functions of the tax law, and therefore, protected from charges of unconstitutional intent.

In addition, reliance on legislative history as an accurate indicator of Congressional intent is contrary to the lessons of much recent scholarship. Public choice theory, which is a major force in contemporary tax scholarship, makes the possibility of an identifiable government intent to discriminate seem absurd. To the contrary, public choice theory suggests that "legislative policy is often fragmentary and irrational." Given the general amalgamation of numerous tax provisions and other budget provisions in one bill, it would be extraordinary to find a discriminatory purpose explaining a statute’s adoption, and where legislation is the product of interest group agitation and legislative horse-trading, it might be hard to find any identifiable purpose at all. In tax legislation, intense lobbying

Welfare Rights Org., 426 U.S. 26 (1976) (holding that there is no standing to challenge IRS decision to fail to collect tax from someone else). The substantive analysis contained in this Article assumes that a challenger is heard by the courts.

152. Tax legislation is always accompanied by committee reports, and the tax press follows the day to day developments in Congress as legislation is being considered, recording statements of members, and publishing the text of proposals that do not become law.


156. Cf. Livingston, supra note 153, at 872-73 (arguing that because of the detailed omnibus nature of tax legislation, published sources may not reveal the intent of tax legislation).

and large campaign contributions are standard, suggesting active interest group participation in the process.\textsuperscript{158} Many legislators are not interested in learning the technical details of the Code, and therefore, may barely understand the provisions that they vote on.\textsuperscript{159} Code provisions, like other federal legislation, are endorsed for different reasons by different legislators.\textsuperscript{160} If public choice theory is accurate and legislation is largely the result of rent-seeking interest groups and politicians acting in their own self-interest,\textsuperscript{161} then there is little room for legislation to be propelled by either good public policy,\textsuperscript{162} as we hope, or a specific intent to discriminate, as we fear.

Furthermore, focusing on legislative intent in tax statutes may be inconsistent with the general approach to interpreting tax statutes, making intent more difficult to discover, and possibly concealing discriminatory intent. Commentators have argued that because of its special nature, the tax law lends itself to a different method of interpretation than other statutes;\textsuperscript{163} the Code's internal logic and coherence may be more important than the original intent of Congress in the day-to-day interpretation of tax statutes.\textsuperscript{164} Purposive approaches to statutory interpretation\textsuperscript{165} that try to make the disparate parts of the Code hang together have long prevailed in the "substance over form" and "step transaction" doctrines, under which the government wins even though the taxpayer complied with the

\textsuperscript{158} But see Edward A. Zelinsky, James Madison and Public Choice at Gucci Gulch: A Procedural Defense of Tax Expenditures and Tax Institutions, 102 YALE L.J. 1165, 1166 (1993) (using empirical evidence to argue that tax writing committees are less likely to be captured by interest groups than other Congressional committees).

\textsuperscript{159} See BIRNBAUM & MURRAY, supra note 47, at 77. The tax-writing committees vote on concepts rather than statutory language. See Livingston, supra note 153, at 833-37.

\textsuperscript{160} The Supreme Court has recognized this. See Arlington Heights v. Metropolitan Hous. Corp., 429 U.S. 252,265 (1977).

\textsuperscript{161} See Easterbrook, supra note 157.

\textsuperscript{162} For a discussion of the public interest theory of legislation, see Shaviro, Beyond Public Choice, supra note 101.

\textsuperscript{163} See Bradford L. Ferguson et al., Reexamining the Nature and Role of Tax Legislative History in Light of the Changing Realities of the Process, 67 TAXES 804, 806 (1989) ("Federal tax statutes and the legislative process that produces them differ from other legislation in such degree that the difference is tantamount to a difference in kind."). But see Paul L. Caron, Tax Myopia, or Mamas Don't Let Your Babies Grow Up to Be Tax Lawyers, 13 VA. TAX REV. 517 (1994).

\textsuperscript{164} Livingston, supra note 153, at 828; see also Deborah A. Geier, Interpreting Tax Legislation: The Role of Purpose, 2 FLA. TAX. REV. 492, 497 (1995) ("One component of statutory purpose in the income tax is the fundamental structure underlying the income tax."); Lawrence Zelenak, Thinking About Nonliteral Interpretations of the Internal Revenue Code, 64 N.C. L. REV. 623 (1986).

literal terms of the statute. A focus on the logic of the Code skews the interpretation of tax statutes away from discriminatory intent because such intent would necessarily represent a departure from any structure underlying the Code. If courts try to make the Code more internally consistent, then they might read out unconstitutional intent. While the internal logic of the Code may be useful in analyzing how different parts of the Code affect one another, it is irrelevant to the question of unconstitutional discriminatory intent. While there may be “basic features” of the Code that remain the same even as the Code is constantly amended, the addition of myriad miscellaneous provisions into the Code undermines the coherence of the Code as a whole, and increases the likelihood that a non-tax-based explanation, possibly an unconstitutional one, best explains Congressional intent.

In sum, the central question under both the equal protection and establishment clauses in evaluating tax benefits focuses on government intent behind the relevant section of the Code. While some hypothetical tax provisions present clear evidence of government intent, most actual Code provisions do not. General-principle provisions are generally immune from constitutional attack because they show insufficient government intent to favor any group. Laundry-list provisions are more likely to indicate government intent to provide targeted benefits, and the laundry-list in section 501(c)(3) may indicate government intent to favor religion. Finally, challenges to income-based classifications with discriminatory impact face very substantial hurdles because of the difficulty of proving government intent to unlawfully discriminate. Nevertheless, because the tax law has been increasingly called upon to carry out specific federal policies in a wide variety of areas, the constitutional limitations on tax provisions may become more significant than they have been in the past; a provision that benefits a small group of taxpayers may provide benefits solely to racist, sexist, or religious organizations. The general availability of most tax benefits to a broad range of recipients is what ensures their constitutional acceptability under current law. By focusing on intent, the courts have limited Congress’ ability to narrowly target tax-based support to organizations that it may not constitutionally fund directly. The constitutional standard thus limits the Code’s ability to reflect narrow unconstitutional preferences.

C. Tax Expenditure Analysis and Equal Protection

With the methodology described in the prior section, I now

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166. See Geier, supra note 164, at 495-96.
return to tax-based aid to discriminatory schools and the role of tax expenditure analysis in judging violations of equal protection. It is well settled that the state may not operate a racially segregated school system,\(^\text{168}\) and is now clear that the state may not operate a college exclusively for men without offering an equivalent opportunity for women.\(^\text{169}\) The question to now directly consider is whether the state may constitutionally provide tax-based support to private institutions that engage in such discrimination. The strong version of tax expenditure analysis, with its focus on economic equivalence, would equate tax-based support of such institutions with direct government support. Therefore, the strong version of tax expenditure analysis would lead one to conclude that allowing a charitable deduction for contributions to single-sex schools is equivalent to the government sending a check to those schools in the amount of the donors’ tax savings.\(^\text{170}\)

The problem with the application of the strong version of tax expenditure analysis to the constitutionality of tax benefits available to discriminatory schools under the charitable contribution deduction is that it treats economic equivalence as constitutionally decisive, while equal protection doctrine does not. Current Supreme Court interpretation of the equal protection clause reflects an “anti-discrimination” principle: the government is not permitted to discriminate on the basis of race or sex. This is why the intent requirement, described above, is central. Under the Supreme Court's decision in Washington v. Davis, it will only subject a statute to heightened scrutiny under the equal protection clause if the statute is facially discriminatory,\(^\text{172}\) or if it has a discriminatory effect and was adopted with a discriminatory purpose.\(^\text{173}\) If a facially neutral statute has only a discriminatory effect, the Court will apply rational basis review, even if the legislature knew that the statute would have a disproportionate effect on an identifiable group.\(^\text{174}\) The economic equivalence of tax benefits and direct spending would be crucial in

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170. See supra note 15 and accompanying text.
171. See TRIBE, CONSTITUTIONAL LAW, supra note 115, § 16-21.
172. Since there are no distinctions expressly based on race or gender in the Code, tax statutes are immune from facial attack. In Washington v. Davis, 426 U.S. 229, 248 (1976), the court noted the potential vulnerability of tax statutes (among others) in explaining the Court's decision to require proof of discriminatory intent under the equal protection clause.
173. See id. at 239-42.
174. See Massachusetts v. Feeney, 429 U.S. 66 (1976). Racial distinctions are subject to strict scrutiny and gender-based distinctions are subject to intermediate scrutiny.
determining whether a tax provision has disparate effects, but it sheds little light on whether the government intended to discriminate. The courts have only once explicitly equated the provision of tax benefits in an equal protection case with direct government spending. Applying tax expenditure analysis to an equal protection challenge, Judge Bazelon, in *McGlotten v. Connally*, compared the section 170 deduction to a government matching grant, relying on the rhetoric of tax expenditure analysis to distinguish such grants from "the structure of an income tax based on ability to pay." The court there struck down, on constitutional grounds, deductions for contributions to fraternal orders that discriminated on the basis of race. Taken together, *McGlotten* and *VMI* provide some support for arguing that tax benefits to private single-sex institutions are unconstitutional. However, that support is quite thin.

Supreme Court doctrine, though sparse in this area, supports this conclusion regarding the relevance of tax expenditure analysis. The only time that the Supreme Court has considered tax-based support of a discriminatory organization, in *Bob Jones University v. United States*, it upheld the Commissioner's denial of exemption on statutory grounds but avoided the constitutional question. *VMI* invites us to reconsider the Court's refusal to adopt the strong version of tax expenditure analysis in that case. The *Bob Jones University*

175. See Part II.D. infra.
177. He also cited Professor Surrey. See id. at 456 n.37, 462 n.68.
178. Id. at 457.
179. Courts have generally not been comfortable adopting tax expenditure analysis into constitutional adjudication. In an important equal protection case challenging tax benefits for discriminatory organizations, the same district court that decided *McGlotten* avoided a constitutional holding by finessing the question of whether tax-based support is legally equivalent to direct support, even while it invalidated the tax exemptions of racially discriminatory organizations. See *Green v. Connally*, 339 F. Supp. 1150, 1164-65 (D.D.C. 1971), *aff'd sub nom.* *Coit v. Green*, 404 U.S. 997 (1971). While indicating its familiarity with the reasoning of tax expenditure analysis, the *Green v. Connally* court declined to rest its holding on that reasoning.
180. Of course, tax-based support to single-sex institutions might withstand the intermediate standard of scrutiny that the Court applies to gender discrimination, even if the equivalent tax-based support failed under the strict scrutiny standard applied to the race discrimination at issue in *McGlotten*.
182. *Bob Jones University* forbade interracial dating between students, and threatened expulsion for those students who advocated interracial marriage. Following the Fourth Circuit's opinion in *Runyon v. McCrary*, 515 F.2d 1082 (1975), *aff'd*, 427 U.S. 160 (1976), Bob Jones University opened its admissions policies to students of all races. See *Bob Jones*, 461 U.S. at 580. The Supreme Court had previously held that laws restricting interracial marriage violated the equal protection clause. See *Loving v. Virginia*, 388 U.S. 1 (1968).
183. *But see* SURREY & MCDANIEL, TAX EXPENDITURES, *supra* note 13 at 131-32
case established a public policy limitation for organizations described in section 501(c)(3): in addition to fitting within one of the enumerated statutory categories (such as religious or educational), an organization must be charitable in the common-law sense in order to qualify for the exemption. Because Bob Jones University’s policies on interracial dating and marriage contravened well-settled national policy against racial discrimination in education, it did not qualify as charitable, and therefore, the Court found that the IRS had been correct in revoking the university’s tax-exempt status.184

The Court could have struck down the exemption on constitutional grounds by applying the strong version of tax expenditure analysis and reasoning from established precedent prohibiting direct aid to racially discriminatory schools.185 If it had adopted the strong version of tax expenditure analysis, its earlier decision in Norwood v. Harrison, prohibiting state textbook loans to segregated private schools, would likely have been controlling because that case could have been interpreted to mean that no equivalent economic aid186 could flow to segregated schools. But instead, the Court construed the meaning of “charitable” and concluded that racially discriminatory schools could not qualify.187 The Court cited its own earlier Norwood decision as only one of many cases evincing a fundamental public policy against race discrimination in education.188

The Court’s approach, though criticized,189 is consistent with its

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184. See Bob Jones, 461 U.S. at 595.
185. See Norwood v. Harrison, 413 U.S. 455 (1973)
186. While the programs clearly operated differently, the dollar benefit to private schools certainly could have been the same.
187. This was the case even though Bob Jones University was clearly an “educational” institution per I.R.C. § 501(c)(3) and even though Bob Jones University claimed a free exercise justification for its policies.
188. See Bob Jones, 461 U.S. at 593.
189. Although commentators have criticized Bob Jones’s approach of adding a common law charitableness requirement and allowing the IRS to determine which organizations contravene public policy, it continues to be the law. See, Note, The Independent Sector and the Tax Laws: Defining Charity in an Ideal Democracy, 64 S. CAL. L. REV. 461 (1991); Note, The Revocation of Tax Exemptions and Tax Deductions for Donations to 501(c)(3) Organizations on Statutory and Constitutional Grounds, 30 UCLA L. REV. 156, 172-74 (1982). But see SURREY & Mc DANIEL, TAX EXPENDITURES, supra note 13, at 127 (arguing that the tax benefits provided to charitable organizations necessarily made the IRS a participant in defining racial policies). Whether it was wise for the Court to refine the statutory definition by adding the public policy limitation, the resulting precedent is much narrower than it would have been if the Court had held that direct expenditures and
interpretation of the equal protection clause. Given the strong intent requirement under current doctrine, tax-based aid to discriminatory schools would be unconstitutional only if a court finds evidence of a government purpose to discriminate in the taxing scheme. The charitable contribution deduction is the key provision, and there is no evidence that it was adopted with government intent to discriminate.\textsuperscript{190} Neither the foreseeability that aid would flow to a discriminatory institution nor the private discriminatory intent of supporters of Bob Jones University (and Smith College) is relevant to the constitutionality of the taxing scheme. A more fulsome interpretation of equal protection would be necessary to impose an affirmative obligation on the government to withhold from certain classes of recipients benefits that are generally available on an entitlement basis.\textsuperscript{191}

The racial and gender bias in the Code, while clearly present,\textsuperscript{192} is too subtle to be explained by any explicit discriminatory purpose—it is in the choices that Congress makes as compared to the choices it might have made.\textsuperscript{193} The purpose may reflect a subtle or coded gender or racial bias. Although it is unthinkable that any committee report would offer an explicitly racist or sexist reason for its legislation, some of the arguments made in debates over tax legislation can be interpreted as discriminatory rhetoric aimed at particular groups. For example, the call for protection of the traditional family through the Code, made explicitly by some

tax expenditures are constitutional equivalents.

In addition to its doctrinal moderation, \textit{Bob Jones} reflects an institutional compromise—Congress generally has unfettered power in questions of taxation, while the courts are the final arbiters of individual rights. If tax expenditure analysis is constitutionalized so that the holding of VMI must apply to tax subsidies because they are equivalent to direct grants, then the courts would have to distinguish “real” taxes from spending through the Code.

190. There is also no evidence that it is administered in a discriminatory way. \textit{See infra} notes 214-218 and accompanying text.

191. \textit{See Part I.I.D. infra.}


193. For example, in 1997 Congress chose to grant a tax credit to all families with children, rather than increasing the credit for families with work-related child-care expenses. \textit{Compare} I.R.C. §§ 24 and 21. This choice increases the tax benefits available for families already benefiting from the imputed income enjoyed (but not taxed) when one spouse stays home to take care of the children. Although Congress did not consider these two choices as alternatives to one another, the choice it made, compared to a narrow range of alternative choices dealing with the same issue (the cost of raising children) shows that Congress failed to choose the route that would have more directly encouraged women to remain in the workforce while raising children.
legislators,\textsuperscript{194} can be interpreted as an argument against workplace equality for women or intolerance for homosexuals.

Although discriminatory purpose may be speculative or ambiguous, many tax provisions have discriminatory effects.\textsuperscript{195} Some provisions seem to disproportionately burden blacks compared to whites.\textsuperscript{196} For example, the marriage penalty/bonus in the current rate structure, which is an unavoidable by-product of a progressive system that allows joint filing,\textsuperscript{197} is more likely to impose a penalty on black couples and a bonus on white couples due to the different income and work patterns of black and white couples.\textsuperscript{198} The alternative to a joint filing system, mandatory individual filing, would, therefore, have a less discriminatory effect on black couples. Similarly, the home mortgage deduction disproportionately benefits whites, who are more likely to own homes than blacks, and has been claimed to contribute to racial segregation in housing.\textsuperscript{199}

Facially neutral tax provisions also operate to create behavioral biases that prevent women from achieving full economic equality.\textsuperscript{200} The joint filing system often imposes high average rates of tax on married women's income because wives are more likely than husbands to be secondary wage earners.\textsuperscript{201} The child tax credit\textsuperscript{202} operates to discriminate against working women because it is equally available to families with untaxed imputed income from household services (\textit{i.e.} where the wife stays at home) and families who must pay for such services with after-tax income. Congress' alternative choice of providing an equally valuable child care credit would have been

\textsuperscript{194} See, \textit{e.g.}, Contract with America, 140 CONG. REC. H9526-01 (Rep. Gingrich outlines the contract).

\textsuperscript{195} Discriminatory impact may be sufficient for a violation of statutory provisions. In \textit{McGlotten v. Connally}, the court considered whether the tax benefits at issue violated the Civil Rights Act. \textit{See supra} notes 176-80 and accompanying text.

\textsuperscript{196} \textit{See} Moran & Whitford, \textit{supra} note 192.


\textsuperscript{198} \textit{See} Dorothy A. Brown, \textit{The Marriage Bonus/Penalty in Black and White}, in \textit{TAXING AMERICA} 45 (Karen B. Brown & Mary Louise Fellows eds., 1996). Whether a particular couple has a marriage penalty or bonus under the current rate structure depends on their joint income and each spouse's relative share of it. Generally, couples in which one spouse earns less than 20\% of the total family income receive a marriage bonus and spouses who each contribute equally to family income suffer the greatest marriage penalty. \textit{See id.} at 47.


\textsuperscript{200} \textit{See} MCCAFFERY, FAMILY, \textit{supra} note 133.

\textsuperscript{201} \textit{See} Blumberg, \textit{supra} note 150; Christian, \textit{supra} note 57; Gann, \textit{supra} note 150.

more advantageous to families with women in the workplace, and could have partially alleviated the penalty that two-earner couples suffer from joint filing.

Despite their discriminatory effects, these provisions will not trigger heightened scrutiny absent a showing of discriminatory intent. Moreover, all these provisions can be explained by a variety of "neutral" nondiscriminatory goals.\textsuperscript{203} The joint filing system offers "couples neutrality," taxing equal-earning couples equally, regardless of the allocation of earnings within the couple.\textsuperscript{204} The home mortgage deduction encourages home ownership and the community stability that such ownership provides. The child credit recognizes the reduced ability to pay tax of families who must support children, and can be understood as an extension of the dependency exemption.\textsuperscript{205}

The tax law seems to have a disproportionate impact on racial minorities partially because of the unequal distribution of wealth in this country.\textsuperscript{206} Facial distinctions in the Code are often based on income level, but the Supreme Court has held that the poor are not a suspect class, and therefore, differentiation based on economic status does not give rise to strict scrutiny.\textsuperscript{207} Thus, many provisions that burden blacks compared to whites can be justified based on arguments about economic status, rather than race.\textsuperscript{208} Congressional decisions about taxation that can be defended on the basis of income measurement and differentiation based on income will always have a

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\textsuperscript{203} As Professor Alstott has pointed out, the concept of neutrality in the tax law is somewhat unclear, and seems to include both the idea of "equal taxation" as well as the economic concept of "decisional neutrality." See Alstott, supra note 148, at 2012-14. The idea of neutrality in equal protection jurisprudence is clearly not the decisional neutrality of economic analysis. In requiring that policymakers make race-blind decisions, it may be closer to the idea of equal taxation. This concept of neutrality implies an absence of taint from racial motivations. If tax provisions are adopted solely to raise revenue, then they are protected from equal protection challenge because they lack government intent to discriminate. See Part II.B. infra. The idea of race-neutrality has been criticized in the equal protection literature. See, e.g., BARBARA J. FLAGG, WAS BLIND, BUT NOW I SEE: WHITE RACE CONSCIOUSNESS & THE LAW (1998) (explaining how "transparent" white decisionmaking, which is ostensibly race-neutral, perpetuates white racial advantage).

\textsuperscript{204} See Bittker, supra note 77; Ferguson, supra note 163.

\textsuperscript{205} See I.R.C. § 151.

\textsuperscript{206} See STATISTICAL ABSTRACT OF THE UNITED STATES, Tables 717, 719, 723, 726, 742 (1997) (providing comparisons of income for white and black households); KEVIN PHILLIPS, THE POLITICS OF RICH AND POOR: WEALTH AND THE AMERICAN ELECTORATE IN THE REAGAN AFTERMATH 207 (1990) (showing that the typical black family's income is only 56% of typical white family's income).


\textsuperscript{208} Since there is no constitutional prohibition, disparate effects on the poor are virtually guaranteed to pass constitutional muster. Professors Beverly Moran and William Whitford have argued that the Code systematically disfavors blacks, even if income is held constant. See Moran & Whitford, supra note 192, at 757.
rational basis justification.\textsuperscript{209}

Even if tax statutes are safe from constitutional attack, administration of the tax laws may still be subject to equal protection challenge even without resort to tax-expenditure analysis.\textsuperscript{210} The Code is only the beginning of the large government bureaucracy that taxes the citizens, and it has lately become much more fashionable to attack the Internal Revenue Service than the Congress.\textsuperscript{211} The Supreme Court has been willing to invalidate administrative practices pursuant to statutes, even where the statutes themselves are nondiscriminatory.\textsuperscript{212} Thus, the intent requirement can be satisfied at the level of administrative decisionmaking if a pattern of purposeful discrimination in administration can be proven.\textsuperscript{213}

For example, even if section 501(c)(3) of the Code is general enough to pass constitutional muster on its face, application of that section to authorize exemptions for racially discriminatory private schools, such as Bob Jones University, could potentially violate equal protection. That conclusion would depend on the constitutional significance of the Internal Revenue Service’s decision to grant a tax exemption to racially discriminatory organizations. One can argue that the government actively approves of a private party’s discrimination by affirmatively granting a discriminating party an exemption and placing that organization on the official and public list of approved organizations.\textsuperscript{214} That list could be evidence that “so implicates the federal government in a private [person’s] activities that, as a matter of substantive equal protection law, the government becomes a partner in the [private person’s] purposeful . . .

\textsuperscript{209} See supra notes 54-57 and accompanying text.

\textsuperscript{210} Perhaps the administration of prior Code § 1071 would have been vulnerable to an equal protection attack. That section relied on FCC certification, which the FCC would provide to encourage minority ownership of radio stations, even though the statute did not contain any race-based criterion. Congress repealed § 1071 in 1995 in the Self-Employed Health Insurance Act, Pub. L. No. 104-7, 109 Stat. 93 (1995).


\textsuperscript{213} Yick Wo court found that the ordinance had been applied “with a mind so unequal and oppressive to amount to a practical denial by the State of equal protection[,]” 118 U.S. at 373.

\textsuperscript{214} See Internal Revenue Service, PUBLICATION 78 (CUMULATIVE LIST OF EXEMPT ORGANIZATIONS).
Placement on the list of exempt organizations could constitute evidence of government intent to discriminate by its affirmative choice to grant a tax benefit to a discriminatory organization.

While the existence of a list of approved organizations compiled by the government provides a potential hook onto which an equal protection claim can be hung, it is nevertheless a problematic approach under current law. The grant of an exemption to an organization that discriminates is unlikely to reflect any pattern by the administrator that is "unexplainable on grounds other than race." An exemption would ordinarily be granted because the organization fulfills the requirements of the statute despite the fact that it discriminates, not because of it. Therefore, the link between government intent and private discrimination would generally be very weak in the allowance of tax exemptions. Although theoretically could, exemptions for racially discriminatory private schools never rose to the level of a pattern of administrative practice that resembles practices struck down by the Court: the Service never systematically favored discriminatory organizations over non-discriminatory organizations in its grant of exemptions.

Thus, because the Supreme Court's standard requires discriminatory purpose under Washington v. Davis, if the Internal Revenue Service had not revoked Bob Jones University's tax exemption on statutory grounds, its revocation would not have been required by the Constitution. By the same token, tax-based aid to single-sex private schools pursuant to the charitable contribution deduction are not constitutionally equivalent to VMI. Nevertheless, single-sex schools are not necessarily home free. Even without the constitutionalization of tax expenditure analysis, the combination of Bob Jones and VMI may still threaten the continued enjoyment of tax-based support by private sex-segregated institutions.

218. See Yick Wo v. Hopkins, 118 U.S. 356 (1886) (holding that none of the Chinese applicants received variances from the ordinance); Gomillion v. Lightfoot, 364 U.S. 339 (1960) (gerrymandering only explainable as attempt to disenfranchise blacks).
219. A different reading of the Court's opinion in VMI may suggest another constitutional infirmity of tax-based support of single-sex educational institutions. VMI may mean that the government may support single-sex institutions only if it supports male and female institutions equally. This reading follows from the Court's conclusion that Virginia's proposal for an all-women's institution was not equal to VMI, and therefore, could not cure the state's exclusion of women from VMI. Assuming that the separate-but-equal principle means either that the amount of support must be equal or that the institutions must be equal, tax-based support is problematic because it is impossible to
created the potential for broad application of a public policy limitation to the Code.\textsuperscript{220} VMI might be the crucial precedent for Smith and Wellesley, not because it makes tax-based aid to single-sex educational institutions unconstitutional, but because it establishes that such support is contrary to public policy.\textsuperscript{221} The public policy approach—whatever public policy is found to be—\textsuperscript{222} is a more likely guarantee that tax-based support will actually provide equal financial benefit to different kinds of institutions. Because of the entitlement-like nature of tax-based support, the government cannot ensure that the amounts of support provided to male and female institutions is in fact equal or that the institutions themselves are equal. This stems from the fact that spending through the tax code is not subject to appropriation by Congress, and the government cannot necessarily predict how many taxpayers will avail themselves of the benefits.


\textsuperscript{221} In Green v. Connally, 330 F. Supp. 1150, 1163 (D.D.C. 1971), the district court wrote that Brown v. Board of Educ., 347 U.S. 483 (1954), proclaimed the policy against racial segregation in education, 330 F. Supp. 1150, 1163 (D.D.C. 1971), suggesting that a judicial statement may pronounce a policy. While Bob Jones was being considered by the Supreme Court, the Reagan Administration noted the possible effects that it could have on single-sex institutions, and even referred to Smith College in explaining why it changed its position in the litigation from supporting the IRS's determination to supporting Bob Jones University's exemption. For the background to the Bob Jones case and a description of the Administration's flip-flop policy regarding exemptions for racially discriminatory schools, see Dale, supra note 220, at 10-14; Note, Tax-Exempt Status of Discriminatory Private Schools, 97 Harv. L. Rev. 261, 262 n.15 (1983). The Supreme Court invited William T. Coleman, Jr., to brief and argue as amicus curiae in support of the judgments below. 456 U.S. 922 (1982).

\textsuperscript{222} One can argue that Smith's eligibility for exemption under section 501(c)(3) should not be affected by VMI, reading Bob Jones narrowly, and interpreting “charitable” in section 501(c)(3) as failing to apply only to organizations that engage in racial discrimination. After the Supreme Court's decision in Bob Jones, the IRS could have used the public policy principle aggressively to deny or revoke exemptions from many organizations, and some commentators were afraid that the IRS would use its authority to favor particular organizations. See Galvin & Devins, supra note 183, at 1372-3. However, the IRS has generally limited its attacks to organizations practicing racial discrimination. See, e.g., Virginia Educ. Fund v. Commissioner, 85 T.C. 743 (1985), aff'd 799 F.2d 903 (4th Cir. 1986); Prince Edward Sch. Found. v. Commissioner, 478 F. Supp. 107 (D.D.C. 1979). This administrative practice provides some support for the argument that the public policy limitation is only about racial discrimination. This interpretation of the public policy limitation must rest on a distinction between the public policy against racial discrimination and the public policy against gender discrimination. Those distinctions have certainly been made. While there are statutes prohibiting both race and sex discrimination, the sex discrimination statutes reflect some tolerance for disparate treatment of men and women. See 20 U.S.C. § 1681(A)(5) (providing exception to Title IX for traditionally single-sex institutions). Similarly, courts have subjected sex discrimination to an intermediate level of scrutiny, rather than the strict scrutiny applied to race discrimination. See, e.g., Frontiero v. Richardson, 411 U.S. 677 (1973) (plurality); Califano v. Westcott, 443 U.S. 76
interpretation of *VMI*'s effect on the tax benefits of private single-sex institutions than the constitutional interpretations suggested above.\textsuperscript{223} As Justice Scalia wrote in his *VMI* dissent: "it is certainly not beyond the Court that rendered today's decision to hold that a donation to a single-sex college should be deemed contrary to public policy and therefore not deductible if the college discriminates on the basis of sex."\textsuperscript{224} If gender discrimination is uncharitable, the public policy exception to charitable status will have to apply to gender discrimination as well.\textsuperscript{225}

The crucial difference between prohibiting tax-based support to single-sex institutions pursuant to the public policy limitation and prohibiting that support based on the functional equivalence highlighted by tax expenditure analysis is in the constitutionalization of the prohibition. If *VMI* establishes the existence of a fundamental public policy against gender discrimination in education so that tax exemptions for such schools violate public policy under *Bob Jones*, Congress could change that result by indicating a contrary understanding of public policy.\textsuperscript{226} Of course, a constitutional holding would mean that it could not.\textsuperscript{227}

(1979); Orr v. Orr, 440 U.S. 268 (1979). Nevertheless, if the public policy limitation in *Bob Jones* were only meant to apply to racial discrimination, then it is curious that the Supreme Court established a "public policy" exception, rather than a racial discrimination exception to charitable status under section 501(c)(3).

The law of charitable trusts does not resolve this issue. In fact, the Restatement cites *Bob Jones* as the principle current case in the definition of public policy for purposes of charitable trust law. See *RESTATEMENT (SECOND) OF TRUSTS* § 377 (c)(Supp.); see also *AUSTIN WAKEMAN SCOTT, LAW OF TRUSTS* (4th ed. 1989) § 377, p. 376.\textsuperscript{223} See text and notes 22-23, supra.


225. More than three years prior to the Supreme Court's decision in *Bob Jones*, Professor Martin Ginsburg wrote that the Service's decision to allow a charitable deduction for a gender-restricted scholarship "flagrantly disregards or misconstrues pertinent federal judicial and legislative pronouncements and manifestly frustrates federal policy." Martin D. Ginsburg, *Sex Discrimination and the IRS: Public Policy and the Charitable Deduction*, 10 TAX NOTES 27 (Jan. 14, 1980). Professor Ginsburg is the husband of Justice Ruth Bader Ginsburg, the author of *VMI*.

226. Congress could do so by amending I.R.C. § 501(c)(3). Such an amendment could either explicitly overrule the Court's decision to incorporate charitable trust law into the Code, or simply undermine the argument that there exists a fundamental public policy enunciated by all three branches of government, such as the Court found in *Bob Jones*. See *Bob Jones Univ. v. United States*, 461 U.S. 574 (1983). The *Bob Jones* Court recognized that public policy could evolve.

227. Some have criticized the Supreme Court's decision in *Bob Jones* for failing to reach the constitutional question. See *Note, Constitutional Law—Religious Schools, Public Policy, and the Constitution: Bob Jones University v. United States*, 62 N.C. L. REV. 1051 (1984); Robert M. Cover, *Foreword: Nomos and Narrative*, 97 HARV. L. REV. 4, 67 (1983) ("the minority community... deserved a constitutional commitment to
To sum up, this section has demonstrated that equal protection doctrine, as developed by the Supreme Court, does not fit well with tax expenditure analysis because of the factors that the Supreme Court has treated as important for purposes of equal protection. Economic equivalence is not relevant to substantive equal protection analysis. Because the charitable deduction (and the tax Code generally) does not facially discriminate on the basis of race or gender and can be seen as having a government intent other than discrimination, it is safe from attack under the equal protection clause.

At the same time, evidence is building that the tax law is instrumental in contributing to the continued economic inequality of minorities and women. Given that the tax law is one of the most important governmental mechanisms for redistribution of societal wealth, its constitutional impenetrability behind a wall of neutrality is unfortunate. The Code's virtual immunity from equal protection analysis and the constitutional acceptability of Bob Jones University's tax exemption should prompt the Supreme Court to reconsider whether the intent requirement of Washington v. Davis fulfills the goals of equal protection. Alternative doctrinal interpretations of the equal protection clause could lead to a different conclusion, and a different understanding of the meaning of the equal protection clause might make tax expenditure analysis a more relevant adjudicatory tool than it is under current law. The next section explores this idea.

avoiding public subsidization of racism”). Those who may have been nervous that Congress could decide to overrule Bob Jones would have felt more secure with a constitutional holding in that case. See Brief of Amicus Curiae in Support of the Judgment Below, Bob Jones University v. United States, 461 U.S. 574 (1983) (No. 83-3, 81-1) (Brief of William T. Coleman). Others have praised the Court's judicial restraint. See, Harvard Note, supra note 221. After VMI, proponents of single-sex education may be glad that the Court took the middle road in Bob Jones, confident that Congress, in its wisdom, would not allow tax subsidies to flow to racially discriminatory institutions.

228. Tax benefits raise a special equal protection concern worth mentioning here. Taxpayer choice may make tax-benefit programs an effective method for implementing direct democracy. See Saul Levmore, Taxes as Ballots, 65 CHI. L. REV. 387 (1998). While Professor Levmore is clearly correct in his observations about how tax benefits operate to implement direct democracy, it is not clear that direct democracy through the tax law is desirable. Outside of the tax context, direct democracy initiatives have been used to undermine governmental efforts at racial desegregation. See TRIBE, CONSTITUTIONAL LAW, supra note 115 § 16-17, at 1485-86 (discussing Hunter v. Erickson, 393 U.S. 385 (1969); Washington v. Seattle Sch. Dist. No. 1, 458 U.S. 457 (1982)). If increased use of direct democracy through the Code allows taxpayers to achieve, with government funds, goals the government would be constitutionally prohibited from achieving itself, then tax-based direct democracy would enlarge the private sphere in which the courts are unable to remedy injustices that the government does not commit. Such a use of the tax law would be unfortunate.

229. See infra Part II.D.
D. Tax Expenditure Analysis and Alternative Interpretations of Equal Protection

In this section, I examine how tax expenditure analysis fits into two alternative approaches to the equal protection clause: equal protection as anti-subordination\(^{230}\) and equal protection as pure protection.\(^{231}\) I discuss these alternative interpretations of the equal protection clause to illustrate how the constitutionality of tax provisions depends on the substantive interests protected by the constitutional provision at issue and how the importance of economic equivalence differs depending on those interests. In contrast to the peripheral importance of economic equivalence under the Supreme Court’s equal protection jurisprudence discussed above, the alternative interpretations of equal protection offered by these constitutional scholars would treat economic equivalence as central to the constitutional analysis. Both the anti-subordination and the pure protection models of equal protection are concerned with ending discrimination and its ill effects, and therefore, would require that courts treat tax expenditures and their economically equivalent direct expenditures alike. Both of these alternative interpretations would be informed by tax expenditure analysis because that analysis highlights how tax provisions and direct government programs can equally support subordination.

Professor Ruth Colker has described the anti-subordination approach as seeking to “eliminate the power disparities between men and women, and between whites and non-whites, through the development of laws and policies that directly redress those disparities.... [I]t focuses on society’s role in creating subordination.”\(^{232}\) Rather than showing that there was a discriminatory intent behind a neutral policy, as under the current anti-discrimination interpretation of the equal protection clause, the anti-subordination interpretation would require that the plaintiff show disparate impact and subordination of the disadvantaged group.\(^{233}\)

As described in the prior section, the insuperable hurdle in challenging the constitutionality of most tax provisions under current law comes from the intent requirement of Washington v. Davis. By dispensing with that element of proof, the anti-subordination approach allows plaintiffs challenging tax provisions that have a


\(^{231}\) See ROBIN WEST, PROGRESSIVE CONSTITUTIONALISM 20-30 (1994).

\(^{232}\) Colker, supra note 230, at 1007-8.

\(^{233}\) See id. at 1014-15.
disparate impact on women and minorities to present a prima facie case based on empirical evidence of the effect of facially neutral statutes on different groups. Under this approach, once a prima facie case is made, the government may defend its program by offering an explanation for how the discriminatory impact alleviates subordination of the affected group.\footnote{See id. at 1015.}

The anti-subordination approach would treat tax provisions differently than the anti-discrimination approach because the anti-subordination approach is concerned with both the intended and unintended effects of a tax provision on groups of people. Therefore, the financial aid that flows to private parties through the Code becomes relevant to the constitutional inquiry regardless of government intent or neutral explanation. The economic equivalence of tax expenditures and direct spending is instructive because it reveals the scope of government support of private discriminatory practices. Under the anti-subordination approach, the economic support that flows to private discriminators promotes subordination, and therefore, is unconstitutional.

Pursuant to the anti-subordination interpretation, the constitutionality of tax benefits flowing to groups and individuals would more closely track the constitutionality of direct government spending with the same economic effect. Any economic support of subordination would be unacceptable; tax benefits would be constitutionally equivalent to direct expenditures with the same economic effect. Returning to our paradigm cases, tax benefits for Bob Jones University would be unconstitutional because by providing economic aid, they would support continuing subordination of blacks. On the other hand, tax benefits for Smith College could be constitutional as long as they help to remedy historical subordination of women.\footnote{This Article takes no position on the desirability of single-sex education for women or the constitutionality of public single-sex education for women. Following VMI, there has been considerable focus on these issues. See e.g., Symposium, Finding a Path to Gender Equality: Legal and Policy Issues Raised by All-Female Public Education, 14 N.Y.L. SCH. J. HUM. RTS. Part 1 (1997); Carrie Corcoran, Single-sex Education After VMI: Equal Protection and East Harlem's Young Women's Leadership School, 145 U. PA. L. REV. 987 (1997); Christopher H. Pyle, Women's Colleges: Is Segregation by Sex Still Justifiable after United States v. Virginia?, 77 B.U. L. REV. 209 (1997); Linda L. Peter, What Remains of Public Choice and Parental Rights: Does the VMI Decision Preclude Exclusive Schools or Classes Based on Gender?, 33 CAL. W. L. REV. 249 (1997); Amy B. Bellman, The Young Women's Leadership School: Single-Sex Public Education After VMI, 1997 WIS. L. REV. 827 (1997).}
endorsed by Professor Robin West would treat economic equivalence with unacceptable direct spending as central in evaluating tax benefits. Professor West's pure protection model of equal protection "requires the state to affirmatively protect each person's exercise of his or her natural or human rights." It focuses on the state's duty to protect all people from private harm by others. If the state allows one group to be subjected to the will of another group, then it is not providing the subjugated group the equal protection of the laws. The pure protection model dispenses with both the intent requirement of *Washington v. Davis* and the state action requirement because, according to West, the equal protection clause gives the state an affirmative obligation to protect its citizens from private discrimination.

If the equal protection clause is interpreted in this affirmative manner, then the government has a much greater burden than under the anti-discrimination approach of current law. While the anti-discrimination approach allows the government to support people and organizations who discriminate as long as it does not explicitly discriminate itself, the pure protection model requires that the government take an active role in eliminating private discrimination. Refraining from providing economic support in any form would thus be a minimal requirement under this approach. If tax benefits provide economic support to people who privately discriminate, then the government violates the Constitution by assisting those people and failing to provide protection to the subjugated citizens. "[W]here the state acquiesces in the subjugation [of one class of citizens to another], the state has violated its promise of equal protection." The allowance of tax benefits, even under a neutral Code provision, would certainly constitute such acquiescence.

Thus, the economic equivalence of tax benefits and direct spending could be illuminating to courts adjudicating equal protection challenges to tax provisions, but only if the Court changes its interpretation of the equal protection clause. I have described the relevance of economic equivalence to equal protection adjudication under current law and these alternative interpretations to demonstrate how the qualified version of tax expenditure analysis that I advance is sensitive to the substantive constitutional interests in each case.

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237. West describes this conception of equal protection as ensuring the sole sovereignty of the state. *See id.* at 25.
238. *See id.* at 34.
239. *Id.* at 37.
E. Tax Expenditure Analysis and Establishment of Religion

This section applies the same mode of analysis already employed in the equal protection arena to consider the constitutionality of tax benefits under the establishment clause. Because that methodology requires consideration of the policies underlying each constitutional provision, this section considers the interests protected by the establishment clause and how tax benefits and direct spending differ with respect to those interests.

Tax benefits currently enjoyed by religious organizations amount to substantial financial support. While direct funding of religious organizations creates establishment clause concerns, the mere fact of some government financial support to religious institutions is insufficient to create an establishment of religion: the Supreme Court has held that the government may support religious organizations as long as that support has a secular purpose, does not have the primary effect of advancing or inhibiting religion, and does not produce excessive entanglement between the religious institution and the state.

240. The Tax Expenditure Budget lumps together the foregone revenue from all charitable deductions, other than education and health, without separately listing religion. The 1998 estimate was over $16 billion for individuals. See ANALYTICAL PERSPECTIVES, supra note 5, at 44. Religious organizations collect more than $50 billion each year. See Biddle, in WHO BENEFITS, supra note 142, at 92.

Tax benefits constitute significant financial support even if we assume that only the deductibility of contributions, and not the exemption from tax, constitutes a government subsidy. The tax exemption for religious organizations may be of no monetary value to them if they would have no taxable income had they been subject to an income tax. See Bittker & Rahdert, supra note 67, at 314 (discussing the computation of taxable income for nonprofit organizations). The greatest subsidy from the exemption may come from the exemption of tax for endowment earnings. See Evelyn Brody, Agents Without Principals: The Economic Convergence of the Nonprofit and For-Profit Organizational Forms, 40 N.Y.L. SCH. L. REV. 457 (1996).

One of the problems with both the case law and commentary analyzing the constitutionality of tax benefits is that they are generally insensitive to the level of economic support provided by a statutory benefit. See, e.g., Brown, supra note 117 (gets it wrong re: economic support from state property tax exemption, which clearly provides support even though federal income tax exemption does not), Bob Jones, (failing to distinguish between the deductibility of contributions and exemption from tax). But see McGlotten v. Connally, 338 F. Supp. 448 (D.D.C. 1972) (analyzing 501(c)(7) as different from 501(c)(8), from perspective of government subsidy) and Bittker & Kaufman, supra note 19.


242. These three requirements were established by the Supreme Court in Lemon v. Kurtzman, 403 U.S. 602, 612-613 (1971). While the Lemon test has been subject to criticism, see Lamb's Chapel v. Center Moriches Union Free Sch. Dist., 508 U.S. 384, 399 (1993) (Scalia, J., dissenting), and ignored on occasion, see Board of Educ. of Kiryas Joel v. Grumet, 512 U.S. 687 (1994) (O'Connor, J., concurring, Scalia, J., dissenting), it has not been overruled.
Like in equal protection analysis, the economic equivalence emphasized by tax expenditure analysis is not of primary importance in establishment clause jurisprudence. Rather, government intent again plays a central role, because the government may not choose to favor religion. Therefore, tax-based funding of religious organizations, through the charitable deduction, may be constitutionally distinguishable from direct government appropriations to churches due to the separability of government intent and taxpayer intent.\textsuperscript{243} In addition, establishment clause jurisprudence is concerned with the nature and degree of the government's involvement with religion. Such concerns, which are not raised in the equal protection context, suggest that non-economic differences between tax benefits and direct spending may be constitutionally relevant.

In \textit{Rosenberger v. Virginia} the Supreme Court declined to constitutionalize tax expenditure analysis in an establishment clause case, despite Justice Thomas's plain invitation to do so. Although not about a tax expenditure, the case implicitly rejects the functional equivalence of tax expenditure analysis. The case arose because the University of Virginia refused to authorize payments out of its student activities fund for the printing costs of a student publication, Wide Awake Productions (WAP), on the ground that the publication was not eligible because it "primarily promote[d] ... a particular belief in or about a deity or an ultimate reality."\textsuperscript{244}

In requiring WAP to be funded, the majority distinguished the facts before it from another scenario that it conceded would be unconstitutional—"a general public assessment designed and effected to provide financial support for a church."\textsuperscript{245} The court concluded that WAP's funding was different than "direct money payments to an institution or group that is engaged in religious activity."\textsuperscript{246} The most important factor leading to this conclusion seems to have been that the University paid outside printers, rather than transferring the amounts directly to WAP.\textsuperscript{247} The Court stressed that "no public funds flow[ed] directly to WAP's coffers."\textsuperscript{248} The Court therefore concluded that these payments were the same as

\textsuperscript{243} This discussion assumes that direct government appropriations specifically to churches would be unconstitutional.


\textsuperscript{245} \textit{Id.} at 841. The majority wrote: "The Court of Appeals (and the dissent) are correct to extract from our decisions the principle that we have recognized special Establishment Clause dangers where the government makes direct money payments to sectarian institutions." \textit{Id.} at 842.

\textsuperscript{246} \textit{Id.} at 842.

\textsuperscript{247} \textit{See id.} at 842-45.

\textsuperscript{248} \textit{Id.} at 842.
providing printing facilities to all students on a neutral basis, noting: "It is, of course, true that if the State pays a church's bills it is subsidizing it, and we must guard against this abuse. That is not a danger here."\textsuperscript{249}

The \textit{Rosenberger} opinion appears to set up two conditions that must be present for a tax to violate the establishment clause:\textsuperscript{250} (1) it must be collected as a general public assessment, and (2) it must be directly paid to an organization engaged in religious activity. These conditions are formal, rather than functional, and they limit the exactions that can violate the establishment clause. The majority's reliance on these formal distinctions suggests that the Court would consider the similarly formal distinctions between direct expenditures and tax expenditures to be legally significant. Tax expenditures would fail to constitute taxes under the \textit{Rosenberger} majority's definition of a tax: the spending inherent in tax expenditures is indirect by definition because the subsidy never actually moves through the government's hands to the organization's coffers.\textsuperscript{251}

For different reasons than the majority, the dissenting justices in

\textsuperscript{249} Id. at 844. The majority's opinion did not explain why payment of the printer's bills was not an equivalent subsidy. \textit{See id.}

\textsuperscript{250} \textit{Rosenberger} defines what constitutes a "tax" where that definition is constitutionally relevant. The Court perceived a collision of free speech with establishment of religion, and the choice of which of these constitutional values would prevail turned on the definition of a tax. If the student activity fee constituted a tax, then funding WAP would have violated the Establishment Clause; if it were not a tax, then refusal to fund WAP would be an unconstitutional restriction on speech. \textit{See id. at 840.}

Although the majority conceded that the student activity fee was an "exaction upon the students," it concluded that it was not a "tax" because it defined a tax as an amount for the support of the government. \textit{See id.} at 840-41. The definition of a tax adopted by the majority is very narrow—it must be a levy on the general public that raises revenue for the support of the government and which the government may use for "unlimited purposes." \textit{Id.} This definition would exclude numerous exactions under current law that most people would consider taxes such as excise taxes, federal payroll taxes that are subject to trust fund restrictions and local property taxes that are dedicated to specific uses. In her concurring opinion, Justice O'Connor elaborated on the majority's definition of a tax. She distinguished the student activity fee from a tax because (1) an objecting student might be able to opt out of paying the fee, and (2) the fees constituted a "common pool" collected from students that was distributed to them and by them. \textit{Id.} at 851-52. In contrast, the dissent's definition of a tax was much broader; the dissenters argued that the fee was a tax because it was collected by virtue of the coercive powers of the state. \textit{See id. at 873.}

\textsuperscript{251} Tax expenditure analysis conceptualizes tax expenditures as first collected and then spent by the government, but in reality, they are taxes foregone, not taxes actually collected and disbursed. Sometimes, tax expenditures may be direct in the sense that the subsidy goes directly from the government to the recipient, rather than through a third party, such as in the case of the exemption for investment income of tax-exempt organizations. \textit{See Brown, supra} note 117. However, some tax benefits, like the charitable deduction, are also indirect in that they flow through a third party on their way to the ultimate recipient. \textit{See infra} notes 287-89 and accompanying text.
Rosenberger also seem to reject the functional equivalence of tax expenditure analysis. In categorizing Rosenberger as an unconstitutional direct funding case, the dissent distinguished it from the constitutionally acceptable indirect-aid cases. The direct/indirect question was critical to the dissent because in the cases of indirect aid, such as tax benefits that flow to religious organizations by virtue of the deduction allowed their contributors, religious institutions benefit as a result of the choices made by individuals. The dissent argued that the imposition of individuals between the state and the religious institution is a distinction of substance that can support different outcomes under the Constitution, while the distinction between paying WAP’s printer and paying WAP directly is a “formalism” that “cannot be the basis of a decision of Constitutional law.”

Thus, eight members of the Supreme Court were unmoved by the basic premise of tax expenditure analysis—the economic equivalence of tax expenditures and direct expenditures—even though their conclusions led them in opposite directions in the case at bar. In contrast, Justice Thomas’s concurrence explicitly adopted tax expenditure analysis and used that analysis in a novel and aggressive way.

Justice Thomas adopted tax expenditure analysis, referring to it explicitly in arguing that direct spending should be treated the same as indirect spending. But he parted from the Surrey school after embracing the economic equivalence highlighted by tax expenditure analysis and proceeded to turn its reasoning upside-down. Instead of arguing for scrutiny of tax expenditures on the same terms as direct expenditures, as do the advocates of tax expenditure analysis, he argued against scrutiny for direct spending on account of the existence of equivalent tax expenditures. Justice Thomas called upon the longstanding acceptance of indirect aid to religion, in the form of tax expenditures, to argue that direct spending to aid religion is consistent with established law. Thus, Justice Thomas used tax expenditure analysis to reach a normative conclusion about direct spending, while Surrey used tax expenditure analysis to bring attention to the absence of normative analysis for spending provisions in the Code. By couching his argument in tax expenditure language, Justice Thomas made his radical position, shared by no other member of the court, seem grounded in current law and practice. Using tax expenditure rhetoric, he argued for direct government funding of core religious activities.

252. See Rosenberger, 515 U.S. at 886 (Scalia, J., dissenting).

253. Justice Thomas interpreted the establishment clause as requiring government neutrality among religions, rather than as a prohibition against funding any religion. See Rosenberger, 515 U.S. at 854-55. However, tax expenditure analysis cannot completely
Notwithstanding Justice Thomas’s concurrence in *Rosenberger*, the Supreme Court has steadfastly refused to adopt tax expenditure analysis into the basic structure of establishment clause jurisprudence. In *Walz*, the landmark case in which the Supreme Court upheld a property tax exemption for churches, the Court refused to legally equate economically equivalent tax benefits and direct subsidies. It has since refused to repudiate that stance. When the Court has invalidated tax programs that benefit religious organizations, it has done so on a case-by-case, facts-and-circumstances basis, rather than by wholesale adoption of tax expenditure analysis. While the Court is clearly aware of the economic equivalence of tax and direct expenditures, it has resisted the temptation to turn that economic equivalence into constitutional equivalence, despite the call of some members of the Court to do so.

The Supreme Court has identified factors other than the fact of financial support as important in establishment clause analysis. It support Justice Thomas’s conclusion. Justice Thomas’s argument requires that there be some explanation of how tax expenditure funding of religion is neutral, without undermining the equivalence of tax expenditure funding and direct funding on which Justice Thomas relies. If the explanation depends on the individual choice of contributors, then it proves too much because it supports the dissent’s view that tax expenditures and direct expenditures are not equivalent. Tax expenditures subsidize established religions with rich adherents much more than fringe religions with poorer adherents because the subsidy from the tax deduction for charitable contributions favors those contributors in high tax brackets and their chosen religions. Even popular religions, which would be well-funded if funding were determined on a per capita basis, with poor believers are less well-funded because the tax benefits attaching to those contributions are small or nonexistent.  

254. Justice Brennan wrote: “Tax exemptions and general subsidies ... are qualitatively different [t]hough both provide economic assistance.” *Walz*, 397 U.S. at 690 (Brennan, J., concurring).


258. See Agostini v. Felton, 117 S. Ct. 1997 (1997) (federally supported special education teachers may provide services on parochial school premises); Board of Educ. of Cent. Sch. Dist. No. 1 v. Allen, 392 U.S. 236 (1968) (textbook loans to sectarian schools upheld); Everson v. Board Of Educ., 330 U.S. 1 (1947) (public busing of parochial school students upheld). One exception may be Meek v. Pittenger, 421 U.S. 349 (1975), in which the Court was concerned about Pennsylvania’s $12 million appropriation for material and equipment available for loan to private schools. In *Meek*, the Court struck down a state program because the public aid to sectarian schools was “neither indirect or incidental” and “even though ostensibly limited to wholly neutral, secular instructional material and
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has been particularly concerned about the appearance of government sponsorship of religion, and the Court has allowed financial support to flow to sectarian institutions, as long as that support does not carry a message of government endorsement.\textsuperscript{259} Government may not give the impression that it prefers a particular religion, or religion as opposed to non-religion.\textsuperscript{260} The message that the government sends by providing support to sectarian institutions seems to be more important than the fact that there is any financial support. Therefore, if tax-based aid fails to send a message where economically equivalent direct aid would, then tax-based aid and direct aid may be constitutionally distinguishable. Under the charitable deduction, taxpayers choose to direct their tax savings to the religious institutions of their choosing. The imposition of the taxpayer is significant for purposes of the establishment clause because she disrupts the symbolic connection between the state and the religious organization that is suspect under the establishment clause.\textsuperscript{261}

If the constitutional imperative turns on the government’s expression of preference for particular religions, then tax-based aid is distinguishable from direct aid because the general availability of the charitable deduction treats all religions equally, and allows taxpayers, rather than government, to choose among religions.\textsuperscript{262} If that is all that the establishment clause requires, then the difference between tax-based support and direct support of religion is of constitutional magnitude, and tax-based programs could be acceptable even where their economically equivalent direct-spending counterparts would not.\textsuperscript{263} However, the administration of the exemption would be

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\textsuperscript{261} See Zorach v. Clauson, 343 U.S. 306, 312 (1952) (“concert or union or dependency” of church and state).

\textsuperscript{262} The exception to this may come from the government’s necessary determination about whether an organization is “religious” under the statute. Because the statute includes religious organizations as an independent category, the IRS is necessarily in the business of deciding whether an institution qualifies as “religious.” See, e.g., Davis v. Commissioner, 81 T.C. 806 (1983), aff'd 767 F.2d 931 (9th Cir. 1985); Granzow v. Commissioner, 739 F.2d 265 (7th Cir. 1984) (tax fraud ministry cases). See generally, \textit{BRUCE R. HOPKINS, THE LAW OF TAX-EXEMPT ORGANIZATIONS} § 9.2 (6th ed. 1992) (discussing the concept of “religious” in I.R.C. §501(c)(3)).

\textsuperscript{263} This seems to be Justice Thomas’s view of what the framers intended that the Establishment Clause protect. See Rosenberger v. Virginia, 515 U.S. 819, 881 n.7 (1995) (Souter, J., dissenting).
particularly important in determining whether the government prefers some religions over others.264

While individual choice is relevant to the constitutional inquiry into government purpose to favor religion, it does not necessarily insulate the government from establishment clause violations. The significance of taxpayer choice depends on the government's definition of the realm of allowable choices that individuals can make. Only the combination of broad, neutral definitions for eligibility determination and meaningful choice for funding recipients separates the taxpayer's intent to favor religion from the government's intent to subsidize a broader, more general class of recipients.265 Where the government narrows the allowable recipient class, then individual choice is illusory. As discussed above, it is possible to make arguments for and against the current-law allowance of tax-deductible contributions to religious organizations.266 On one hand, the availability of the deduction to a broad range of organizations belies any government intent to favor religion: since individual taxpayers make the ultimate determination about where government funds go, and can choose from a wide variety of organizations, taxpayer choice helps to refute the claim that the government's purpose in adopting a statute is to support religion.267 On the other hand, the laundry-list provision should not provide a means of obfuscation for unconstitutional government support.268

The Supreme Court has identified excessive entanglement with religion as an additional concern raised by the establishment clause. Direct spending through government bureaucracy is likely to involve greater entanglement than tax-based support.269 Taxpayer choice makes the taxpayer the fact-finder for eligible recipients, avoiding


265. See supra Part II.B.

266. See supra notes 136-42 and accompanying text.

267. But see supra note 137 and accompanying text.

268. The laundry-list provision may mean that the government's subsidy is not available on the neutral basis as allowed by the Court's establishment clause cases. See Witters v. Washington Dept. of Servs. for the Blind, 475 U.S. 1091 (1986) (vocational services available to all visually handicapped persons); Zobrest v. Catalina Foothills Sch. Dist., 509 U.S. 1 (1993) (state could pay for deaf student's sign language interpreter even though student attended a religious school).

269. The Court has noted that the annual appropriations process itself presents a "political entanglement" problem because it "provides successive opportunities for political fragmentation and division along religious lines." Meek v. Pittenger, 421 U.S. 349, 372 (1975).
government entanglement with religious organizations at the application-for-funds stage, and tax-based programs are generally characterized by minimal monitoring of benefit recipients.\textsuperscript{270} Tax-based aid is also less likely to present entanglement problems than direct aid because the government does not need to deal directly with a religious institution in providing tax-based aid to it; the charitable deduction subsidizes the institution’s donor.\textsuperscript{271} Whereas a direct grant is an arrangement between government and the recipient, “a tax exemption [sic deduction] is a matching fund arrangement entered into between government and the recipient’s contributors.”\textsuperscript{272} Thus, tax-based and direct aid programs may involve constitutionally distinct levels of government entanglement.

By nature, taxation requires some entanglement with all institutions. Unlike direct spending programs, which require state involvement only for organizations that are eligible for such programs, the tax system affects everyone. If it grants the exemption, it must monitor eligibility for exemption; if it does not, then it must collect the tax.\textsuperscript{273} In some cases, this requires the Internal Revenue Service to evaluate whether an organization is, in fact, a religion.\textsuperscript{274}

The courts prefer to avoid this question. For example, in Hernandez v. Commissioner,\textsuperscript{275} deductions to the Church of Scientology were disallowed on the ground that the amounts given to the church were payments for services (albeit religious services) rather than charitable contributions. As Justice O’Connor pointed out in dissent, the Supreme Court’s reasoning is hard to square with the accepted deductibility of quid-pro-quo type payments to mainstream religions.\textsuperscript{276} The underlying issue, which was not explicitly addressed—but which would have made the case more clear—was whether the Church of Scientology qualified as a religious organization. Some might find the government’s power to decide

\textsuperscript{270} While it is clear that Congress could design direct spending programs with little administrative oversight, the fact remains that a major difference between tax expenditures and direct spending programs is that tax programs are largely self-administered.

\textsuperscript{271} See infra notes 289-292 and accompanying text.

\textsuperscript{272} Greenya v. George Washington University, 512 F.2d 556, 561 (D.C. Cir. 1975).

\textsuperscript{273} Walz v. Tax Commission of the City of New York, 397 U.S. 664, 692 (Brennan, J., concurring).


\textsuperscript{275} 490 U.S. 680 (1989).

\textsuperscript{276} See id. at 708-712.
what constitutes a religion for purposes of section 501(c)(3) to be an intolerable entanglement. On the other hand, if a religious organization is not exempt, then the government is involved with that organization in its attempt to collect tax. Whether exemption or non-exemption produces more entanglement with religion is a question on which people may disagree.

Another important component of establishment clause jurisprudence focuses on whether support to religion is incidental. The Supreme Court seems untroubled by incidental support to religion, and does not consider such support to have the unconstitutional effect of advancing religion. Tax-based support from the charitable deduction may qualify as incidental for establishment clause purposes because of the requirement of taxpayer cost in all charitable contributions. Tax benefits can be distinguished from simple government appropriations because the government only partially funds a religious organization with tax-based aid.

As long as tax rates remain below 100%, tax benefits in the form of deductions require that taxpayers incur some after-tax economic cost in order to choose how to allocate government funds. For example, for a taxpayer with a marginal rate of 28%, the government chips in 28 cents for each 72 cents that the taxpayer contributes to charity. While much has been made of the government’s contribution of 28%, the significance of the taxpayer’s required contribution of 72% has been little considered. This requirement of individual cost distinguishes the tax expenditure method of funding religious organizations that we have in current law from both a taxpayer


278. See Walz, 397 U.S. at 674 (majority belief that the exemption produced less entanglement). Cf. Judith C. Miles, Beyond Bob Jones: Toward the Elimination of Governmental Subsidy of Discrimination By Religious Institutions, 8 HARV. WOMEN’S L. J. 31, 55-58 (1985) (arguing that the exemption for religious organizations should be repealed to avoid the entanglement necessary in enforcing the antidiscrimination policy upheld in Bob Jones).


281. Credits, which generally allow taxpayers to credit only a percentage of expenses against tax, also require that taxpayers incur some economic cost.

282. A potential exception to this is the deduction allowed under current law for the fair market value of appreciated property, despite the exclusion of the built-in gain on such property from the donor’s income. When marginal tax rates exceeded 50%, it was possible for a taxpayer to shift the entire cost of a donation to the government.

283. But see Levmore, supra note 228.
designation system in which individuals could direct government funds to their favorite charities at no cost to themselves and a system of direct government grants determined by the legislature.

In the context of aid to religious organizations, individual cost is significant if it transforms the government's subsidy into incidental support. If one takes the perspective of the individual taxpayer or the exempt organization, then the level of the taxpayers' support compared to the level of the government's support may make the government's share seem small enough to be incidental. The smaller the government's share of support, the less visible is the governmental presence in the organization, and the less control over the organization the government can wield. One can argue that these limits on governmental involvement may prevent unconstitutional levels of government entanglement with religious organizations and may also weaken the message of connection between church and state that full government support would imply.

However, the argument that individual cost minimizes the government's role enough to make government support of religion incidental is problematic. Focusing on the resources of the organization may be insufficiently sensitive to the interests protected by the establishment clause. Because establishment clause analysis is designed to prevent the government from having too close a relationship with religion, the appropriate perspective from which to determine acceptability under that clause must be the government's perspective. From that perspective, it appears that the taxpayer's cost should not be significant at all; the relative support provided by the private and public sectors is not as significant as the overall level of public support and the government's goals in providing that support. That, of course, is exactly the issue posed by direct spending programs that aid religion, even those that require no cost to the individual. Whether the government's support is merely incidental must be determined in relation to the government's purpose, not in relation to the support of others.

Another argument for the incidental nature of tax-based support to religious organizations may stem from the indirectness of tax-based support. All tax benefits are indirect in the sense that the

284. See Zelinsky, supra note 19 at 409 (suggesting that the equivalence of tax benefits and direct expenditures may depend on the perspective from which the issue is analyzed).


286. For example, government support for services for the homeless that happen to support church-based soup kitchens or subsidies for parents who incur private school tuition costs would involve the same analysis regardless of the tax-based nature of the support or the level of co-payments made by individuals.

287. In distinguishing constitutional textbook loans from unconstitutional equipment
government does not directly disburse funds for any particular programs, but rather refrains from collecting tax that would otherwise be paid. The subsidy that religious organizations receive under the charitable contribution deduction is also indirect in another way: the subsidy flows directly to the contributor, rather than the religious organization, and the contributor can choose to pass that subsidy on or keep it. In the case of the charitable contribution deduction, the incidence of the tax benefit often falls on someone other than the taxpayer who claims the benefit because the contributor saves tax by virtue of the deduction and chooses whether to adjust the contributed amount to account for the savings.

For example, if T would contribute $100 to her church without the charitable contribution deduction, and she is in the 28% tax bracket, she may decide to contribute $100, with the deduction reducing her after-tax cost of the contribution to $72. She also may gross up her contribution by the tax savings so that she continues to bear a $100 after-tax cost for the gift. In that case, her contribution would be $139. Whether she adjusts her contribution for the tax savings depends on whether she is responsive to the tax deduction—her elasticity of charitable giving. If the charitable deduction causes her to increase her contribution by at least the amount of tax savings to her—if the elasticity of giving is equal to or greater than one—then her tax savings is transferred to the exempt recipients.

loans, the Supreme Court noted that the books were loaned to the students, while the equipment was loaned to the schools. See Meek v. Pittenger, 421 U.S. 349, 362 (1975).

It has been argued that tax-based support is not indirect in the sense that the economic benefit flows directly from the government to the recipient organizations, without any third party intermediary who actually receives the funds. See Brown, supra note 117, at 106 n.52. This is sometimes true. For example, where the tax benefit is an exemption from tax that relieves the taxpayer from the burden of taxation. Such was the case in Walz itself, which involved a property tax exemption for church-owned property. There was no intermediary in that case, as there is in the case of the charitable contribution deduction.

An example outside the charitable-contribution context that isolates the incidence of the benefit may help clarify this idea: if a tax deduction for people who install energy-saving devices in their homes allows the producers of those devices to raise the price of the devices so that the entire tax savings claimed by the users is offset by the increase in price, then the real economic benefit of the tax provision flows to the manufacturers, rather than to the users. Congress may decide that this is the most effective method for encouraging manufacturers to produce these devices. The tax benefit is accurately described as "indirect" because the tax dollars foregone by the government are transferred to the manufacturers through the users.

If she contributes $139 and takes a deduction, she saves $39 in taxes (139 x 28% = 39), for an after-tax cost of $100.

See CHARLES T. CLOTFELTER, FEDERAL TAX POLICY AND CHARITABLE GIVING 33, 274 (1985) and Gergen, supra note 126, at 1406.

This is not a high elasticity and empirical studies suggest that the elasticity is
Only in that case does the foregone revenue benefit the organization. Because contributors may decide to keep the tax savings of their contributions for themselves, the government benefits that flow to organizations may be considered incidental to the government's decision to reduce the tax burden on contributors.

For establishment clause analysis, the indirect nature of tax support under the charitable contribution deduction may be significant because both the fact and amount of government support is contingent on choices made by the nominal taxpayers and the market's distribution of the economic benefit. Because of these two contingencies, the provision of indirect benefits implies a significantly lower level of government intent, control and entanglement than either direct spending or tax benefits that flow directly. Indirect benefits do not imply government support and approval to the same extent as benefits that emanate straight from the government.

At the same time that the indirectness of benefits argues for greater establishment clause acceptability, indirectness also raises special establishment concerns. One consequence of the indirect nature of the charitable contribution deduction is that it constitutes unconditional support for the ultimate beneficiary organizations. Tax-based support provided through the charitable contribution deduction is unrestricted in purpose and can be used directly for support of sectarian functions that the Court has never allowed the government to finance. For this reason, tax-based support is unlike the Title I support allowed in Agostini, the sign-language interpreter allowed in Zobrest, and the secular books loaned in School District No. 1. The argument made in Agostini — that the support provided by the state did not relieve a burden from the religious schools because the individual schools simply would not have provided the services at all — cannot be made in the tax context. The funds made available to religious organizations by the tax deductibility of contributions are available to support all the ordinary functions of those organizations. The fungibility of money prevents any tax-based subsidy, which is always in money, from benefiting only a narrow purpose. When the government provides funds, it frees up other funds to be used according to the recipient's discretion. Thus, all the functions of the organization are indirectly benefited by any probably greater than one in absolute value. See CLOTFELTER, supra note 291, at 274. If the elasticity of charitable giving is no greater than one, then the charitable contribution deduction is providing no incentive for taxpayers to increase their after-tax contributions, and the provision is not a very effective way to increase public support for charity. See Gergen, supra note 126, at 1412.

tax-based subsidy, and the government cannot limit its financial support to secular purposes. This aspect of tax-based funding suggests that such funding might be less acceptable under the establishment clause than in-kind, secular-purpose aid to religious institutions that the Supreme Court has approved.

In sum, this section has described how courts should approach tax-based aid to religious organizations. Even though it is not entirely clear whether tax-based aid to religious organizations is constitutionally acceptable where economically equivalent direct aid would be prohibited, it is clear that the economic equivalence of tax benefits and direct spending is not the most important factor to consider in establishment clause analysis. The establishment clause is concerned with government entanglement with religion and the government's need to achieve secular purposes without primarily promoting or inhibiting religion. Economic equivalence of tax benefits and direct spending programs is not critical to these concerns, but other distinctions between tax benefits and direct spending programs are. While reasonable people can differ about the proper constitutional outcome, in considering the constitutionality of tax provisions under the establishment clause, courts should consider the purpose of the statute and its administration, the practical manner of carrying out the program, the indirect nature of tax-based support, and the significance of taxpayer choice.

III. Beyond Constitutionality

One of the important lessons that the proponents of tax expenditure analysis have taught is that the tax law is not simply a revenue raising tool. They have emphasized this fact by looking to the incentive provisions in the Code. But the lesson is well-learned for every provision in the Code. Even if the Code were simply a revenue raising tool—if we enacted a model income tax proposed by experts—it would still contain numerous policy judgments. The basis on which we choose to raise revenue and the people from whom we choose to raise it reflects some conception of fairness and justice.

This Article has attempted to examine the constitutionality of tax benefits under the equal protection and establishment clauses, considering the doctrines developed by the Supreme Court, and, in the case of equal protection, alternative doctrinal approaches that would also be possible under the Constitution. Because of the tax

296. Economic equivalence could be significant under the effects prong of Lemon. See Meek v. Pittenger, 421 U.S. 349 (1975).

297. Such as that in BRADFORD, supra note 62 or TAX REFORM FOR FAIRNESS, SIMPLICITY AND ECONOMIC GROWTH, supra note 98.
law's increasing role in federal policy, the constitutional questions are becoming more important. At the same time, the theoretical questions underlying the constitutional issues become harder to ignore by isolating taxation from constitutional norms.

It has been suggested that both the anti-discrimination and anti-subordination approaches to equal protection reflect conflicting notions of the meaning of equality. The anti-discrimination approach reflects a formal understanding, while the anti-subordination approach reflects a substantive understanding of equality. Most of this Article is about how tax policy—in particular, tax expenditure analysis—should affect constitutional law. But these conflicting approaches to the equal protection clause, regardless of whether they are good interpretations of the equal protection clause, provide helpful insight for thinking about tax policy.

The anti-discrimination approach in equal protection analysis parallels the horizontal equity approach in traditional tax policy. They are both concerned with the government treating like-situated people alike, without inquiring into the historical, social and institutional questions that surround what it means to be alike. While formal justice in this sense may be all that the Constitution requires for equal protection, and it may be desirable for the Constitution to be limited in this way, tax policy's aspirations can be more expansive. Tax policy can be about defining and achieving substantive equality, even if it is beyond what the Constitution requires, and even though it requires explicitly linking tax policy to ideas that are outside its traditional borders. Horizontal equity, and the income measure on which it is based, sells the tax law short of the potential it has for contributing to a meaningful vision of social equality. The richness of the scholarship on the equal protection clause highlights the narrowness of the tax policy inquiry.

This Article tries to help situate tax policy more firmly in broader government policy by examining how courts should approach
a fundamentally tax-centered axiom in deciding whether tax provisions violate constitutional norms. If tax expenditure analysis is constitutionalized by courts so that tax expenditures are always treated as the equivalent of direct expenditures, at first glance, tax policy appears to be integrated with social policy because governmental action is subject to consistent review, regardless of the tax context or expenditure context of that action. However, on closer examination, the constitutionalization of tax expenditure analysis reinforces the separateness of tax policy by limiting the legal consequences of different tax provisions depending on their categorization as income-defining or not.

Even if like taxpayers are taxed alike, as the horizontal equity norm instructs, the tax system may not contribute to any larger vision of equality in society. The increasing importance of the tax law as one of the few vessels that can still be legitimately filled with federal policy places pressure on the traditionally insular perspective of tax policy, which treats tax policy as dependent only upon the internal structure and coherence of the tax law. The tax law should be a tool for achieving substantive equality because it is powerful, its effects are widespread, and its medium is money, the root of so much social inequality. As the tax law takes over the public agenda, it must better serve the fundamental ideals of government, even if they are beyond the Constitution.

301. For example, at the same time that it considered expanding education IRA's, Congress also considered cutting direct spending on education. See Katharine Q. Seelye, Panel Approves Deep Cuts in Programs Championed by Clinton, N.Y. TIMES, June 24, 1998, at A17 col. 1.

302. The Basic Income Tax casebooks generally reflect this approach, by spending considerable time on the definition of income. See, e.g., MICHAEL J. GRAETZ & DEBORAH H. SCHENK, FEDERAL INCOME TAXATION, PRINCIPLES AND POLICIES (3d ed. 1995). See also COMPREHENSIVE INCOME TAXATION (Joseph A. Pechman, ed. 1977). Tax policy was not always understood this way. See John Stuart Mill, Principles of Political Economy, Bk. V.II. (originally published in 1848) (considering taxation as part of larger political and social structure).