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## Tax Expenditures, Social Justice, and Civil Rights: Expanding the Scope of Civil Rights Laws to Apply to Tax-Exempt Charities

David A. Brennen

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Tax Expenditures, Social Justice, and Civil Rights:  
Expanding the Scope of Civil Rights Laws to Apply to  
Tax-Exempt Charities

*David A. Brennan\**

TABLE OF CONTENTS

PROLOGUE .....		169
I. INTRODUCTION .....		171
II. TAX-EXEMPT CHARITIES AND THE INADEQUACIES OF CURRENT CIVIL RIGHTS RESTRICTIONS .....		176
A. Overview of Tax-Exempt Charities .....		176
B. Current Civil Rights Restrictions Imposed on Charities .....		179
1. Traditional Civil Rights Laws: Constitutional and Statutory Limitations .....		179
2. Bob Jones University's Public Policy Limitations...		183
C. Inadequacies of Current Civil Rights Restrictions .....		185
1. Inadequacies of Traditional Civil Rights Laws .....		185
2. Inadequacies of the Public Policy Limitations.....		186
III. FEDERAL FINANCIAL ASSISTANCE UNDER FEDERAL CIVIL RIGHTS STATUTES .....		191
A. Civil Rights Statutes that Cover Recipients of FFA .....		192

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\* Associate Professor of Law, University of Richmond School of Law. B.B.A. Florida Atlantic University; J.D., L.L.M., University of Florida College of Law. I would like to thank Professors Tony Baldwin, Evelyn Brody, Mechele Dickerson, Frances Hill, Mary Heen, Ann Hodges, Beverly Moran, Rodney Smolla and Jonathan Stubbs, my research assistant Caryl Stephens Johnson, and reference librarians John Barden and Gail Zwirner for comments and research assistance on earlier versions of this article. Special thanks to the organizers of the Southeastern Association of American Law Schools Conference in August 2000 and the faculty workshop at University of Cincinnati College of Law in October 2000 during which earlier versions of this article were presented. As always, thanks to my wife, Kimberly Dianna Brennan, for her never-ending support. Research for this article was funded in part by a summer research grant awarded by University of Richmond School of Law.

1. Discrimination based on race, color, national origin .....	192
2. Gender discrimination in education .....	193
3. Discrimination based on disability.....	193
4. Discrimination based on age.....	194
B. Traditional Interpretations of the Phrase FFA.....	194
1. FFA generally .....	196
2. Tax exemptions and tax deductions as FFA .....	200
a. <i>McGlotten</i> : Tax benefits <i>may</i> be FFA .....	201
b. <i>Bachman</i> : Tax benefits are <i>never</i> FFA .....	205
c. Conclusions.....	207
IV. TAX EXPENDITURE THEORY: <i>ECONOMIC</i> EQUIVALENCE	
VS. <i>CONSTITUTIONAL</i> EQUIVALENCE.....	208
A. Equivalence as an Essential Element of Tax Expenditure Theory .....	208
B. The Supreme Court's Uniform Acceptance of Economic Equivalence in Constitutional Decision Making.....	212
1. <i>Walz v. Tax Commission</i> .....	213
2. <i>Committee for Public Education and Religious Liberty v. Nyquist</i> .....	216
3. <i>Mueller v. Allen</i> .....	219
4. <i>Texas Monthly, Inc. v. Bullock</i> .....	221
C. Limitations of the Equivalence Concept Espoused by Tax Expenditure Theory.....	224
V. DISTINGUISHING TAX BENEFITS FOR CHARITIES FROM TAX BENEFITS FOR NON-CHARITIES AND INDIVIDUALS...	225
VI. CONCLUSION.....	226

## PROLOGUE

In recent years, courts have decided a number of cases in which private organizations discriminated against people based solely on their race, gender, sexual orientation, or other immutable traits. For example, in 2000, the Boy Scouts of America revoked a New Jersey man's membership in the Boy Scouts because he was gay.<sup>1</sup> New Jersey's supreme court held that the Boy Scouts' action violated New Jersey's anti-discrimination law.<sup>2</sup> Notwithstanding the state court's holding, the United States Supreme Court concluded that the First Amendment prevented any court from forcing the Boy Scouts to keep a gay man as a member of its private group.

A great number of discriminating private organizations, like the Boy Scouts, are tax-exempt charities that receive significant government and public financial support as a result of their eligibility for various tax benefits. What if the Boy Scouts, like many private white supremacist groups, decided that black people are not entitled to membership? What about handicapped people? The elderly? Women? The issue is, should we permit our tax system to fund groups that engage in invidious discrimination based on race, gender, disability, age, or sexual orientation? Many would agree that private groups (whether tax-supported or not) should have the freedom to decide on the membership of their organizations by use of certain preferences, such as those allowed under lawful affirmative action plans. However, most would also undoubtedly agree that we should not allow tax monies to fund private groups that discriminate in such harmful ways against minority groups. Unfortunately, as currently interpreted, federal laws that define eligibility for the type of tax benefits received by charities like the Boy Scouts do not clearly, explicitly, and effectively prohibit harmful discriminatory behavior by these groups.<sup>3</sup> Indeed, despite calls for an end to tax benefits for the

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1. *See, e.g.*, *Boy Scouts of Am. v. Dale*, 530 U.S. 640 (2000) (invalidating, on First Amendment grounds, application of state anti-discrimination law against Boy Scouts' exclusion of scout leader solely because scout leader was admitted homosexual).

2. *Dale v. Boy Scouts of Am.*, 734 A.2d 1196, 1230 (N.J. 1999) (holding that BSA, as a "place of public accommodation" under New Jersey law, N.J.S.A. 10:5-4, cannot deny persons "accommodations, advantages, facilities, and privileges . . . because of . . . sexual orientation").

3. *See generally* David A. Brennan, *The Power of The Treasury: Racial Discrimination, Public Policy and "Charity" in Contemporary Society*, 33 U.C. DAVIS L. REV. 389 (2000), for background discussion of this issue.

Boys Scouts in the wake of the recent Supreme Court ruling,<sup>4</sup> the Boy Scouts still receive tax benefits and still exclude gays from membership.<sup>5</sup>

To combat harmful discrimination by private tax-supported groups, society should, at a minimum, maximize use of all currently existing legal tools. One such tool used by the federal government against private groups (whether tax-supported or not) is the conditioning, under civil rights laws, of the receipt of federal financial assistance (FFA) on the recipient's agreement not to discriminate. However, these civil rights laws have not been interpreted broadly enough to apply to private, tax-supported organizations based solely on their receipt of tax benefits. Instead, one must show that the organization, in addition to its tax support, receives other types of federal financial support (such as government grants or loans) that may constitute FFA.<sup>6</sup>

The scope of coverage of these statutory civil rights laws could be significantly increased by adopting an express policy that prohibits particular tax-supported groups, like tax-exempt charities, from engaging in wrongful discrimination. If Congress were ever to consider the matter again, it could adopt such a policy by enacting appropriate federal legislation. But even without new legislation, there is sound basis to interpret existing federal tax and civil rights laws as supporting the proposition that charities, solely by virtue of their

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4. See, e.g., *Commentary*, ASBURY PARK PRESS (Neptune, N.J.), July 18, 2000, at A17 ("If they want to openly discriminate, whether it's to bar gays, left-handers or brown-eyed people, then they need to become totally private. No free use of public facilities, no tax breaks, no assistance that involves public money, no free advertising and no public subsidization whatsoever.").

5. This statement is not intended as a political statement about the social acceptability and advisability of laws favoring or disfavoring homosexuality. Others have quite adequately addressed that matter. See, e.g., Patricia A. Cain, *Heterosexual Privilege and the Internal Revenue Code*, 34 U.S.F. L. Rev. 465 (2000) (noting many ways in which the Internal Revenue Code disadvantages homosexuality as compared to heterosexuality). Instead, this statement is merely intended to highlight that an organization whose activities violate a principle contained in state law—that discrimination against homosexuals by places of public accommodation is wrong—is entitled to engage in invidious discrimination while receiving public tax benefits.

6. Though many state statutes like those in New Jersey prohibit discrimination based on one's sexual orientation, federal civil rights statutes (as currently written and interpreted) do not prohibit such discrimination. See RODNEY A. SMOLLA, *FEDERAL CIVIL RIGHTS ACT* § 10.06 (3d ed. 2000). See also *Ulane v. Eastern Airlines, Inc.*, 742 F.2d 1081, 1084 (7th Cir. 1984) ("[H]omosexuals and transvestites do not enjoy Title VII protection."); *DeSantis v. Pacific Tel. & Tel. Co.*, 608 F.2d 327, 329–30 (9th Cir. 1979) ("[W]e conclude that Title VII's prohibition of 'sex' discrimination applies only to discrimination on the basis of gender and should not be judicially extended to include sexual preference such as homosexuality." (citations omitted)).

preferred tax status, receive FFA and are thus prohibited from engaging in invidious discrimination. This article explains why such an interpretation is appropriate as public policy, consistent with the underlying purposes of existing civil rights legislation, and sound tax policy.

## I. INTRODUCTION

Many civil rights statutes prohibit discrimination based on race, gender, disability, and age in programs or activities that receive FFA.<sup>7</sup> These laws direct government agencies that award FFA to ensure compliance with the “nondiscrimination” requirement<sup>8</sup> and promulgate rules that interpret the phrase FFA.<sup>9</sup> Courts also interpret the phrase FFA for these civil rights statutory purposes.<sup>10</sup> The basic consensus of agencies and courts is that FFA refers to funds received directly or indirectly from the federal government.<sup>11</sup> Thus, private entities receiving federal grants or loans are subject to coverage by these

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7. *See, e.g.*, Title VI of the Civil Rights Act of 1964, 42 U.S.C. § 2000d (2000) (“No person in the United States shall, on the ground of race, color, or national origin, be excluded from participation in, be denied the benefits of, or be subjected to discrimination under any program or activity receiving Federal financial assistance . . . .”); Title IX of the Education Amendments of 1972, 20 U.S.C. § 1681(a) (2000) (“No person in the United States shall, on the basis of sex, be excluded from participation in, be denied the benefits of, or be subjected to discrimination under any education program or activity receiving Federal financial assistance . . . .”); Rehabilitation Act of 1973, 29 U.S.C. § 794(a) (2000) (“No otherwise qualified individual with a disability in the United States, as defined in [29 U.S.C. § 706(20)], shall, solely by reason of her or his disability, be excluded from the participation in, be denied the benefits of, or be subjected to discrimination under any program or activity receiving Federal financial assistance . . . .”).

8. *See, e.g.*, Title IX, 20 U.S.C. § 1682. Title IX provides:

Each Federal department and agency which is empowered to extend Federal financial assistance to any education program or activity, by way of grant, loan, or contract other than a contract of insurance or guaranty, is authorized and directed to effectuate the provisions of [§ 1681 of Title IX] with respect to such program or activity by issuing rules, regulations, or orders of general applicability which shall be consistent with achievement of the objectives of the statute authorizing the financial assistance in connection with which the action is taken.

*Id.*

9. *See id.*

10. *See* *Grove City College v. Bell*, 465 U.S. 555 (1984) (concluding that college with students receiving federal grants was a recipient of FFA). *But see* *NCAA v. Smith*, 525 U.S. 459 (1999) (concluding that dues received from member institutions did not constitute federal financial assistance even though the member institutions were recipients of federal financial assistance); *cf.* *Richard Foss v. Chicago*, 817 F.2d 34 (7th Cir. 1987) (holding that the Fire Department of the City of Chicago was not a recipient of federal financial assistance because the City of Chicago received federal funding).

11. *See Grove City College*, 465 U.S. at 563.

civil rights laws as direct recipients of FFA.<sup>12</sup> Further, private entities that receive fees from direct recipients of FFA are subject to coverage as indirect recipients.<sup>13</sup> Yet, what about recipients of tax benefits in the form of exemptions, credits, or deductions? Should tax-exempt charities that receive no other direct or indirect federal financial benefits be covered by civil rights laws because of their tax-favored status as recipients of FFA? Social justice advocates would likely say, “Yes.”<sup>14</sup>

Two federal district courts have addressed the meaning of FFA in the context of tax exemptions or deductions.<sup>15</sup> However, these courts reached different conclusions. In *McGlotten v. Connally*, a federal district court concluded that certain federal tax benefits are FFA for purposes of Title VI of the Civil Rights Act of 1964.<sup>16</sup> Later, in *Bachman v. American Society of Clinical Pathologists*, a different federal district court reached the opposite conclusion—that tax-exemption alone is not FFA as required by section 504 of the Rehabilitation Act of 1973.<sup>17</sup>

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12. *See id.*

13. *See, e.g., id.*

14. The term “social justice” has been defined in many ways. For example, one scholar defines it as

that branch of the virtue of justice that moves us to use our best efforts to bring about a more just ordering of society—one in which people’s needs are more fully met. It solves the problem of assignability because it is something due from everyone whose efforts can make a difference to everyone whose needs are not met as things stand. I do not owe the man on the grate a place to live, but I do owe him whatever I can do to provide a social order in which housing is available to him. I do not owe any poor person a share of my wealth, but I owe every poor person my best effort to reform the social institutions by which I am enriched and he or she is impoverished.

Robert E. Rodes, Jr., *Social Justice and Liberation*, 71 NOTRE DAME L. REV. 619, 620–21 (1996). Drawing on this definition, the term “social justice,” as used in this article, is intended to refer to the concept of justice that recognizes a societal obligation (not just an individual one) to provide appropriate remedies for harm to others caused by legal, moral, or cultural structures instituted by society. Thus, for example, it is socially just for society to engage in race-based affirmative action and other efforts aimed at correcting the long term effect of invidious societal discrimination against blacks. *See also* discussion *infra* note 58 and accompanying text.

15. *See* *McGlotten v. Connally*, 338 F. Supp. 448 (D.D.C. 1972); *Bachman v. American Soc’y of Clinical Pathologists*, 577 F. Supp. 1257 (D.N.J. 1983).

16. *See* *McGlotten*, 338 F. Supp. at 462; *see also* discussion *infra* notes 157–91 and accompanying text.

17. *See* *Bachman*, 577 F. Supp. at 1265; *see also* discussion *infra* notes 192–204 and accompanying text.

The United States Supreme Court has yet to decide if tax benefits are FFA under federal civil rights statutes.<sup>18</sup> However, the Supreme Court has addressed the related issue of whether the government's grant of certain tax benefits should be analyzed as government expenditures or as government neutrality for constitutional law purposes.<sup>19</sup> The problem is that the Court uses expenditure analysis<sup>20</sup> in some contexts and neutrality analysis<sup>21</sup> in others, thus failing to provide clear guidance on how tax benefits should be analyzed under federal civil rights statutes.<sup>22</sup>

18. While the Court has not provided specific guidance on whether tax benefits are FFA for civil rights statutory purposes, it has provided general guidance on the meaning of this jurisdictional term. *See* *Grove City College v. Bell*, 465 U.S. 555, 563 (1984); *see also* discussion *infra* notes 130–56 and accompanying text.

19. *See, e.g.*, *Walz v. Tax Comm'n*, 397 U.S. 664 (1970) (discussing equivalence of state real property tax exemptions). *See also*, *Texas Monthly, Inc. v. Bullock*, 489 U.S. 1 (1989) (discussing equivalence of state sales tax exemptions); *Mueller v. Allen*, 463 U.S. 388 (1983) (discussing equivalence of state income tax deductions); *Committee for Pub. Educ. & Religious Liberty v. Nyquist*, 413 U.S. 756 (1973) (discussing equivalence of “special” income tax reductions); discussion *infra* notes 225–81 and accompanying text.

20. Expenditure analysis refers to the Court's treatment of a tax benefit as the same, in all relevant respects, as a direct government outlay of money. Tax expenditures are revenue losses attributable to provisions of tax laws that allow, for example, exclusion, exemption, or deduction from gross income or that provide credits, preferential tax rates, or deferral of tax liability. *See* Congressional Budget and Impoundment Control Act of 1974, 2 U.S.C. § 622(3) (2000); JOINT COMM. ON TAXATION, ESTIMATES OF FEDERAL TAX EXPENDITURES FOR FISCAL YEARS 2000–2004, at 2 (Comm. Print 1999). Under tax expenditure theory, tax benefits and direct government expenditures are considered equivalent only if the tax benefit was enacted to implement social policy, as opposed to further delineating the appropriate tax base. *See* discussion *infra* note 214 and accompanying text.

21. Neutrality analysis refers to the Court's treatment of a tax benefit as something other than a direct outlay of money by the government. The principle of neutrality emanates from the Court's First Amendment cases and provides that the government must remain neutral towards religion, neither endorsing nor inhibiting religious activities. In *Walz v. Tax Commission*, the Court provides a good explanation of neutrality.

The course of constitutional neutrality . . . cannot be an absolutely straight line; rigidity could well defeat the basic purpose of [the First Amendment], which is to insure that no religion be sponsored or favored, none commanded, and none inhibited. The general principle deducible from the First Amendment and all that has been said by the Court is this: that we will not tolerate either governmentally established religion or governmental interference with religion. Short of those expressly proscribed governmental acts there is room for play in the joints productive of a benevolent neutrality which will permit religious exercise to exist without sponsorship and without interference.

*Walz*, 397 U.S. at 669.

22. *See* Linda Sugin, *Tax Expenditure Analysis and Constitutional Decisions*, 50 HASTINGS L.J. 407, 411 n.20 (1999) (“The Supreme Court has been reticent to adopt tax expenditure analysis as a basis for constitutional decision-making, despite repeated invitations. The Court has shown that it clearly understands the economic equivalence of tax subsidies and

Using tax-expenditure theory as a guide, this article argues that tax-exempt charities, because of their favored tax status, receive FFA and should comply with civil rights laws that cover recipients of government financial assistance. This article uses tax policy to extend social policy beyond current civil rights norms.<sup>23</sup> Admittedly, many tax-exempt charities are covered by these civil rights laws without regard to their tax-exempt charitable status because they are state actors or receive traditional forms of FFA,<sup>24</sup> either directly (e.g., government grants) or indirectly (e.g., accepting students with government guaranteed student loans).<sup>25</sup> However, other tax-exempt charities receive no financial aid from the federal government except for tax benefits stemming from their tax-exempt charitable status.<sup>26</sup> Thus, unless courts and agencies view this tax-favored status as a form of FFA, civil rights laws that apply to recipients of FFA do not apply to these other charities.<sup>27</sup>

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direct subsidies.”); Edward A. Zelinsky, *Are Tax “Benefits” Constitutionally Equivalent to Direct Expenditures?*, 112 HARV. L. REV. 379, 380–81 (1998) (“The Court itself has equivocated, equating tax benefits and direct spending in some constitutional cases but not in others without indicating a rationale for such a seemingly inconsistent approach.”). *See also* Texas Monthly, Inc. v. Bullock, 489 U.S. 1, 43 (1989) (Scalia, J., dissenting) (“[I]n other contexts we have suggested that tax exemptions and subsidies are equivalent. We have not treated them as equivalent, however, in the Establishment Clause context.” (citations omitted)).

23. *See* Sugin, *supra* note 22, at 472–74 (indicating that tax policy should reflect “some conception of fairness and justice,” and, consequently, tax law should be a tool for achieving such ends “because it is powerful, its effects are widespread, and its medium is money, the root of so much social inequality”); Laura Sager & Stephen Cohen, *How the Income Tax Undermines Civil Rights Law*, 73 S. CAL. L. REV. 1075, 1080 (2000) (contending that tax law should “permit civil rights plaintiffs either to deduct fully or to exclude from income the portion of a recovery expended for attorney’s fees” so as to “preserve the purposes of . . . federal civil rights law”).

24. *See* discussion *infra* notes 49–64 and accompanying text.

25. For example, under the Elementary and Secondary Education Act of 1965, 20 U.S.C. § 7701 (2000), many private grade schools that have tax-exempt status receive government grants for various educational initiatives. Also, many tax-exempt private colleges and universities accept students that receive government grants or loans. *See, e.g.*, United States v. Virginia, 518 U.S. 515, 564 (1996) (“The private women’s colleges [in Virginia] are treated . . . exactly as all other private schools are treated, which includes the provision of tuition-assistance grants to Virginia residents.”). In a recent decision, the United States Supreme Court held that parochial schools that received indirect or direct government assistance under the statute did not violate the Establishment Clause. *Mitchell v. Helms*, 530 U.S. 793 (2000).

26. Thus, a scholarship fund organized as a tax-exempt charitable organization may receive the entirety of its direct funding from private donors and may receive no traditional forms of indirect funding.

27. *See, e.g.*, *Bachman v. American Soc’y of Clinical Pathologists*, 577 F. Supp. 1257, 1264 (D.N.J. 1983) (concluding that tax-exemption alone is not FFA for purposes of Rehabilitation Act of 1973).

Current law ostensibly imposes civil rights restrictions on tax-exempt charities by prohibiting charities from violating “established public policy.”<sup>28</sup> However, it is unclear when or whether violation of civil rights laws is equivalent to violation of “established public policy”<sup>29</sup> or, conversely, whether compliance with civil rights laws is equivalent to compliance with such policy.<sup>30</sup> Therefore, to expand civil rights protections and clarify when a charity violates generally accepted civil rights standards, the need exists to expressly extend coverage of these civil rights laws to tax-exempt charities. This article articulates one method of accomplishing this social justice goal<sup>31</sup> of maximizing human liberty through law.<sup>32</sup>

Part II of this article describes tax-exempt charities and demonstrates how civil rights laws, as currently interpreted, are inadequate to restrict the actions and policies of private tax-exempt charities that do not receive traditional forms of FFA. Part III provides a brief outline of civil rights laws in this country and discusses selected provi-

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28. See *Bob Jones Univ. v. United States*, 461 U.S. 574, 591 (1983) (“A corollary to the public benefit principle is the requirement, long recognized in the law of trusts, that the purpose of a charitable trust may not be illegal or violate *established public policy*.” (emphasis added)); see also discussion *infra* notes 65–73 and accompanying text.

29. See discussion *infra* notes 81–100 and accompanying text.

30. See generally Brennen, *supra* note 3.

31. See *supra* note 14 for a definition of the term “social justice.”

32. Professor Linda Sugin also posits an approach that would increase civil rights restrictions imposed on charities. Under Professor Sugin’s approach, the Equal Protection Clause could be applied against the government for allowing tax deductions to charities that discriminate based on race. See Sugin, *supra* note 22, at 457–59 (indicating that “anti-subordination” and “pure protection” models for interpreting the Equal Protection Clause would eliminate intent requirement of current law, permitting tax expenditures to be treated as equivalent to direct expenditures for all relevant purposes). This article, however, does not attempt to alter Equal Protection or other constitutional interpretive methodology to the extent that the methodology requires proof of discriminatory intent. Eliminating the “intent” requirement of constitutional analysis is unnecessary for civil rights statutory applicability purposes because intent is not generally a required element of proof for these statutory purposes—at least where relief requested is injunctive or declaratory in nature and not compensatory. See discussion *infra* note 56 and accompanying text.

This article will also not address the practical problem of who, other than authorized government agencies, would have standing to challenge the tax-exempt charitable status of an entity relying, in part, on a claim that tax benefits are FFA. See Francis R. Hill & Barbara L. Kirschten, *Operational Issues: Public Policy Requirement*, in *FEDERAL AND STATE TAXATION OF EXEMPT ORGANIZATIONS* ¶ 2.03[6][d] (1998) (“One reason that there is so little guidance on the scope of the public policy requirement is that the current judicial interpretation of the standing requirement limits the number of cases that will be decided on their merits.”). See also *Allen v. Wright*, 468 U.S. 737 (1984) (denying standing to parents of black schoolchildren who complained that the service was not adequately implementing the public policy requirement).

sions of those laws that cover recipients of FFA. Part III also describes the traditional interpretations of the phrase FFA as used in the civil rights statutory context by courts and agencies. Part IV outlines the basics of tax expenditure theory by tracing the history of the issue of equivalence of tax benefits and direct expenditures in the Supreme Court, using as examples the Court's religion clause cases.<sup>33</sup> In addition, Part IV reviews recent academic discussion about equivalency to show that tax benefits and direct government expenditures, while not always constitutionally equivalent, are nonetheless economically equivalent.<sup>34</sup> Finally, Part V explains why the analysis in this article is limited only to certain organizations that receive tax benefits—namely, tax-exempt charities. Relying on the equivalence concept of tax expenditure theory, this article concludes that courts and federal agencies should adopt the view that tax-exempt charities are recipients of FFA under Title VI, Title IX, and any other federal civil rights statute for which receipt of FFA triggers coverage.

## II. TAX-EXEMPT CHARITIES AND THE INADEQUACIES OF CURRENT CIVIL RIGHTS RESTRICTIONS

This Part provides an overview of the relevant laws affecting tax-exempt charities and explains how current law fails to adequately ensure that charities do not violate individual civil rights.

### A. Overview of Tax-Exempt Charities

A tax-exempt charity is a trust, corporation, or unincorporated association that is both exempt from the requirement to pay federal income tax<sup>35</sup> and permitted to receive tax-deductible contributions

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33. See *Walz v. Tax Comm'n*, 397 U.S. 664 (1970); *Committee for Pub. Educ. & Religious Liberty v. Nyquist*, 413 U.S. 756 (1973); *Mueller v. Allen*, 463 U.S. 388 (1983); *Texas Monthly, Inc. v. Bullock*, 489 U.S. 1 (1989).

34. See generally *Zelinsky*, *supra* note 22; *Sugin*, *supra* note 22.

35. See, e.g., I.R.C. § 1 (2000) (imposing tax on taxable income of individuals, trusts, and estates); see *id.* § 11 (imposing tax on taxable income of corporations). Section 501(a) of the Internal Revenue Code provides that certain described organizations are exempt from the requirement to pay the income tax: "(a) Exemption from taxation—An organization described in subsection (c) or (d) or section 401(a) shall be exempt from taxation under this subtitle unless such exemption is denied under section 502 or 503." *Id.* § 501(a). Among these exempt organizations are "charities," which are described in section 501(c)(3) as entities or funds that are

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 (but only if no part of its activities involve the provision of athletic facilities or equipment), or for the prevention of cruelty to children or

from the public.<sup>36</sup> Tax-exempt charities have existed in this country for as long as the United States has had an income tax.<sup>37</sup> To obtain tax-exempt charitable status today, an entity must be organized and operated for charitable purposes and must avoid certain proscribed acts.<sup>38</sup>

In § 501(c)(3) of the Internal Revenue Code (the “Code”), Congress identifies several tax-exempt charitable purposes, including: testing for public safety, fostering amateur sports competition, preventing cruelty to children or animals, and advancing religion, science, literature, or education.<sup>39</sup> Entities serving other general public benefit purposes may also qualify for tax-exempt charitable status even if the entity does not serve one of those purposes specifically identified in § 501(c)(3).<sup>40</sup> The Department of the Treasury (“Treas-

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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.

*Id.* § 501(c)(3).

36. The tax deductions for contributions are allowed pursuant to § 170 of the Internal Revenue Code, which provides that “there shall be allowed as a deduction any charitable contribution . . . payment of which is made within the taxable year.” *Id.* § 70(a)(1). The few exceptions where entities other than § 501(c)(3) charities are entitled to income tax exemption as well as the right to receive tax deductible contributions from the public are certain veterans organizations (§ 170(c)(3)), fraternal organizations (§ 170(c)(4)), and cemetery associations (§ 170(c)(5)). The one exception of when a charity is not entitled to receive tax deductible contributions from the public is organizations that “test[] for public safety.” These public safety testing organizations are not described in the deductibility provisions. *See generally id.* § 170; BRUCE R. HOPKINS, *THE LAW OF TAX-EXEMPT ORGANIZATIONS* 233 (7th ed. 1998) (describing tax status of public testing organizations).

37. *See, e.g.*, Revenue Act of 1913, ch. 16, 38 Stat. 114, 172 (exempting from tax “any corporation or association organized and operated exclusively for religious, charitable, scientific, or educational purposes, no part of the net income of which inures to the benefit of any private stockholder or individual”).

38. *See* I.R.C. § 501(c)(3) (2000). The prohibited acts include “substantial lobbying,” political campaign activities, private benefit, and inurement transactions. *See id.* One scholar recently noted that the private inurement prohibition “embodies the primary distinction between taxable and tax-exempt entities” and “is of such significance that it underlies all but one of the emerging theoretical justifications for tax-exemption.” *See* Darryll K. Jones, *The Scintilla of Individual Profit: In Search of Private Inurement and Excess Benefit*, 19 VA. TAX REV. 575, 576–77, 579 (2000).

39. *See id.*

40. *See* Treas. Reg. § 1.501(c)(3)–1(d)(2) (2000). This regulation specifically provides the following:

(2) Charitable defined. The term *charitable* is used in section 501(c)(3) in its generally accepted legal sense and is, therefore, not to be construed as limited by the separate enumeration in section 501(c)(3) of other tax-exempt purposes which may fall

(“Treasury”), as the federal agency authorized to enforce § 501(c)(3),<sup>41</sup> has indicated that these other general public benefit purposes might include protection of the environment,<sup>42</sup> operation of a public interest law firm,<sup>43</sup> or engaging in certain community development activities.<sup>44</sup> These general public benefit purposes are related to each other in that each stems from contemporary and historical understandings of the term “charitable.”<sup>45</sup> In *Bob Jones University v. United States*, the Supreme Court further expanded the requirements for tax-exempt charitable status by holding that a charitable entity may not violate “established public policy.”<sup>46</sup> This public policy limitation, however, is not specifically set out in the Code.<sup>47</sup> Thus, the Treasury, subject to possible judicial review, must make the initial determination about whether a particular entity’s actions or policies violate “established public policy.”<sup>48</sup>

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within the broad outlines of *charity* as developed by judicial decisions.

*Id.*

41. Section 7805(a) of the Internal Revenue Code provides:

Except where such authority is expressly given by this title to any person other than an officer or employee of the Treasury Department, the Secretary shall prescribe all needful rules and regulations for the enforcement of this title, including all rules and regulations as may be necessary by reason of any alteration of law in relation to internal revenue.

I.R.C. § 7805(a) (2000).

42. See Rev. Rul. 76-204, 1976-1 C.B. 152.

43. See Rev. Rul. 75-74, 1975-1 C.B. 152.

44. See Rev. Rul. 74-587, 1974-2 C.B. 162.

45. See Rob Atkinson, *Altruism in Nonprofit Organizations*, 31 B.C. L. REV. 501, 599-601 (1990) (discussing role of federal income tax on not-for-profit organizations); Henry B. Hansmann, *The Role of Nonprofit Enterprises*, 89 YALE L.J. 835, 883-84 (1980) (discussing applicability of charitable deductions).

46. See *Bob Jones Univ. v. United States*, 461 U.S. 574, 591 (1983) (“A corollary to the public benefit principle is the requirement, long recognized in the law of trusts, that the purpose of a charitable trust may not be illegal or violate *established public policy*.”) (emphasis added)). See also Brennen, *supra* note 3, for a general discussion of the problems and dangers of the Treasury’s public policy power.

47. See Lars G. Gustafsson, *The Definition of “Charitable” for Federal Income Tax Purposes: Defrocking the Old and Suggesting Some New Fundamental Assumptions*, 33 HOUS. L. REV. 587, 590 (1996).

48. See *Bob Jones Univ.*, 461 U.S. at 596-97 (“In the first instance, however, the responsibility for construing the Code falls to the IRS.”); *Commissioner v. Portland Cement Co.*, 450 U.S. 156, 169 (1981); *United States v. Correll*, 389 U.S. 299, 306-07 (1967) (stating that the Court must defer to administration’s implementing congressional mandate); *Boske v. Comingore*, 177 U.S. 459, 469-70 (1900) (holding that the Treasury Secretary’s judgment should be upheld unless clearly inconsistent with law); I.R.C. § 7805(a) (stating that Treasury Secretary may prescribe rules for enforcement). Despite the 1983 judicial mandate in *Bob Jones University* that comporting with public policy is a prerequisite to obtaining charitable status, the IRS “has yet to clearly set forth a consistent definition and scope of what constitutes a fun-

*B. Current Civil Rights Restrictions Imposed on Charities*

The current civil rights restrictions imposed on private charities consist of (1) traditional civil rights laws—at least to the extent the charity triggers coverage under these laws—and (2) the public policy limitation, as outlined by the Supreme Court in *Bob Jones University v. United States*.

*1. Traditional civil rights laws: Constitutional and statutory limitations*

Traditional federal civil rights protections are contained in a framework of laws consisting of the Constitution, statutes, regulations, executive actions, and court interpretation.<sup>49</sup> These protections attempt to cover all those situations in which one expects governmental assurance of fundamental fairness. However, none of these governmental protections applies across the board to all persons who might claim entitlement to them. For example, federal constitutional civil rights protections do not apply unless the civil rights violator is a state actor.<sup>50</sup> Since charities are not necessarily state actors, they are not typically subject to the restrictions imposed by the Constitution.<sup>51</sup> Thus, private charities that commit civil rights violations are

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damental public policy.” John W. Lee et al., *Capitalizing And Depreciating Cyclical Aircraft Maintenance Costs: More Trouble Than It’s Worth?*, 17 VA. TAX. REV. 161, 230–31 (1997). The failure to define what a fundamental public policy is has the effect of enabling the Treasury to retain significant discretion to determine what is and what is not qualified to receive tax-exempt charitable status solely due to a public policy violation.

49. See, e.g., U.S. CONST. amend. XIV; Equal Educational Opportunities Act of 1974, 20 U.S.C. § 1701 (2000); Equal Pay Act of 1963, commonly known as the Fair Labor Standards Act, 29 U.S.C. § 206 (2000); Nondiscrimination in Federally Assisted Programs of the Department of Agriculture—Effectuation of Title VI of the Civil Rights Act of 1964, 7 C.F.R. § 15.1 (2000); Housing and Urban Development, Compliance Procedures for Affirmative Fair Housing Marketing, 24 C.F.R. § 108.25 (2000); Exec. Order No. 13166, 65 Fed. Reg. 50121 (Aug. 11, 2000) (Improving Access to Services for Persons with Limited English Proficiency); Exec. Order No. 13160, 65 Fed. Reg. 39775 (June 23, 2000) (Nondiscrimination on the Basis of Race, Sex, Color, National Origin, Disability, Religion, Age, Sexual Orientation, and Status as a Parent in Federally Conducted Education and Training Programs).

50. See, e.g., *The Civil Rights Cases*, 109 U.S. 3, 11 (1883) (“It is state action of a particular character that is prohibited. Individual invasion of individual rights is not the subject-matter of the [Fourteenth] amendment.”); *Lugar v. Edmondson Oil Co., Inc.*, 457 U.S. 922, 937 (1982) (“Our cases have accordingly insisted that the conduct allegedly causing that deprivation of a [constitutional] federal right be fairly attributable to the State”). See also SMOLLA, *supra* note 6, at § 1.02[3][b] (“The state action requirement remains a bedrock principle of American constitutional law.”); Sugin, *supra* note 22, at 430 (“One might argue that tax benefits do not involve sufficient state action to trigger constitutional scrutiny.”).

51. State actors are not foreclosed from organizing as tax-exempt charities, in the sense

generally not subject to punishment or penalty for those violations unless the charity is covered by any number of federal statutes that impose civil rights restrictions on private, nonstate actors.<sup>52</sup>

The fact that private actors are covered by civil rights statutes and not directly covered by constitutional provisions that protect civil rights does not mean that the restrictions imposed on private actors are somehow less onerous than those imposed by the Constitution. In fact, civil rights statutes often impose greater restrictions on private actors than the Constitution would impose if the actor were a state actor. For example, certain civil rights statutes extend constitutional-like protections to “forms of discrimination not covered in any meaningful way by the Constitution,”<sup>53</sup> such as discrimination based on age or disability.<sup>54</sup> Also, civil rights statutes often broaden the “substantive principles governing discrimination,”<sup>55</sup> by allowing claims to be based upon disparate impact, rather than proof of dis-

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that their income is statutorily exempt from the income tax and they are permitted to receive tax-deductible contributions from the public. Additionally, where private parties, including charities, exercise governmental power by executing a traditional public function, the Supreme Court might find that the private actor is indeed a state actor. *See, e.g.*, *Terry v. Adams*, 345 U.S. 461, *reh'g denied*, 345 U.S. 1003 (1953) (holding that a private party that managed elections for public office was state actor); *Marsh v. Alabama*, 326 U.S. 501 (1946) (holding that a private company that operated a “company town” was state actor). Thus, it is possible that a particular tax-exempt charity (1) is not a private entity, but rather, a state actor or (2) is both a private party and a state actor. This article’s focus, however, is on tax-exempt charities as private actors.

52. Among these federal statutory restrictions are 42 U.S.C. § 1983 (imposing constitutional limitations on private actors acting “under color of state law”) and Title VI of the Civil Rights Act of 1964, 42 U.S.C. § 2000d (prohibiting discrimination based on race or sex in “any program or activity receiving ‘FFA’”). Though state statutes may also impose civil rights restrictions on charities, many such statutes are often limited by federal constitutional law. *See, e.g.*, *Boy Scouts of Am. v. Dale*, 530 U.S. 640 (2000) (invalidating, on First Amendment grounds, application of state anti-discrimination law against Boy Scouts’ exclusion of scout leader solely because scout leader was admitted homosexual). Further, private employment agreements, such as those between a union and its employers or between individual employees and their employers, may waive the right to a judicial forum and provide for arbitration of statutory civil rights claims. *See* Ann C. Hodges, *Arbitration of Statutory Claims in the Unionized Workplace: Is Bargaining with the Union Required?*, 16:3 OHIO ST. J. ON DISP. RESOL. (forthcoming) (discussing whether unions are authorized by federal law to waive employee rights to litigate statutory civil rights claims in court). In some cases, a statutory claim may never be heard if it is confined to the collectively bargained arbitration procedure because the union effectively controls the arbitration process and has limited resources to arbitrate. *See id.*

53. *See* SMOLLA, *supra* note 6, at § 1.01[2].

54. *See, e.g.*, The Education of the Handicapped Act, 20 U.S.C. §§ 1401–20; The American With Disabilities Act of 1990, 42 U.S.C. §§ 12101–213; The Age Discrimination in Employment Act, 29 U.S.C. § 621.

55. *See* SMOLLA, *supra* note 6, at § 1.01[2].

criminary intent.<sup>56</sup> Thus, civil rights statutes arguably provide greater protections against civil rights violations than the Constitution.<sup>57</sup>

In addition to civil rights statutes often providing greater civil rights protections than the Constitution, these statutes permit private actors to be more proactive in advancing social justice objectives through methods like affirmative action.<sup>58</sup> For example, private em-

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56. *See, e.g.*, Title VI of the Civil Rights Act of 1964, 42 U.S.C. § 2000d (providing remedies for discrimination based on race on showing of discriminatory impact); *Guardians Ass'n v. Civil Serv. Comm'n*, 463 U.S. 582, 584 (1983) (indicating that five Justices of the Supreme Court interpret Title VI as not requiring proof of discriminatory intent, as is the case with Equal Protection Clause); Title VII of the Civil Rights Act of 1964, 42 U.S.C. § 2000e (providing remedies for employment discrimination on a showing of disparate impact); *Griggs v. Duke Power Co.*, 401 U.S. 424, 431 (1971) (concluding that Title VII outlaws employment “practices that are fair in form, but discriminatory in operation”). *Compare* *McCleskey v. Kemp*, 481 U.S. 279 (1987) (requiring proof of “discriminatory intent” for showing of Equal Protection violation by governmental actor) *with* *Washington v. Davis*, 426 U.S. 229, 238–48 (1976) (Equal Protection Clause prohibits only intentional discrimination). The requirement of proof of discriminatory impact only, and not discriminatory intent, for civil rights statutory purposes is limited to situations in which the requested relief is declaratory or injunctive in nature, not compensatory. *See* SMOLLA, *supra* note 6, at § 8.02[3]; *Guardians Ass'n*, 463 U.S. at 584, 597–606 (White, J.) (concluding that “unless discriminatory intent is shown, declaratory and limited injunctive relief should be the only available private remedies for Title VI violations”).

57. Indeed, some justices of the Supreme Court take the view that Title VI “has independent force, with language and emphasis in addition to that found in the Constitution.” *See* *Regents of the Univ. of Cal. v. Bakke*, 438 U.S. 265, 416 (1978) (Stevens, J., concurring, joined by Burger, C.J., Stewart, J., and Rehnquist, J.).

58. *See, e.g.*, Honourable Mr. Justice Michel Bastarache, *Does Affirmative Action Have a Future as an Instrument of Social Justice?*, 29 OTTAWA L. REV. 497 (1977). Regarding affirmative action as a type of social justice, Justice Bastarache states:

[T]he “individual justice” approach to equality law. . . centres on the relationship between the state and the individual, and in particular, on the view that the state’s role in eliminating disadvantage is two-fold: the elimination of any use of a personal characteristic as a criterion for the conferral of a social benefit, where the personal characteristic is irrelevant to an individual’s entitlement; and the elimination of criteria which, though facially neutral, reduce the ability of individuals with certain personal characteristics to obtain a social benefit.

The “individual justice” model does not attempt to root out prejudicial assumptions; it ignores the fact that justice has distributive effects. This model is opposed to the “social justice” model, which has for its premise the view that discrimination against certain groups is so pervasive that real equality for the members of the group can never be achieved through simple identification and removal of discriminatory barriers. Instead, systemic remedies conferring benefits on the group are required to remedy the lingering effects of past injustice against the group. Thus, the social justice model permits the allocation of social benefits to individuals on the basis of group membership, past discrimination having resulted in the deprivation of social benefits in precisely the same manner.

*Id.* at 500.

ployers have long enjoyed greater freedom under Title VII of the Civil Rights Act of 1964<sup>59</sup> than government employers under the Constitution<sup>60</sup> to engage in aggressive voluntary affirmative action programs aimed at recruiting, hiring, and promoting racial and gender minorities.<sup>61</sup> When properly structured, an employer's voluntary affirmative action plan will not be invalidated under Title VII so long as the plan is consistent with Congress's goal of eliminating discrimination against traditional minorities.<sup>62</sup> However, if a government employer were to implement a similar voluntary affirmative action plan (such as one based on race) and that plan were evaluated under the Constitution, a court would more likely invalidate the plan as unconstitutional.<sup>63</sup> Thus, civil rights statutes, though providing greater protections against civil rights violations than the Constitution, do not unnecessarily hinder private actors who want to achieve social justice through methods like voluntary affirmative action.<sup>64</sup>

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59. 42 U.S.C. § 2000e.

60. *See, e.g.*, Equal Protection Clause of the Fourteenth Amendment, U.S. CONST. amend. XIV (providing that “[n]o State shall . . . deny to any person within its jurisdiction the equal protection of the laws”).

61. *See, e.g.*, *Johnson v. Transportation Agency*, 480 U.S. 616, 640–42 (1987) (approving, for Title VII purposes, a government employer's voluntary gender-based affirmative action plan for women); *United Steelworkers v. Weber*, 443 U.S. 193, 200–08 (1979) (approving a private employer's voluntary race-based affirmative action plan for blacks).

62. *See United Steelworkers*, 443 U.S. at 204. The court quoted Senator Humphrey in stating:

It would be ironic indeed if a law triggered by a Nation's concern over centuries of racial injustice and intended to improve the lot of those who had “been excluded from the American dream for so long” constituted the first legislative prohibition of all voluntary, private, race-conscious efforts to abolish traditional patterns of racial segregation and hierarchy.

*Id.* (quoting 110 CONG. REC. 6552 (1964) (statement by Sen. Humphrey)).

63. *See, e.g., Johnson*, 480 U.S. at 628 n.6 (rejecting Justice Scalia's claim “that the obligations of a public employer under Title VII must be identical to its obligations under the Constitution” and instead concluding that “the statutory prohibition with which that employer must contend was not intended to extend as far as that of the Constitution”). This is not to say that race-based affirmative action plans instituted by government actors are necessarily unconstitutional. Indeed, federal courts have clearly indicated that government may use race as a factor in its affirmative action efforts but that such use is subject to strict scrutiny review. *See, e.g.*, *Regents of the Univ. of Cal. v. Bakke*, 438 U.S. 265, 289 (1978) (holding that strict scrutiny will be applied to “a classification based on race”); *Adarand Constructors, Inc. v. Peña*, 515 U.S. 200, 225–26 (1995) (holding strict scrutiny applies to racial classifications); *Smith v. University of Wash.*, 233 F.3d 1188 (9th Cir. 2000) (recognizing that race may be used as a factor in university admissions decisions, subject to review under a strict scrutiny standard that complies with Powell's opinion in *Bakke*); *Hopwood v. Texas*, 78 F.3d 932, 940 (5th Cir. 1996), *cert. denied*, 518 U.S. 1033 (1996) (“[T]here is now absolutely no doubt that courts are to employ strict scrutiny when evaluating all racial classifications.”).

64. The Supreme Court has also interpreted some civil rights statutes as permitting pri-

## 2. Bob Jones University's public policy limitation

The public policy limitation provides that the Treasury may revoke or, where appropriate, deny tax-exempt charitable status of an organization that acts contrary to “established public policy.”<sup>65</sup> This public policy limitation on charities came from the Treasury in a 1970 News Release.<sup>66</sup> The News Release indicated that the Internal Revenue Service (“IRS”) could not “legally justify” granting charitable status to private schools that racially discriminate, nor could it allow tax deductions for contributions to such schools.<sup>67</sup> The Supreme Court later expressly approved this public policy limitation on charitable activities in *Bob Jones University v. United States*, where the Court upheld the revocation of a charity's tax-exempt status because the charity discriminated against blacks.<sup>68</sup> Even though *Bob Jones University* involved discrimination only against blacks, the IRS (the administrative arm of the Treasury) has posited that the *Bob Jones University* principle applies to any number of public policy matters besides racial discrimination.<sup>69</sup> Included among these other public

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vate rights of action. *See* *Guardians Ass'n v. Civil Serv. Comm'n*, 463 U.S. 582, 635–38 (1983) (concluding that private cause of action for relief exists under Title VI); *Cannon v. University of Chicago*, 441 U.S. 677, 710–16 (1979) (concluding that private right of action exists under Title IX of the Education Amendments Act of 1972).

65. *See Bob Jones Univ.*, 461 U.S. at 586 (“[E]ntitlement to tax exemption depends on meeting certain common law standards of charity—namely, that an institution seeking tax-exempt status must serve a public purpose and not be contrary to *established public policy*.” (emphasis added)); Brennen, *supra* note 3, at 391 n.2 (citing various revenue rulings and general counsel memoranda applying public policy determinations to tax matters).

66. I.R.S. News Release (Jul. 10, 1970), *reprinted in* [1970] 7 Stand. Fed. Tax Rep. (CCH) § 6,790.

67. *See id.* The IRS later revised its policy on discrimination. Rev. Rul. 71-447 formalized the revised policy:

Both the courts and the Internal Revenue Service have long recognized that the statutory requirement of being “organized and operated exclusively for religious, charitable, . . . or educational purposes” was intended to express the basic common law concept [of charity]. . . . All charitable trusts, educational or otherwise, are subject to the requirement that the purpose of the trust may not be illegal or contrary to public policy.

Rev. Rul. 71-447, 1971-2 C.B. 230, *clarified in* Rev. Proc. 72-54, 1972-2 C.B. 834, *superseceded by* Rev. Proc. 75-50, 1975-2 C.B. 587. When the Treasury tried to revoke Revenue Ruling 71-447 and to recognize exemption for discriminatory private schools, a federal court enjoined it from doing so. *See* *Wright v. Regan*, 656 F.2d 820, 837-38 (D.C. Cir. 1981), *rev'd on other grounds*, *Allen v. Wright*, 468 U.S. 737 (1984).

68. *See Bob Jones Univ.*, 461 U.S. at 586.

69. *See, e.g.*, Priv. Ltr. Rul. 89-10-001 (Nov. 30, 1988) (“Although applying on its face only to race discrimination in education, the [public policy power] extends . . . to any activity violating a clear public policy.”). *Accord* Hill and Kirschten, *supra* note 32, at ¶ 2.03[6][c] (“[T]he scope of the public policy doctrine remains unclear, in part because the question of

policy areas might be gender preference,<sup>70</sup> sexual orientation,<sup>71</sup> drug use,<sup>72</sup> or other areas in which public policies are said to be sufficiently “established.”<sup>73</sup>

what public policies trigger the public policy requirement for purposes of the section 501(c)(3) remains undefined . . .”). In determining whether an organization’s activities will be considered permissible under § 501(c)(3), (1) the purpose of the organization must be charitable; (2) the activities must not be illegal, contrary to a clearly defined and established public policy, or in conflict with express statutory restrictions; and (3) the activities must be in furtherance of the organization’s exempt purpose and reasonably related to the accomplishment of the purpose. *See* Rev. Rul. 80-278, 1980-2 C.B. 175. Thus, even where an organization is in strict compliance with “the law,” the public policy power permits the Treasury to revoke or deny charitable status if the organization’s admittedly legal activity violates “established public policy.” *See id.*

70. For example, the recent decision involving the Virginia Military Institute could prompt the Treasury to question whether single gender schools—either all-male or all-female—violate “established public policy” with respect to gender preferences. *See* *United States v. Virginia*, 518 U.S. 515, 556-58 (1996) [hereinafter “VMI”] (holding that state’s policy of admitting only men to a state school violates equal protection); Christopher H. Pyle, *Women’s Colleges: Is Segregation by Sex Still Justifiable After United States v. Virginia?*, 77 B.U. L. REV. 209, 260-71 (1997) (discussing whether women’s colleges have sufficient grounds to exclude men after VMI); Zelinsky, *supra* note 22, at 383-87 (discussing implications of VMI for same-sex tax-exempt institutions); Sugin, *supra* note 22, at 453-54 (discussing the potential broad application of *Bob Jones University* and the public policy limitation and indicating that “VMI might be the crucial precedent for Smith and Wellesley . . . because it establishes that such support is contrary to public policy”). *See* Hill & Kirschten, *supra* note 32, at ¶ 2.03[6][c] (“The case of discrimination based on gender is potentially instructive both because there are adverse judicial precedents of uncertain precedential value and because contemporary issues relating to what may or may not be gender-based discrimination have raised extremely difficult questions.”).

71. In a recent First Amendment free association case, the Supreme Court held that Boy Scouts of America, a tax-exempt charity, has the constitutional right to exclude gay persons from positions of leadership solely because of the person’s sexual orientation. *See* *Boy Scouts of Am. v. Dale*, 530 U.S. 640 (2000); *Arlington County v. White*, 528 S.E.2d 706, 713 (Va. 2000) (Hassell, J., dissenting) (concluding that “common law marriages or ‘same-sex unions’ . . . are not recognized in this Commonwealth and are violative of the public policy of this Commonwealth”).

72. *See, e.g.*, American Bar Association, *Edited Transcript of the January 21, 2000 ABA Tax Section Exempt Organizations Committee Meeting*, EXEMPT ORG. TAX REV. April 2000, at 59 (questioning how the IRS should respond in situations where state or local law makes something legal, like distributing needles to reduce the transmission of HIV among drug users or distributing marijuana for medicinal purposes, but there is arguably a federal policy or law against it). The United States Supreme Court is expected to decide a case this term that addresses the issue of the legality of a state law that permits distribution of marijuana for medicinal purposes while a federal law prohibits such distribution. *See* *United States v. Oakland Cannabis Buyers’ Coop.*, 221 F.3d 1349 (9th Cir. 2000) (*reported in full at* 2000 U.S. App. LEXIS 9963 (9th Cir. Cal. May 10, 2000)), *cert. granted*, *United States v. Cannabis*, 2000 U.S. LEXIS 7699 (U.S. Nov. 27, 2000) (involving an action brought by United States to enjoin Cannabis clubs from distributing marijuana as violations of Controlled Substance Act, 21 U.S.C. § 841).

*C. Inadequacies of Current Civil Rights Restrictions*

Current civil rights restrictions imposed on private charities—because of gaps in coverage, lack of Congressional authority, and unclear limitations on authority—are inadequate to ensure that charities will be penalized if they violate civil rights protected by federal statutes.<sup>74</sup> These restrictions might also be used to hinder attempts to advance social justice through methods like affirmative action, thus undermining civil rights advancement.<sup>75</sup>

*1. Inadequacies of traditional civil rights laws*

Traditional civil rights laws, as currently interpreted, are inadequate to ensure against civil rights violations by private charities because they contain significant gaps in coverage.<sup>76</sup> For example, *Bob Jones University* came before the Supreme Court because none of the traditional civil rights laws existing at that time covered Bob Jones University's discriminatory behavior.<sup>77</sup> Although, from a public policy perspective, most agreed that Bob Jones University's discrimination against blacks was reprehensible, the government was powerless to use its traditional civil rights arsenal against a private, nonstate actor.<sup>78</sup> As explained previously, this traditional civil rights arsenal con-

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73. See INTERNAL REVENUE SERVICE, EXEMPT ORGANIZATION CPE TECHNICAL INSTRUCTION PROGRAM TEXTBOOK ch. L, § 4.b. (1994) [hereinafter "IRS EXEMPT ORGANIZATION TEXTBOOK"] ("Just as the Service responded to public outrage over racial discrimination in education in *Bob Jones* and to possible kickbacks in *GCM 39862*, the Service can be expected to re-evaluate positions in other areas as the public policy considerations become more clearly focused because of Congressional action, decisions of the Executive Branch, or court actions."); Hill and Kirschten, *supra* note 32, at ¶ 2.03[6][c] ("In practical terms, gender, disability, or sexual orientation may well provide the basis of a fundamental public policy that defines the limit of qualification for exemption."). See also National Office Technical Advice Memorandum from the IRS to the Kamehameha Schools/Bernice Pauahi Bishop Estate (Feb. 4, 1999) (on file with author) [hereinafter "Bishop Estate TAM"] (discussing application of public policy power with respect to a tax-exempt Hawaiian school that excluded Caucasians and other non-Hawaiians from admission consideration).

74. See generally Brennen, *supra* note 3, at 394 n.159 (describing application of civil rights laws in private sector context).

75. See *id.*

76. But see Pyle, *supra* note 70, at 215–16 (suggesting that no gap in coverage exists because courts, for example, "may . . . find that tax exemptions to private women's colleges for non-compensatory purposes" constitute FFA for statutory civil rights purposes).

77. See *Bob Jones Univ.*, 461 U.S. at 574.

78. Even today, Bob Jones University continues to discriminate against blacks. See, e.g., *Bob Jones Univ. Museum and Gallery, Inc. v. Commissioner*, 71 T.C.M. (CCH) 3120 (1996) (issuing declaratory judgment that museum, affiliated with non-exempt Bob Jones University, is entitled to be exempt from Federal income taxation under § 501(a) as an organization meet-

sists of constitutional limitations (which do not generally apply to charities) and statutory limitations (which do not apply to particular charities).<sup>79</sup> Thus, Bob Jones University's discrimination against blacks in the 1970s presented the Treasury and the Court with a situation that, short of congressional action, appeared unsolvable unless the Treasury resorted to use of the public policy power.<sup>80</sup>

## 2. *Inadequacies of the public policy limitations*

The Supreme Court's response to the inadequacy of traditional civil rights laws was to recognize in Treasury a public policy power: the power to make tax law decisions based on the Treasury's own assessment of the existence and the clarity of a particular public policy.<sup>81</sup> However, the Treasury's public policy power is also an inadequate tool for advancing social justice because it lacks sufficient legal authority and a clearly defined scope of applicability.<sup>82</sup>

Unfortunately, Congress has not clearly authorized Treasury to make important non-tax public policy decisions with respect to civil rights enforcement.<sup>83</sup> No currently existing federal statute explicitly

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ing the requirements of § 501(c)(3)). However, in order to maintain § 501(c)(3) tax-exempt status for its museum, Bob Jones University allows all, regardless of race, to view its affiliated museum displays. *See id.* ("The museum is open to the public free of charge.").

79. *See* discussion *supra* notes 49–64 and accompanying text.

80. At least one commentator suggests that the IRS's knowing grant of tax-exempt charitable status to organizations that discriminate based on race, like Bob Jones University, might violate the Equal Protection Clause. *See* Sugin, *supra* note 22, at 452–53 (asserting that application of § 501(c)(3) "to authorize exemptions for racially discriminatory private schools, such as Bob Jones University, could potentially violate equal protection" because of the view 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").

81. *See* Brennen, *supra* note 3, at 394 (discussing implied statutory authority of Treasury to regulate public policy).

82. *See id.*; *FDA v. Brown & Williamson Tobacco Corp.*, 529 U.S. 120 (2000). In *Brown & Williamson*, Justice O'Connor, for the majority, writes:

Nonetheless, no matter how "important, conspicuous, and controversial" the issue, and regardless of how likely the public is to hold the Executive Branch politically accountable, an administrative agency's power to regulate in the public interest must always be grounded in a valid grant of authority from Congress. And "in our anxiety to effectuate the congressional purpose of protecting the public, we must take care not to extend the scope of the statute beyond the point where Congress indicated it would stop."

*Id.* at 1315 (quoting *United States v. An Article of Drug*, 394 U.S. 784, 800 (1969)).

83. *See* Brennen, *supra* note 3, at 416 (explaining that Congress has not expressly authorized Treasury to regulate public policy on non-tax matters). In the more than 30 years since the Treasury's adoption of the public policy power in 1970, Congress has enacted no law that would codify the *Bob Jones University* result. *But see Bob Jones Univ.*, 461 U.S. at 601

provides that Treasury has the legal authority to act solely on public policy grounds.<sup>84</sup> In the absence of express congressional authority, the Court in *Bob Jones University* was compelled to rely upon its interpretation of the term “charitable” as used in § 501(c)(3) of the Code as its basis for recognizing Treasury’s public policy power.<sup>85</sup> In doing so, the Court referred to the legislative history of § 501(c)(3) and English charitable trust law.<sup>86</sup> The problem with relying on legislative history to support the Treasury’s definition of “charitable” was that, several years prior, Congress had considered and refused to adopt that very definition.<sup>87</sup> In a recent decision, the Supreme Court

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(stating that “Congress affirmatively manifested its acquiescence in the IRS policy when it enacted the present § 501(i) of the Code, Act of October 20, 1976, Pub. L. 94–568, 90 Stat. 2697 (1976)”). Section 501(i), which prohibits discrimination by social clubs only, provides, in part:

[A social club] shall not be exempt from taxation under [§ 501(a)] for any taxable year if, at any time during such taxable year, the charter, bylaws, or other governing instrument, of such organization or any written policy statement of such organization contains a provision which provides for discrimination against any person on the basis of race, color, or religion.

I.R.C. § 501(i) (2000). However, social clubs, exempt via § 501(c)(7) of the Code, are not charities. Rather, they are “organized for pleasure, recreation, and other nonprofitable purposes, substantially all of the activities of which are for such purposes and no part of the net earnings of which inures to the benefit of any private shareholder.” *Id.* § 501(c)(7). Section 501(i)’s prohibition does not apply to charities, which are exempt via § 501(c)(3) of the Code.

84. In his dissent in *Bob Jones University*, Justice Rehnquist notes that “it seems to me that in § 501(i) Congress showed that when it wants to add a requirement prohibiting racial discrimination to one of the tax-benefit provisions, it is fully aware of how to do it.” *Bob Jones Univ.*, 461 U.S. at 621 (Rehnquist, J., dissenting).

85. *See id.*

86. *See id.* at 588–89.

87. Before Treasury first acted pursuant to its public policy power in 1970, *see* IRS News Release, *supra* note 66, Congress considered and rejected a proposal to amend the Code to provide the Treasury with clear statutory authority to deny charitable status to organizations that discriminate based on race. *See* William N. Eskridge, Jr., *Interpreting Legislative Inaction*, 87 MICH. L. REV. 67, 90 n.143 (1988) (citing H.R. 6342, 89th Cong. (1965), *reprinted in* 111 CONG. REC. 5140 (1965)). In 1965, Congress attempted to pass a bill that would amend the Code “to provide that an organization described in section 501(c)(3) . . . which engages in certain discriminatory practices shall be denied an exemption.” *Id.* This bill failed to become law. *See A Bill to Amend the Internal Revenue Code of 1954 to Provide that an Organization Described in Section 501(c)(3) of Such Code Which Engages in Certain Discriminatory Practices Shall be Denied an Exemption*, H.R. 6342, 89th Cong. (1965), *reprinted in* 111 CONG. REC. 5140 (1965). (A search of the Congressional Index and the Congressional Record do not reflect that the bill ever emerged out of the House Ways and Means Committee.) Congress’s consideration and outright rejection of this amendment to § 501(c)(3) indicates Congress’s “acquiescence in exactly the opposite interpretation” than that posited by the Court in *Bob Jones University*, thus raising concerns regarding the legal legitimacy of the public policy power. *See* Eskridge, *supra* note 87, at 90–91; Mayer G. Freed & Daniel D. Polsby, *Race, Religion & Public Policy: Bob Jones University v. United States*, 1983 SUP. CT. REV. 1 (stating

held that an agency does not ordinarily have regulatory authority with respect to a matter when Congress considered and rejected legislation that would expressly grant such authority.<sup>88</sup> Given that Congress considered and rejected legislation that would implement a narrow version of the public policy power, one can infer that Congress would have also rejected the broad version of the power as understood by the Treasury.<sup>89</sup> Thus, Treasury's public policy power lacks firm legal grounding.<sup>90</sup>

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that hearings were never held on the bill because it had so little support in Congress).

88. See *FDA v. Brown & Williamson Tobacco Corp.*, 529 U.S. 120 (2000). In *Brown & Williamson*, Justice O'Connor describes how Congress' consideration and rejection of several legislative proposals to grant FDA authority to regulate tobacco indicate that FDA lacked such regulatory authority:

[C]ongress considered and rejected several proposals to give the FDA the authority to regulate tobacco. In April 1963, Representative Udall introduced a bill "to amend the Federal Food, Drug, and Cosmetic Act so as to make that Act applicable to smoking products." . . . In December 1963, Representative Rhodes introduced another bill that would have amended the FDCA "by striking out 'food, drug, device, or cosmetic' each place where it appears therein and inserting in lieu thereof 'food, drug, device, cosmetic, or smoking product.'" And in January 1965, . . . Representative Udall again introduced a bill to amend the FDCA "to make that Act applicable to smoking products." None of these proposals became law.

Congress ultimately decided in 1965 to subject tobacco products to the less extensive regulatory scheme of the FCLAA, which created a "comprehensive Federal program to deal with cigarette labeling and advertising with respect to any relationship between smoking and health." The FCLAA rejected any regulation of advertising, but it required the warning, "Caution: Cigarette Smoking May Be Hazardous to Your Health," to appear on all cigarette packages. In the Act's "Declaration of Policy," Congress stated that its objective was to balance the goals of ensuring that "the public may be adequately informed that cigarette smoking may be hazardous to health" and protecting "commerce and the national economy . . . to the maximum extent."

*Id.* at 147–48 (citations omitted).

89. In describing the legislation considered and rejected by Congress as "a narrow version of the public policy power," the intent is to convey the message that the legislation did not attempt to grant Treasury a broad public policy power relating to any number of racial and non-racial matters.

90. The problem with the Court's use of English charitable trust law is that English trust law provides, at best, only tangential support for Treasury's tax law definition of "charitable." See *Bob Jones Univ.*, 461 U.S. at 588–89. The only textual reference to an English law basis is a statement of Lord McNaughten that "charity" in its legal sense comprises four principal divisions: trusts for the relief of poverty; trusts for the advancement of education; trusts for the advancement of religion; and trusts for other purposes beneficial to the community, not falling under any of the preceding. See *id.* at 589 (citing *Commissioners v. Pemsel*, [1891] App. Cas. 531, 583). Further, the Court in *Bob Jones University* cited no statement in the Congressional reports. See *Bob Jones Univ.*, 461 U.S. at 586–88 & n.12 (citing H.R. REP. NO. 91–413, at 35, 43 (1969), reprinted in 1969 U.S.C.C.A.N. 1645, 1680), and little floor debate, see *id.* at 590 (citing 55 CONG. REC. 6728 (1917) (statement of Sen. Hollis)), on

The public policy power is also an inadequate tool for civil rights enforcement because the Court in *Bob Jones University* failed to define the scope of applicability of this power.<sup>91</sup> That is, the Court did not address the limits of the Treasury's power to determine when or if a particular public policy is sufficiently "established" in any context other than whites discriminating against blacks. For example, the Court did not discuss the acceptability of race-based affirmative action programs or single gender private schools as consistent or inconsistent with "established public policy."<sup>92</sup> With respect to race-based affirmative action programs, who is to say whether the Treasury might view these programs as contrary to established public policies affecting race because they involve racial preferences, albeit for blacks and others historically oppressed by American segregation laws?

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§ 501(c)(3) mentioning the public policy requirement. *See also* Robert M. Cover, *The Supreme Court, 1982 Term: Forward: Nomos and Narrative*, 97 HARV. L. REV. 4, 63–64 (1983) ("Neither the text of the Code nor the legislative history before the IRS's 1970 ruling seemed to compel [the Court's] interpretation."). Scholars and courts likewise question the use of trust law concepts in tax settings. *See, e.g.*, Miriam Galston, *Public Policy Constraints on Charitable Organizations*, 3 VA. TAX REV. 291, 292 (1984) (concluding that "trust law does not provide the theoretical foundation for public policy constraints in the area of federal tax law"); Gustafsson, *supra* note 47, at 647 (arguing that the charitable trust law definition of "charitable" should not have been adopted for federal income tax exemption and deductibility of contribution purposes); Brennen, *supra* note 3, at 446 (asserting that Congress has passed no law affirmatively stating that Treasury shall, pursuant to its own determinations of "established public policy," grant or deny tax-exempt charitable status to organizations that discriminate based on race); *International Reform Fed'n v. District Unemployment Compensation Bd.*, 131 F.2d 337, 342–46 (D.C. Cir. 1942) (Miller, J., dissenting) ("There is no necessary identity between the indicia of a charitable trust and those of a charitable purpose which will exempt an agency from taxation."); *Schuster v. Nichols*, 20 F.2d 179, 181 (D. Mass. 1927) (concluding that term "charitable" signifies corporations organized and operated solely for "eleemosynary purposes"). Thus, the Court in *Bob Jones University* incorrectly extended the English trust law definition of "charitable" to United States income tax law. *Cf. Merkel v. Commissioner*, 132 F.3d 844, 850–51 (9th Cir. 1999) (declaring that the Ninth Circuit refused to define "liability" for tax law purposes in same way that term is defined for bankruptcy law purposes).

91. *See* Brennen, *supra* note 3, at 403 (describing analysis used by United States Supreme Court to conclude that Treasury has authority to determine the public purpose of a charity); Hill & Kirschten, *supra* note 32, at ¶ 2.03[6][c] ("In the absence of specific guidance . . . it is neither possible nor prudent to state with certainty what 'clear public policies' other than racial discrimination might lead to nonrecognition or revocation of exempt status.>").

92. *See Bob Jones University*, 461 U.S. at 591. The Treasury has indicated that other matters besides discrimination against blacks are areas contemplated by the public policy power. *See* IRS EXEMPT ORGANIZATION TEXTBOOK, *supra* note 73 ("Just as the Service responded to public outrage over racial discrimination in education in *Bob Jones* and to possible kickbacks in *GCM 39862*, the Service can be expected to re-evaluate positions in other areas as the public policy considerations become more clearly focused because of Congressional action, decisions of the Executive Branch, or court actions.>").

For constitutional law purposes, the Court applies one standard of review when evaluating race preference policies—whether it is examining discrimination against blacks or so-called benign discrimination against whites.<sup>93</sup> The Treasury, through the IRS, has indicated a willingness to follow this constitutional law precedent in making its public policy decisions. For example, in a recent agency decision, the IRS hinted that, in its view, preferences for Hawaiians that disadvantage whites might violate “established public policy”<sup>94</sup> just as government preferences for blacks and Hispanic Americans necessarily violate constitutional law in some judicial circuits.<sup>95</sup>

On a related matter, in *Rice v. Cayetano*,<sup>96</sup> the Court recently decided that the state of Hawaii could not constitutionally prefer Hawaiians to whites and other non-Hawaiians in determining the right to vote for trustees of a state fund benefiting native Hawaiians.<sup>97</sup> Should this constitutional law decision with respect to government actors dictate the Treasury’s public policy decisions with respect to private nongovernmental actors? While the IRS appears to think so,<sup>98</sup> it remains to be seen how the IRS and the Treasury will actually re-

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93. See, e.g., *Regents of the Univ. of Cal. v. Bakke*, 438 U.S. 265, 295 (1978) (“It is far too late to argue that the guarantee of equal protection to all persons permits the recognition of special wards entitled to a degree of protection greater than that accorded others.”). See also *Adarand Constructors, Inc. v. Peña*, 515 U.S. 200, 225–26 (1995) (holding strict scrutiny applies to “benign” and non-benign racial classifications); *Hopwood v. Texas*, 78 F.3d 932, 940 (5th Cir. 1996), *cert. denied*, 518 U.S. 1033 (1996) (“[T]here is now absolutely no doubt that courts are to employ strict scrutiny when evaluating all racial classifications, including those characterized by their proponents as ‘benign’ or ‘remedial.’”).

94. See *Bishop Estate TAM*, *supra* note 73. In the *Bishop Estate TAM*, the IRS advised the Bishop Estate, a tax-exempt trust, that its policy of only admitting Hawaiian children to the trust’s school is consistent with established public policy. *Id.* However, the IRS continued that the Bishop Estate “should consider requesting a private letter ruling on whether the [Supreme Court’s] decision [in *Rice v. Cayetano*] has any effect on the [Service’s] analysis.” *Id.*; see also Evelyn Brody, *A Taxing Time for Bishop Estate: What is the I.R.S. Role in Charity Governance?*, 21 U. HAW. L. REV. 537, 542 n.27 (1999).

95. See *Hopwood*, 78 F.3d at 962 (concluding that, in the Fifth Circuit, government can never use race as a factor when making decisions about public law school admissions), *cert. denied*, 518 U.S. 1033 (1996); *Podberesky v. Kirwan*, 38 F.3d 147, 161–62 (4th Cir. 1994), *cert. denied*, 514 U.S. 1128 (1995) (concluding that a race-exclusive scholarship program at University of Maryland violated Equal Protection Clause of Fourteenth Amendment).

96. See *Rice v. Cayetano*, 528 U.S. 495 (2000).

97. See *id.*

98. See *Bishop Estate TAM*, *supra* note 73. *But see* Brennen, *supra* note 3, at 435 n.236 (noting generally that evaluation of constitutional law standards is not synonymous with evaluation of public policy standards); Hill & Kirschten, *supra* note 32, at ¶ 2.03[6][c] (explaining that Service’s reliance on Constitutional law standards when making public policy decisions is “flaw[ed]”).

spond as it evaluates race-conscious programs involving preferences for Hawaiians in light of the Court's decision in *Rice*.<sup>99</sup>

In sum, the public policy power outlined by the Court in *Bob Jones University* is inadequate as a tool for broad civil rights enforcement because that power lacks sufficient legislative authority and its scope is unclear. Although the Court cautiously stated that violation of a given public policy must be "established," it set no clear boundaries for the Treasury to determine when a policy other than discrimination against blacks is sufficiently established.<sup>100</sup> Conceivably, in this era of affirmative action retrenchment, Treasury might interpret a private charity's affirmative efforts to achieve social justice as violating "established public policy" against redressing the effects of pervasive societal discrimination through use of race-conscious policies.

### III. FEDERAL FINANCIAL ASSISTANCE UNDER FEDERAL CIVIL RIGHTS STATUTES

As discussed in Part II, current civil rights restrictions imposed on private tax-exempt charities are inadequate for a number of reasons. These restrictions do not cover all charities and vest too much discretionary power in the Treasury to make initial determinations about denial or revocation of tax-exempt status. The legislative and judicial decisions in this area are a slender reed upon which to rely for civil rights protection. For example, recent Supreme Court decisions make it likely that the Court's decision in *Bob Jones University* will be insufficient to advance or protect important and desirable social justice goals.<sup>101</sup> One possible solution to the inadequacies of the current civil rights restrictions imposed on charities is to develop an interpretive framework that takes advantage of existing civil rights laws that apply to private actors generally. Specifically, if courts and agencies viewed tax-exempt charities as recipients of FFA for purposes of civil rights statutes that cover such recipients, all charities

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99. To date, the IRS has not issued a follow-up TAM or other letter ruling to the Bishop Estate on the matter of the Bishop Estate's school's policy of limiting admissions to Hawaiian children.

100. See *Bob Jones Univ. v. United States*, 461 U.S. 574, 592 (1983). The Court stated: We are bound to approach these questions with full awareness that determinations of public benefit and public policy are sensitive matters with serious implications for the institutions affected; a declaration that a given institution is not "charitable" should be made only where there can be no doubt that the activity involved is contrary to a fundamental public policy.

*Id.*

101. See discussion *supra* notes 96-99 and accompanying text.

would be subject to civil rights restrictions in a more uniform, predictable, and just manner.

*A. Civil Rights Statutes that Cover Recipients of FFA*

Congress has enacted many statutes to protect citizens' civil rights.<sup>102</sup> However, this article will only examine those civil rights laws that apply to private actors who receive FFA.<sup>103</sup> Title VI of the Civil Rights Act of 1964<sup>104</sup> and Title IX of the Education Amendments Act of 1972<sup>105</sup> are the principal laws that forbid discrimination based on race and sex, respectively, by private actors that receive FFA.<sup>106</sup> The Rehabilitation Act of 1973 and the Age Discrimination Act also impose civil rights restrictions based on a private actor's receipt of FFA.<sup>107</sup> This subpart will describe each of these laws in turn.

*1. Discrimination based on race, color, or national origin*

Title VI, first enacted in 1964,<sup>108</sup> provides that: "No person in the United States shall, on the ground of race, color, or national origin, be excluded from participation in, be denied the benefits of, or be subjected to discrimination under any program or activity receiving Federal financial assistance."<sup>109</sup> Title VI's prohibitions against exclusion, denial, or discrimination came from Congress's powers under the Spending Clause to set conditions on the receipt of federal funds<sup>110</sup> and from the Thirteenth and Fourteenth Amendments.<sup>111</sup> Under Title VI, federal agencies "empowered to extend Federal Financial assistance" through "grant[s] loan[s] or contract[s]" to a private actor for "any program or activity" are required to enforce the

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102. *See, e.g.*, Title VI of the Civil Rights Act of 1964, 42 U.S.C. § 2000d (2000); Title IX of the Education Amendments of 1972, 20 U.S.C. § 1681(a) (2000); Rehabilitation Act of 1973, 29 U.S.C. 794(a) (2000); Age Discrimination Act, 42 U.S.C. § 6101 (2000); Americans With Disabilities Act of 1990, 42 U.S.C. § 12101 (2000); Equal Credit Opportunity Act, 15 U.S.C. § 1691 (2000); Equal Employment Opportunity Act of 1972, 42 U.S.C. § 2000-e (2000).

103. *See, e.g.*, Title VI of the Civil Rights Act of 1964, 42 U.S.C. § 2000d (2000); Title IX of the Education Amendments of 1972, 20 U.S.C. § 1681(a) (2000); Rehabilitation Act of 1973, 29 U.S.C. § 794(a) (2000); Age Discrimination Act, 42 U.S.C. § 6101 (2000).

104. 42 U.S.C. § 2000d.

105. 20 U.S.C. §§ 1681-86.

106. *See* SMOLLA, *supra* note 6, § 8.01.

107. 29 U.S.C. § 794; 42 U.S.C. § 6102.

108. *See* Act of July 2, 1985, Pub. L. No. 88-352, 78 Stat. 252.

109. 42 U.S.C. § 2000d.

110. *See* U.S. CONST. art. I, § 8.

111. *See* SMOLLA, *supra* note 6, § 8.02[1].

provisions of Title VI.<sup>112</sup> In its enforcement role, the federal agency is authorized to seek voluntary compliance with the operative anti-discrimination provisions of Title VI and, failing voluntary compliance, to threaten to terminate the violator's federal financial funding.<sup>113</sup>

### 2. *Gender discrimination in education*

Title IX of the Education Amendments Act of 1972 provides: "No person in the United States shall, on the basis of sex, be excluded from participation in, be denied the benefits of, or be subjected to discrimination under any education program or activity receiving Federal financial assistance."<sup>114</sup> Though narrower in scope than Title VI,<sup>115</sup> Title IX relies on the exact same jurisdictional basis as Title VI; that is, Title IX only applies if the alleged civil rights violator acts within the context of a program or activity "receiving Federal financial assistance."<sup>116</sup> Thus, it is the meaning of this jurisdictional phrase that is the focus of this article's thesis.

### 3. *Discrimination based on a disability*

The Rehabilitation Act of 1973 also imposes civil rights restrictions on private entities that receive FFA.<sup>117</sup> The Rehabilitation Act, which prohibits discrimination based on disability, provides:

No otherwise qualified individual with a disability in the United States, as defined in section 7(20) [29 U.S.C. § 706(20)], shall, solely by reason of her or his disability, be excluded from the participation in, be denied the benefits of, or be subjected to discrimination under any program or activity receiving Federal financial assistance . . . .<sup>118</sup>

112. 42 U.S.C. § 2000d-1.

113. *See* *Caufield v. Board of Educ.*, 632 F.2d 999 (2d Cir. 1980), *cert. denied*, 450 U.S. 1030 (1981).

114. 20 U.S.C. § 1681(a).

115. While Title VI applies to "any program or activity." 42 U.S.C. § 2000d (1994). Title IX only applies to "any *education* program or activity." *Id.* § 1681(a) (emphasis added).

116. 20 U.S.C. § 1681(a).

117. 29 U.S.C. § 794 (2000).

118. *Id.* § 794(a).

#### 4. *Discrimination based on age*

The Age Discrimination Act prohibits discrimination based on age by private entities that receive FFA. The relevant portion of the Age Discrimination Act provides:

Pursuant to regulations prescribed under [42 U.S.C. § 6103], and except as provided by [42 U.S.C. § 6103(b)] and [42 U.S.C. § 6103(c)], no person in the United States shall, on the basis of age, be excluded from participation in, be denied the benefits of, or be subjected to discrimination under, any program or activity receiving Federal financial assistance.<sup>119</sup>

#### B. *Traditional Interpretations of the Phrase FFA*

Courts have not uniformly interpreted the phrase FFA for federal civil rights statutory purposes to include federal tax benefits. While some federal district and circuit courts addressing the issue have concluded (either in dicta or otherwise) that tax exemptions, credits, and deductions may be treated as FFA,<sup>120</sup> other courts have concluded otherwise.<sup>121</sup> For example, Title VI defines FFA as “assistance to any program or activity, by way of grant, loan, or contract other than a contract of insurance or guaranty.”<sup>122</sup> The typical regulation issued by federal agencies pursuant to Title VI provides:

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119. 42 U.S.C. § 6102.

120. *See, e.g.*, *M.H.D. v. Westminster Schools*, 172 F.3d 797, 802 n.12 (11th Cir. 1999) (rejecting jurisdiction of the case because the statute of limitations lapsed and concluding that the claim that tax-exemption is FFA is neither immaterial nor wholly frivolous); *Glantz v. Automotive Service Ass'n of Pa., Inc.*, 1991 U.S. Dist. LEXIS 18299 (E.D. Pa. 1991) (holding that plaintiff's claim that private receipt of federal tax credits constitutes federal assistance under Title VI was dismissed because plaintiff did not allege that plaintiff was the intended beneficiary of the federal assistance); *Paralyzed Veterans of Am. v. Civil Aeronautics Bd.*, 752 F.2d 694, 709 (D.C. Cir. 1985) (holding that while investment tax credits available to railroad and airline industries under § 46(a)(8) do not amount to assistance that triggers coverage by section 504, the *McGlotten* “fundamental” principle that tax benefits *may* constitute FFA is sound); *National Alliance v. United States*, 710 F.2d 868, 876 n. 14 (D.C. Cir. 1983) (stating that *McGlotten* and other like decisions “call into question whether an organization enjoying an educational tax exemption under federal law may deny membership on the basis of race”).

121. *See, e.g.*, *Martin v. Delaware Law Sch. of Widener Univ.*, 625 F. Supp. 1288, 1302 n.13 (D. Del. 1985) (stating, under Rehabilitation Act, that “‘assistance’ connotes transfer of government funds by way of subsidy, not merely exemption from taxation”), *aff'd*, 884 F.2d 1384 (3d Cir.), *cert. denied*, 493 U.S. 966 (1989); *Stewart v. New York Univ.*, 430 F. Supp. 1305, 1314 (S.D.N.Y. 1976) (finding tax benefits insufficient to create FFA under Title VI).

122. *See* 42 U.S.C. § 2000d-1.

[The term] “federal financial assistance” includes (1) grants and loans of Federal funds, (2) the grant or donation of Federal property . . . , (3) the detail of Federal personnel, (4) the sale and lease of, and the permission to use . . . Federal property . . . without consideration or at a nominal consideration, . . . and (5) any Federal agreement . . . which has as one of its purposes the provision of assistance.<sup>123</sup>

However, these regulations do not specifically state whether FFA includes federal tax benefits. Instead, courts have provided guidance in this regard.

*Grove City College v. Bell* is the seminal case in which the Supreme Court generally outlined its interpretation of FFA for civil rights statutory purposes, doing so in the context of defining what a “program or activity” is under Title IX.<sup>124</sup> In *Grove City College*, however, the Court did not extend its analysis to specifically consider tax benefits as a form of FFA.

While the Supreme Court has not addressed the issue of tax benefits as FFA, several lower courts have. Two significant reported lower court cases involving whether FFA includes tax benefits are *McGlotten v. Connally*<sup>125</sup> and *Bachman v. American Society of Clinical Pathologists*.<sup>126</sup> *McGlotten* and *Bachman* were decided prior to *Grove City College* and involved interpretation of FFA as used in Title VI and section 504 of the Rehabilitation Act of 1973.

This subpart will, first, outline the general interpretation of FFA as articulated by the Supreme Court in *Grove City College v. Bell*.<sup>127</sup> Second, this subpart will discuss those lower court decisions that address the specific issue of whether tax benefits are a form of FFA for civil rights statutory purposes.<sup>128</sup> This subpart will conclude by comparing and contrasting these court decisions to discern the correct

123. 7 C.F.R. § 15.2 (2001) (Department of Agriculture); *see also* 28 C.F.R. § 42.101 (Department of Justice); 45 C.F.R. § 80.13 (2001) (Department of Health, Education and Welfare).

124. *See* *Grove City College v. Bell*, 465 U.S. 555 (1984).

125. 338 F. Supp. 448, 462 (D.D.C. 1972) (concluding that, while provision of tax exemption for 501(c)(7) social clubs does not come within scope of Title VI, provision of tax exemption for 501(c)(8) fraternal organizations and provision of tax deductions for 170(c) charitable contributions are grants of FFA within scope of Title VI).

126. 577 F. Supp. 1257, 1265 (D.N.J. 1983) (concluding that tax exemption alone is not FFA rendering organization as whole subject to Title VI).

127. *See* discussion *infra* notes 130–56 and accompanying text.

128. *See* discussion *infra* notes 160–87, 192–99 and accompanying text.

analytical approach that should be used when questioning whether FFA includes tax benefits.<sup>129</sup>

1. *FFA generally*

*Grove City College* involved the Supreme Court's interpretation of "receiving 'FFA'" as used in Title IX of the Education Act Amendments of 1972.<sup>130</sup> Grove City was a private college that refused to accept state and federal financial support so that it could avoid government oversight and maintain its institutional autonomy.<sup>131</sup> Accordingly, Grove City refused to participate in government aid programs under which the government made payments directly to the college or indirectly to the college through student aid programs involving government loans, work study, or most government grants.<sup>132</sup> However, Grove City did accept students who received federal Better Education Opportunity Grants ("BEOG").<sup>133</sup> BEOGs required very little involvement by Grove City because the United States Department of Education performed most administrative tasks relating to the grants, such as calculating the amount awarded to each student and paying that amount directly to the student (who then paid the amount over to Grove City as tuition).

Grove City's only involvement in the BEOG grant program, other than being a recipient of the grant money as tuition, was the making of required certifications to appropriate federal agencies.<sup>134</sup>

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129. See discussion *infra* notes 200–04 and accompanying text.

130. See *Grove City College*, 465 U.S. at 557. The pertinent portion of Title IX provided: "No person in the United States shall, on the basis of sex, be excluded from participation in, be denied the benefits of, or be subjected to discrimination under any education program or activity receiving Federal financial assistance . . ." *Id.* at n.1 (citing 20 U.S.C. § 1681(a)). Title IX also directs agencies awarding most types of assistance to promulgate regulations to ensure that recipients adhere to that prohibition. Compliance with departmental regulations may be secured by termination of assistance "to the particular program, or part thereof, in which . . . noncompliance has been . . . found" or by "any other means authorized by law." *Id.* at 557–58 n.2 (citing 20 U.S.C. § 1682).

131. See *Grove City College*, 465 U.S. at 559.

132. See *id.*

133. See *id.* BEOGs were authorized by 20 U.S.C. § 1070a (1982).

134. The Department of Education established an Alternative Disbursement System for schools like Grove City that wanted little to do with the administration of BEOGs. Under the Regular Disbursement System, in which most schools participated, the Department estimated the amount a school needed for grants and advanced that amount to the school, which then selected students, calculated awards, and distributed the grants to students. 34 C.F.R. §§ 690.71–85 (1983). Under the Alternative Disbursement System, participating schools make appropriate certifications to the Department, but the Department calculates awards and makes disbursements directly to students. *Id.* §§ 690.91–96.

Among these required certifications was that Grove City sign an Assurance of Compliance agreeing to comply with Title IX's prohibition (which applied to all recipients of FFA) against discrimination based on sex. The Department of Education defined FFA to include:

A grant or loan of Federal financial assistance, including funds made available for: . . . (ii) Scholarships, loans, grants, wages or other funds extended to any entity for payment to or on behalf of students admitted to that entity, or extended directly to such students for payment to that entity.<sup>135</sup>

The Department of Education defined "recipient" of FFA to include: "[Any] public or private agency, institution, or organization, or other entity, or any person, to whom Federal financial assistance is extended directly or through another recipient and which operates an education program or activity which receives or benefits from such assistance."<sup>136</sup>

Claiming that it was not a recipient of FFA under these rules, and therefore not required to comply with Title IX, Grove City refused to sign the Assurance of Compliance. Accordingly, the Department of Education, pursuant to its enforcement and regulatory authority with respect to Title IX, refused to award BEOG's to students attending Grove City.<sup>137</sup> Grove City and several of its students sued the agency in federal court and won on technical grounds at the district court level<sup>138</sup> but eventually lost on appeal to the Third Cir-

135. *Id.* § 106.2(g)(1).

136. *Id.* § 106.2(h).

137. Section 902 of 20 U.S.C. § 1682 provides in part:

Each Federal department and agency which is empowered to extend Federal financial assistance to any education program or activity, by way of grant, loan, or contract other than a contract of insurance or guaranty, is authorized and directed to effectuate the provisions of section [901] with respect to such program or activity by issuing rules, regulations, or orders of general applicability which shall be consistent with achievement of the objectives of the statute authorizing the financial assistance in connection with which the action is taken. . . . Compliance with any requirement adopted pursuant to this section may be effected (1) by the termination of or refusal to grant or to continue assistance under such program or activity to any recipient . . . or (2) by any other means authorized by law . . . .

20 U.S.C. § 1602 (2000).

138. *Grove City College v. Harris*, 500 F. Supp. 253 (1980). The District Court held that BEOGs were "[contracts] of insurance or guaranty" that could not be terminated under Title IX; that Grove City could not be required to execute an Assurance of Compliance because either Subpart E of the Title IX regulations, which prohibits discrimination in employment, was invalid or Title IX permitted termination only upon an actual finding of sex discrimination, not a mere refusal to execute an Assurance; and that affected students were entitled to hearings before their aid could be discontinued. The Supreme Court has since up-

cuit Court of Appeal. Relying on close scrutiny of the language and legislative history of Title IX, the Third Circuit held that Title IX applied to both direct and indirect assistance and that colleges with students receiving BEOG grants were recipients of FFA for purposes of Title IX.<sup>139</sup>

On writ of certiorari, the Supreme Court affirmed the Third Circuit, concluding that the Department of Education could terminate Grove City's status as a school eligible to enroll students receiving BEOG's because of Grove City's status as a recipient of FFA. In reaching this conclusion, the Court looked to the statutory language of Title IX, Congress's intent, and the Department's administrative interpretation.

According to the Court in *Grove City College*, the structure of the legislation creating the BEOG grant program and Title IX's nondiscrimination requirement "strongly suggests" that the grants were intended to be a form of indirect FFA.<sup>140</sup> The Court noted that Congresspersons referred to the special grants provision as the "centerpiece of the bill"<sup>141</sup> and that "Title IX [related] directly to [its] central purpose."<sup>142</sup> Thus, in the words of the Court, it would be "anomalous" to find that the grant program was not intended to "trigger coverage under Title IX."<sup>143</sup>

The Court stated that the text of Title IX's nondiscrimination requirement contains no indication that Congress perceived any substantive difference between direct aid to a college and indirect aid received by a college through its students. To the contrary, the Court refused to read limitations on Title IX's applicability that were not apparent on the face of the statute.<sup>144</sup>

The Court also determined that Congress' intent and the Department's administrative interpretations support the conclusion that Grove City was a recipient of FFA for Title IX purposes. As noted by the Court, "the BEOG program was structured to ensure that it effectively supplements the College's own financial aid program,"<sup>145</sup> and Congress was aware of this when it enacted amendments to Title IX in 1972.<sup>146</sup> One of the purposes of those 1972 amendments relat-

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held the validity of Subpart E in *North Haven Bd. of Educ. v. Bell*, 456 U.S. 512 (1982).

139. See *Grove City College v. Bell*, 687 F.2d 684 (3d Cir. 1982).

140. See *Grove City College v. Bell*, 465 U.S. 555, 563 (1984).

141. *Id.* (quoting from 118 Cong. Rec. 20297 (1972) (Rep. Pucinski)).

142. *Id.* (quoting from 117 Cong. Rec. 30412 (1971) (Sen. Bayh)).

143. *Id.*

144. See *id.* at 564.

145. *Id.* at 565.

146. See *id.* at 565-66 (citing H.R. Rep. No. 92-554, at 244 (1972) (Supplemental

ing to student aid was to “[provide] assistance to institutions of higher education.”<sup>147</sup> Notably, the legislative history of Title VI of the Civil Rights Act of 1964,<sup>148</sup> after which Title IX was patterned,<sup>149</sup> indicates Congress’s contemplation that a school’s receipt of student aid funds (like those provided by the BEOG grants) would trigger Title VI coverage.<sup>150</sup> The relevant coverage language contained in Title IX was identical to that contained in Title VI. Accordingly, the Court could find no reason to conclude that Congress envisioned a different meaning for FFA for Title IX purposes.<sup>151</sup> Congress reinforced this view when it failed to overturn the Department’s administrative determination that FFA included government aid provided to students attending a particular school.<sup>152</sup>

*Grove City College* demonstrates that “FFA,” for civil rights statutory purposes, essentially requires that a private entity receive some direct or indirect financial benefit from a governmental source. There is no requirement that the benefit be subject to governmental control or even governmental restrictions. In fact, unless the statute on its face expressly limits Title IX’s applicability, the Court has resisted the idea that Title IX does not apply.<sup>153</sup> Further, if the benefit

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Views)); 117 Cong. Rec. 2007 (Sen. Pell), 37778, 37782 (Rep. Quie), 39256 (Rep. Steiger) (1971); 118 Cong. Rec. 20295 (Rep. Reid), 20297 (Rep. Pucinski), 20312 (statement of Isaac K. Beckes), 20310 (letter from Kingman Brewster, Jr.), 20324 (Rep. Mitchell) (1972).

147. See *Grove City College*, 465 U.S. at 566 (citing 20 U.S.C. § 1070(a)(5)).

148. Pub. L. 88–352, 78 Stat. 252, 42 U.S.C. § 2000d–2007. Section 601 of Title VI provides: “No person in the United States shall, on the ground of race, color, or national origin, be excluded from participation in, be denied the benefits of, or be subjected to discrimination under any program or activity receiving Federal financial assistance.”

149. See *Cannon v. University of Chicago*, 441 U.S. 677, 684–85 (1979); 118 Cong. Rec. 5807 (1972) (Sen. Bayh).

150. See *Grove City College*, 465 U.S. at 566 (citing H.R. Rep. No. 914, 88th Cong., 1st Sess., 104–105 (1963); 110 Cong. Rec. 13388 (1964) (Sen. McClellan)).

151. See *id.*

152. See *id.* at 568. Relying on post-enactment legislative history, the Court in *Grove City College* noted:

The Department’s sex discrimination regulations made clear that “scholarships, loans, [and] grants . . . extended directly to . . . students for payment to” an institution constitute federal financial assistance to that entity. 40 Fed. Reg. 24137 (1975). . . . Congress was afforded an opportunity to invalidate aspects of the regulations it deemed inconsistent with Title IX. The regulations were clear, and Secretary Weinberger left no doubt [in congressional testimony] concerning the Department’s position that “the furnishing of student assistance to a student who uses it at a particular institution . . . [is] Federal aid which is covered by the statute.”

*Id.* (quoting *Sex Discrimination Regulations: Hearings Before the Subcommittee on Postsecondary Education of the House Committee on Education and Labor*, 94th Cong. 482 (1975) (statement of Secretary Weinberger)). Yet, neither House passed a disapproval resolution.

153. See *Grove City College*, 465 U.S. at 564.

at issue was intended by Congress to provide assistance to educational institutions, the Court will be inclined to find that the institutions must comply with the relevant civil rights laws.<sup>154</sup> Thus, it appears as though, so long as a private entity receives a traceable financial benefit from the federal government and Congress intended that benefit to be a type of assistance, that entity will be treated as a recipient of FFA. In these circumstances, such an entity is subject to the restrictions of Title IX.

Further, since Title VI and Title IX are interpreted consistent with one another in regards to the FFA language,<sup>155</sup> private entities receiving traceable financial benefits from the federal government are also subject to the restrictions of Title VI.<sup>156</sup> Given this interpretive background, there still remains the question of whether courts should uniformly interpret FFA as including tax benefits.

## 2. Tax-exemptions and tax deductions as FFA

*McGlotten v. Connally*<sup>157</sup> and *Bachman v. American Society of Clinical Pathologists*,<sup>158</sup> both decided by federal district courts prior to *Grove City College*, are the only two reported cases that exhaustively address this question of whether FFA includes tax benefits.<sup>159</sup>

154. *See id.* at 566.

155. *See* discussion *supra* notes 151–52 and accompanying text.

156. *See id.*

157. 338 F. Supp. 448, 462 (D.D.C. 1972).

158. 577 F. Supp. 1257, 1265 (D.N.J. 1983).

159. While other courts have addressed the issue of the equivalence of tax benefits and FFA, none has provided as detailed analysis as that contained in *McGlotten* and *Bachman*. *See, e.g.,* M.H.D. v. Westminster Schools, 172 F.3d 797, 802 n.12 (11th Cir. 1999) (rejecting jurisdiction of case because statute of limitation lapsed and concluding that a claim that tax-exemption is FFA is neither immaterial nor wholly frivolous); *Glantz v. Automotive Serv. Ass'n of Pa., Inc.*, 1991 U.S. Dist. LEXIS 18299, (E.D. Pa. 1991) (dismissing plaintiffs claim that private actor's receipt of federal tax credits constitutes federal assistance under Title VI because plaintiff did not allege that plaintiff is intended beneficiary of the federal assistance); *Paralyzed Veterans of Am. v. Civil Aeronautics Bd.*, 752 F.2d 694, 709 (D.C. Cir. 1985) (holding that, while investment tax credits available to railroad and airline industries under § 46(a)(8) do not amount to assistance that triggers coverage by section 504, the *McGlotten* "fundamental" principle that tax benefits *may* constitute FFA is sound); *National Alliance v. United States*, 710 F.2d 868, 876 n.14 (D.C. Cir. 1983) (indicating that *McGlotten* and other like decisions "call into question whether an organization enjoying an educational tax exemption under federal law may deny membership on the basis of race"). *Cf. Martin v. Delaware Law Sch. of Widener Univ.*, 625 F. Supp. 1288, 1302 n.13 (D. Del. 1985) (stating, under Rehabilitation Act, that "'assistance' connotes transfer of government funds by way of subsidy, not merely exemption from taxation"), *aff'd*, 884 F.2d 1384 (3d Cir.), *cert. denied*, 493 U.S. 966 (1989); *Stewart v. New York Univ.*, 430 F. Supp. 1305, 1314 (S.D.N.Y. 1976) (finding tax benefits insufficient to create FFA under Title VI).

a. *McGlotten*: *Tax benefits may be FFA*. The issue in *McGlotten* was whether FFA for Title VI purposes includes tax exemptions for nonprofit social clubs,<sup>160</sup> tax exemptions for fraternal organizations,<sup>161</sup> and tax deductions for contributions to fraternal organizations.<sup>162</sup> *McGlotten* involved a class action suit filed against the Treasury by a black man who was denied membership in a tax-exempt private club.<sup>163</sup> The *McGlotten* plaintiff sought to enjoin the Treasury from granting tax exemption and tax deduction benefits to nonprofit social clubs and fraternal organizations that refuse membership to blacks. Among the plaintiff's many grounds for relief was that these tax benefits are a type of FFA<sup>164</sup> and, thus, violate Title VI's prohibition against providing federal assistance to programs that discriminate based on race.<sup>165</sup>

In analyzing the issue of whether tax benefits may count as FFA, the court in *McGlotten* relied primarily on the "plain purpose" of Title VI since the legislative history contained no information on the issue.<sup>166</sup> The court determined that the purpose of Title VI is to eliminate discrimination in programs or activities benefiting from FFA.<sup>167</sup> Thus, the court viewed "[d]istinctions as to the method of distribution of federal funds or their equivalent [as] . . . beside the point."<sup>168</sup> Invoking tax expenditure theory,<sup>169</sup> the court in *McGlotten*

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160. The tax exemption for nonprofit social clubs is authorized by § 501(c)(7). Social clubs are described in § 501(c)(7) as "[c]lubs organized and operated exclusively for pleasure, recreation, and other non-profitable purposes, no part of the net earnings of which inures to the benefit of any private shareholder." I.R.C. § 501(c)(7) (2000).

161. The tax exemption for fraternal organizations is authorized by § 501(c)(8). Fraternal organizations are described in § 501(c)(8) as entities "operating under the lodge system or for the exclusive benefit of the members of a fraternity itself operating under the lodge system, and providing for the payment of life, sick, accident, or other benefits to the members of such society, order, or association or their dependents." *Id.* § 501(c)(8).

162. The tax deduction for contributions to fraternal organizations is authorized by § 170(c)(4). Section 170(c)(4) provides that the term "charitable contribution" means a contribution to or for the use of "a domestic fraternal society, order, or association, operating under the lodge system, but only if such contribution or gift is to be used exclusively for religious, charitable, scientific, literary, or educational purposes, or for the prevention of cruelty to children or animals." *Id.* § 170(c)(4).

163. *See McGlotten*, 338 F. Supp. at 450.

164. The plaintiff in *McGlotten* asserted three separate bases for relief: (1) that granting the tax benefits violates the Constitution, (2) that the Internal Revenue Code does not authorize granting these tax benefits, and (3) that granting the tax benefits violates Title VI. *See id.*

165. *See id.* at 450, 460–62.

166. *Id.* at 461 ("In the absence of strong legislative history to the contrary, the plain purpose of the statute is controlling.").

167. *See id.*

168. *Id.*

concluded that the only significant issue with respect to the specific tax benefits granted to social clubs and fraternal organizations was whether these benefits “relate primarily to the operation of the tax itself.”<sup>170</sup> If so, the specific benefit is not the type of federal assistance contemplated by Congress as compelling Title VI coverage.<sup>171</sup>

The court in *McGlotten* concluded that the social club tax exemption is not FFA because it is limited to member-generated funds only and it is available to social clubs no matter what activity the club conducts.<sup>172</sup> The limitation to member-generated funds<sup>173</sup> indicates that the social club tax exemption is granted simply as a result of Congress’s desire to properly define income that should be taxable.<sup>174</sup> According to the Court, member-generated funds should not be taxed because the funds are merely “shifted from one pocket to another, both within the same pair of pants.”<sup>175</sup> Thus, the social club exemption reflects the perception that, as to member-generated funds, social clubs do not operate as entities separate from their members.<sup>176</sup> Further, the social club’s tax exemption (regardless of the activity the club conducts) indicates that the government is not encouraging discrimination by the “appearance of government approval.”<sup>177</sup>

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169. See Sugin, *supra* note 22, at 447 (“Applying tax expenditure analysis[,] . . . 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.’”).

170. *McGlotten*, 338 F. Supp. at 461. (“[T]he deductions provided in the Code are not all cut from the same cloth. Most relate primarily to the operation of the tax itself, and thus would not constitute a grant of FFA.”).

171. See *id.*

172. See *id.* at 462.

173. According to the *McGlotten* court, all income of nonprofit social clubs, including passive income, is taxed at regular corporate rates by § 511 as unrelated business taxable income. See *id.* at 457–58. However, income derived from members is exempt from this unrelated business income tax as “exempt function income.” *Id.* at 458.

174. See *id.*

175. *Id.*

176. See *id.*

177. *Id.* It is unclear from the *McGlotten* opinion whether the court’s analysis with respect to “government approval” was necessary to decide the Title VI coverage issue because of the court’s cross-reference within the opinion from its Title VI analysis to its constitutional analysis. See *id.* at 462 n.71. The obstacles involved with trying to establish that the actions of a private actor constitute state action for constitutional law purposes are huge, see Sugin, *supra* note 22, at 431 (“The lack of government control inherent in provision of tax benefits supports the argument that such benefits cannot constitute state action.”), but the task is not insurmountable. See *Burton v. Wilmington Park Auth.*, 365 U.S. 715 (1961) (holding that private restaurant’s decision to exclude blacks was state action because restaurant was tenant of city-owned parking garage, even though city had no control over operations of restaurant).

Unlike the social club tax exemption, the court in *McGlotten* concluded that the fraternal order tax exemption is FFA because it exempts all income from taxation (including passive investment income) and is available only to government-specified groups conducting only government-specified activities.<sup>178</sup> The fraternal order tax exemption is not simply a way of defining taxable income.<sup>179</sup> Instead, according to the court, this tax exemption “operates in fact as a subsidy in favor of the particular activities these groups are pursuing,” unlike the social club tax exemption, which is available no matter what activity the social club conducts.<sup>180</sup> Since the fraternal order tax exemption is more of a specific subsidy, as opposed to a general subsidy like the social club tax exemption, the court concluded that the fraternal order tax exemption is FFA for Title VI purposes.<sup>181</sup> The *McGlotten* court also determined that the fraternal order tax deduction is clearly FFA because the deduction is not required for income-defining purposes.<sup>182</sup> Instead, the tax deduction acts as a matching government grant available for government-specified purposes and to government-specified organizations.<sup>183</sup>

The *McGlotten* case, thus, provides a two-tiered analysis for courts to determine if a particular tax benefit is FFA. First, the tax benefit must be the type that Congress intended as more than an income-defining provision.<sup>184</sup> For example, if Congress’s intent when

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Nevertheless, the accepted view is that tax benefits do not suffice to transform a private actor into a state actor. See Sugin, *supra* note 22, at 432 n.115 (“*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 also *McCoy v. Schultz*, 73-1 USTC ¶ 9233 (D.D.C. 1973) (“[T]he tax classification of private entities no more transforms that entity into an arm of the government than the grant by a state of a tax exemption to a religious body constitutes state establishment of religion.”). Further, this monumental step by the court was unnecessary for the court’s more reasoned conclusion that tax-exemption and tax deduction may be considered forms of FFA.

178. See *McGlotten*, 338 F. Supp. at 462.

179. See *id.*

180. See *id.*

181. See *id.*

182. See *id.* at 462; see Stanley S. Surrey, *Federal Income Tax Reforms: The Varied Approaches Necessary to Replace Tax Expenditures with Direct Governmental Assistance*, 84 HARV. L. REV. 352, 384 (1970) (“The charitable contribution deduction is a special tax provision not required by, and contrary to, widely accepted definitions of income applicable to the determination of the structure of an income tax.”).

183. See *McGlotten*, 338 F. Supp. at 462.

184. This article’s discussion of congressional intent with respect to tax benefits for charities is somewhat illusory because Congress never expressly *intended* anything with respect to these tax benefits. See, e.g., Evelyn Brody, *Of Sovereignty and Subsidy: Conceptualizing the Charity Tax Exemption*, 23 IOWA J. CORP. L. 585, 590 n.23 (1998) (“[F]ew recorded expres-

enacting a particular tax benefit was to exempt from tax an amount that fits properly within the definition of taxable income,<sup>185</sup> that amount is more likely be treated as FFA.<sup>186</sup> Second, if that same tax benefit is granted on condition that the beneficiary limit its activities to government-specified purposes, a court following *McGlotten* will probably treat the benefit as FFA.<sup>187</sup>

This two-tiered analysis is consistent with the Supreme Court's approach in *Grove City College* that FFA essentially requires that a private entity receive direct or indirect financial benefit from a governmental source.<sup>188</sup> However, in light of *Grove City College*, *McGlotten*'s conclusion that the tax benefit recipient be subject to governmental approval is questionable.<sup>189</sup> In *Grove City College*, the Supreme Court resisted the idea that Title IX was inapplicable without finding inapplicability apparent on the face of the statute.<sup>190</sup> Instead of *McGlotten*'s approach requiring that the tax benefit be en-

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sions exist of legislative intent for enacting a tax benefit for charity.”). According to Professor Brody, one exception to this lack of express congressional intent is in “the legislative history to Congress’s 1938 decision that charity begins at home.” *See id.* (citing H.R. Rep. No. 1860, 75th Cong., 3d Sess. 19 (1938)). In 1938, the House Ways and Means Committee reported:

The bill provides that the deduction . . . be also restricted to contributions made to domestic institutions. The exemption from taxation of money or property devoted to charitable and other purposes is based upon the theory that the Government is compensated for the loss of revenue by its relief from financial burden which would otherwise have to be met by appropriations from public funds, and by the benefits resulting from the promotion of the general welfare.

H.R. Rep. No. 1860, 75th Cong., 3d Sess. 19.

185. The term “taxable income” is a term of art in tax law that refers to those statutorily defined items that are considered when deciding how much income tax is due. *See, e.g.*, I.R.C. § 1(a) (2000) (describing tax liability for married individuals filing jointly as function of “taxable income” and specified tax rates). “Taxable income” generally means the excess of gross income over allowed deductions. *See id.* § 63.

186. *See McGlotten*, 338 F. Supp. at 461. A key aspect of tax expenditure theory is the manner by which tax-base defining tax benefits are distinguished from those tax benefits that do not define the tax base. While some benefits are clearly base-defining and others not, there are many benefits that are subject to multiple interpretations. *See Independent Sector Comments on JCT Disclosure Study For Exempts*, 2000 TNT 54-95 n.1 (2000) (contrasting arguments for treating charitable contributions as subsidies or as essential elements of income tax base); Mary Louise Fellows, *Rocking the Tax Code: A Case Study of Employment-Related Childcare Expenditures*, 10 YALE J.L. & FEMINISM 307 (1998).

187. *See McGlotten*, 338 F. Supp. at 461.

188. *See discussion supra* notes 130-56 and accompanying text.

189. The portion of *McGlotten* that discusses the requirement that a tax benefit must be encapsulated with government approval probably went too far for civil rights statutory purposes. Instead, this type of requirement would likely be more appropriate for determining if a benefit is sufficient to transform a private actor into a state actor for constitutional law purposes. *See discussion supra* note 177.

190. *See Grove City College v. Bell*, 465 U.S. 555, 564 (1984).

meshed with government approval, the Supreme Court would likely only require that Congress expressly intend a specified benefit (like BEOG funds for students) to the particular organization.<sup>191</sup> Coupling the *Grove City College* analysis with the *McGlotten* analysis results in an interpretive framework in which a tax benefit will be treated as FFA if the benefit provides financial assistance to the benefited organization and Congress intended to assist that organization.

b. *Bachman*: *Tax benefits are never FFA*. In contrast, a different federal court examining the issue of whether tax benefits may be treated as FFA concluded that tax benefits can never be FFA because Congress did not intend so.<sup>192</sup> In *Bachman v. American Society of Clinical Pathologists*, a person afflicted with dyslexia sued a tax-exempt medical society (“ASCP”) for failing to comply with section 504 of the Rehabilitation Act of 1973 (“section 504”).<sup>193</sup> The ASCP received no direct federal funding. The plaintiff alleged, in part, that the ASCP medical society was a recipient of FFA for section 504 purposes because of the society’s tax-exempt status. The court’s opinion in *Bachman* does not indicate the Internal Revenue Code provision under which the medical society was exempt.<sup>194</sup> Nevertheless, the court in *Bachman* concluded that Congress did not intend section 504 “to cover tax-exempt institutions absent any further affirmative federal financial assistance.”<sup>195</sup>

In reaching its conclusion that FFA under section 504 does not cover tax exemption, the court in *Bachman* relied on the plain meaning of section 504, the administrative definition of FFA, and interpretations of other statutes similar to section 504.<sup>196</sup> Without much explanation, the court noted that the term “assistance” in FFA means transfer of government money by subsidy, not exemption.<sup>197</sup> The court also noted that the Department of Health Education and Welfare’s administrative regulation defining FFA does not list tax-exemption among the various forms of assistance.<sup>198</sup> Finally, the

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191. *See id.* at 566.

192. *See Bachman v. American Soc’y of Clinical Pathologists*, 577 F. Supp. 1257 (D.N.J. 1983).

193. *See id.* at 1259; Rehabilitation Act of 1973, 29 U.S.C. § 794 (2000).

194. The court in *Bachman* refers to the medical society throughout the opinion as non-profit and tax-exempt. Thus, it is unclear what Internal Revenue Code provision authorized the medical society’s federal tax-exemption.

195. *See Bachman*, 577 F. Supp. at 1264.

196. *See id.* at 1264–65.

197. *See id.* at 1264. Although the court in *Bachman* did cite to cases indicating that “assistance” does not include government contracts, it did not explain how or why government contracts are necessarily the same as tax-exemption. *See id.*

198. *See id.* The Health Education and Welfare Department defined FFA as:

court in *Bachman* evaluated how Title IX was interpreted. The court reasoned that, because courts in cases like *Grove City College* rely on an educational institution's receipt of grants and loans, FFA must not include tax exemption.<sup>199</sup>

The court's narrow interpretation of FFA in *Bachman* is clearly at odds with the broader definition urged by the Supreme Court in *Grove City College v. Bell*,<sup>200</sup> especially where the Supreme Court says:

Nothing in [Title IX] suggests that Congress elevated form over substance by making the application of the nondiscrimination principle dependent on the manner in which a program or activity receives federal assistance. There is no basis in [Title IX] for the view that only institutions that themselves apply for federal aid or receive checks directly from the Federal Government are subject to regulation. As the Court of Appeals observed, "by its all inclusive terminology [Title IX] appears to encompass all forms of federal aid to education, direct or indirect." We have recognized the need to "accord [Title IX] a sweep as broad as its language," and we are reluctant to read into Title IX a limitation not apparent on its face.<sup>201</sup>

The court's definition of FFA in *Bachman* is narrow in that the court refused to extend the definition beyond those particular forms of FFA already recognized in either the statute, regulation, or judicial decisions.<sup>202</sup> In *Grove City College*, the Supreme Court urges against such a narrow view of this important jurisdictional term.<sup>203</sup> In comparison to the grudging interpretation of the *Bachman* court, *McGlotten* took a broad view of the scope of civil rights protections by requiring only that the tax benefit be non-income-defining and

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[A]ny grant, loan, contract (other than a procurement contract or a contract of insurance or guaranty), or any other arrangement by which the Department provides or otherwise makes available assistance in the form of:

- (1) Funds;
- (2) Services of Federal personnel; or
- (3) Real and personal property or any interest in or use of such property, including:
  - (i) Transfers or leases of such property for less than fair market value or for reduced consideration; and
  - (ii) Proceeds from a subsequent transfer or lease of such property if the Federal share of its fair market value is not returned to the Federal Government.

*Id.* (citing 45 C.F.R. § 84.3(h) (1983)).

199. *See id.* at 1264–65.

200. *See* discussion *supra* notes 130–56 and accompanying text.

201. *Grove City College v. Bell*, 465 U.S. 555, 564 (1984).

202. *See Bachman*, 577 F. Supp. at 1264–65.

203. *See Grove City College*, 465 U.S. at 564.

the activities supported by the tax benefit not be government-specified.<sup>204</sup>

*c. Conclusions.* The broader interpretations of FFA in *Grove City College* and *McGlotten* are the preferred method of interpretation in terms of maximizing protections to those persons whose federal civil rights are violated. Under this broader interpretive approach espoused by the Supreme Court and implemented in *McGlotten*, civil rights litigants will spend more time on substantive issues (e.g., deciding whether a defendant's actions are discriminatory) than on nonsubstantive ones (e.g., deciding whether the form of financial benefit is sufficient for coverage purposes).<sup>205</sup> Furthermore, the overarching social justice goal of maximizing human liberty will be enhanced.

However, even in the face of this Supreme Court analysis, the *Bachman* opinion demonstrates that, because the Supreme Court has not ruled that certain tax benefits are equivalent to expenditures of tax revenues, some lower courts will find ways around imposing civil rights restrictions on nontraditional defendants.<sup>206</sup> It is very likely that, if the tax benefit at issue in *Bachman* were provided to the nonprofit ASCP medical society in the form of a grant or loan from the government (as with a typical FFA defendant), the dyslexic plaintiff would have succeeded in her coverage claim.<sup>207</sup> Yet, because the financial benefit to the ASCP in *Bachman* was provided via a tax exemption, the dyslexic plaintiff lost his chance to litigate this potentially viable claim.

There are justifiable reasons for limiting the ability of civil rights plaintiffs to successfully sue potential civil rights defendants.<sup>208</sup> These reasons, however, should be based on the substantive effects of permitting the claim, not on the form in which the defendant receives the financial benefit. As Part IV of this article demonstrates, tax expenditure theory presents an opportunity to utilize substance, not

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204. See discussion *supra* notes 160–87 and accompanying text.

205. Professor Sugin suggests that a strong view of tax expenditure analysis actually limits social justice “by limiting the legal consequences of different tax provisions depending on their categorization as income-defining or not.” See Sugin, *supra* note 22, at 474.

206. See discussion *supra* notes 192–99 and accompanying text. The phrase “non-traditional defendant” is a reference to those civil rights defendants who are not state actors and who do not receive traditional forms of FFA like government loans or grants.

207. *Accord* *Walz v. Tax Comm'n*, 397 U.S. 664, 674 (1970) (indicating that exempting religious property from state property tax does not violate religious clause of First Amendment, although exempting said property and paying the religious owner an amount equivalent to the tax paid would violate First Amendment).

208. For example, the limitation that constitutional civil rights claims be made against state actors only.

form, to determine when a tax benefit is FFA and thus avoid these unjust results.<sup>209</sup>

IV. TAX EXPENDITURE THEORY: *ECONOMIC* EQUIVALENCE V.  
*CONSTITUTIONAL* EQUIVALENCE

A central aspect of this article's thesis involves explaining how a legal concept—the equivalence of tax expenditures and direct expenditures—can be examined on multiple levels. This article uses the example of government funding of religion to illustrate this point. When government chooses to take action that might provide an economic benefit to religion, it has at least two options. On the one hand, government could authorize certain tax benefits that inure to religious organizations. Conversely, government could authorize the disbursement of direct grants to religious organizations. Either of these government options to fund religion may have the same financial or economic impact on religion (*economic* equivalence). Nevertheless, these same government options may be very different constitutionally in that one option may be constitutionally permissible under the First Amendment whereas the other option may be constitutionally impermissible (*constitutional* equivalence).<sup>210</sup> Thus, two government funding options can be the same economically, yet differ constitutionally. As the discussion of the religion cases in this Part develops, the reader should focus on separating the *economic* equivalence question from the *constitutional* equivalence question.

*A. Equivalence as an Essential Element of Tax Expenditure Theory*

Tax expenditure theory essentially provides that the legal effect of certain tax benefits should be analyzed as if the government had provided the recipient of the tax benefit an equivalent grant of

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209. See, e.g., Sugin, *supra* note 22, at 473:

The anti-discrimination approach in equal protection analysis parallels the . . . 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, . . . 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.

210. Furthermore, as demonstrated by the discussion of religion cases in Part IV.B., two different tax benefits for religion may provide the same or similar economic benefits to religion. However, one of these tax benefits may be constitutional and the other may be unconstitutional. See, e.g., discussion *infra* note 255 and accompanying text.

money.<sup>211</sup> For example, if a taxpayer receives a tax deduction for contributing money to a charity, tax expenditure theory would require the law to treat the dollar value of the deduction as equivalent to a grant of money by the government to the taxpayer-donor.<sup>212</sup> Similarly, if a taxpayer is exempt from the requirement to pay federal income tax, tax expenditure theory would mandate that the law treat the dollar value of the exemption as a grant of money by the government to the exempt taxpayer.<sup>213</sup> Pursuant to tax expenditure theory, the equivalency of tax benefits and direct government expenditures applies only to tax benefits enacted to implement social policy—not those intended as a further delineation of the appropri-

211. See STANLEY S. SURREY, *PATHWAYS TO TAX REFORM: THE CONCEPT OF TAX EXPENDITURES* 6–7, 30–49 (1973); STANLEY S. SURREY & PAUL R. MCDANIEL, *TAX EXPENDITURES* 1–30 (1985). See also *Regan v. Taxation With Representation of Wash.*, 461 U.S. 540, 544 (1983) [hereinafter *TWR*] (“Both tax exemptions and tax deductibility are a form of subsidy that are administered through the tax system.”).

212. For direct grant equivalency purposes, the dollar value of a tax deduction is generally computed by multiplying the amount of the tax deduction times the marginal tax rate of the deduction recipient. For example, if for the annual tax year 2000 an individual with \$150,000 of taxable income gave a charity \$10,000 in cash, so that the individual had \$140,000 of taxable income after the contribution, the dollar value of that contribution to the individual contributor is roughly \$10,000 x 31% (or \$3,100). See generally I.R.C. §§ 1, 63, 170(a) (2000). This calculation does not account for the dollar value of the personal exemption phase-out, the overall limitation on itemized deductions, or any state tax benefits that flow from the contribution. See also *TWR*, 461 U.S. at 544 (“Deductible contributions are similar to cash grants of the amount of a portion of the individual’s contributions.”).

213. For example, if for the annual tax year 2000 a corporate taxpayer with \$50,000 of taxable income qualified under § 501(c)(3) of the Code as a tax-exempt charity, the dollar value of the tax exemption to the exempt taxpayer is roughly \$50,000 x 15% (or \$7,500). See generally I.R.C. §§ 11, 501(a), 501(c)(3) (2000). This calculation does not account for the dollar value of any state tax benefits or any other non-tax benefits that flow from charitable status. See also *TWR*, 461 U.S. at 544 (“A tax exemption has much the same effect as a cash grant to the organization of the amount of tax it would have to pay on its income.”). Revocation or denial of charitable status would likely mean loss of many other federal benefits, including (1) the ability to receive tax-deductible contributions from the public, I.R.C. § 170; (2) exemption from the federal unemployment tax, I.R.C. § 3306(c)(8); (3) eligibility for preferred postal rates, 39 C.F.R. § 111.1 (2000); (4) ability to issue tax-exempt bonds, I.R.C. § 145; and (5) ability to provide certain types of tax-deferred retirement plans for employees, I.R.C. § 403(b). The many state benefits that also hinge on an organization maintaining tax-exempt charitable status include exemption from (1) real property taxes; (2) sales and use taxes; (3) business and occupational taxes; (4) state unemployment taxes; and (5) the requirement to pay certain permit or license fees. See generally BRUCE R. HOPKINS, *THE LAW OF TAX-EXEMPT ORGANIZATIONS* § 3.2 (7th ed. 1998); JAMES J. FISHMAN ET AL., *NONPROFIT ORGANIZATIONS: CASES AND MATERIALS*, 314–15 (1995). In fact, some charities obtain federal tax-exempt status merely to obtain these state benefits. See *id.* at 335. “Many nonprofits do not earn a significant net profit or rely on charitable contributions as a major source of their support. State and local tax exemptions may be the most significant governmental benefit for these organizations, especially if they own real property.” *Id.*

ate tax base.<sup>214</sup> Thus, a central element of pure tax expenditure theory is the notion that tax benefits implemented to accomplish social policy and government expenditures implemented for the same purpose are equivalent, both *economically* and *constitutionally*.<sup>215</sup>

This article's view is that *economic* equivalence is very different from *constitutional* equivalence. This view is reflected in the discussion of the religion cases in Part IV.B. This view is also consistent with recent academic commentary questioning the value of tax expenditure theory in judicial decision making for constitutional law purposes.<sup>216</sup> These scholars accept that tax expenditure theory and its economic equivalence concepts are relevant for some purposes.<sup>217</sup> However, the scholars contend that courts should place less emphasis on economic equivalence when making constitutional law decisions and more emphasis on the particular constitutional context. For example, one scholar "calls for a case-by-case determination[] of equivalence by considering the particular constitutional contexts, the specific tax and direct spending programs at issue, and the appropriate perspective in each of those contexts."<sup>218</sup> Another scholar simi-

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214. See SURREY, *supra* note 211, at 6 ("The federal . . . tax system consists. . . of two parts: one part comprises the structural provisions necessary to implement the income tax. . . ; the second part comprises a system of tax expenditures under which . . . financial assistance programs are carried out through special tax provisions rather than through direct Government expenditures."); SURREY & MCDANIEL, *supra* note 211, at 3 ("[A]n income tax is composed of two . . . elements[:] structural provisions necessary to implement the normal income tax, such as the definition of income. . . [and] special preferences . . . [that are]. . . departures from the normative tax structure [and] represent government spending for favored activities . . . effected through the tax system rather than through direct . . . government assistance."); Zelinsky, *supra* note 22, at 381 n.2 ("The . . . premise of [the] theory is that tax provisions [are] divided into 'normative' provisions, which are necessary to implement the theoretical base of the tax, and provisions that are adopted to implement policies extraneous to the tax base. These latter provisions . . . are . . . government[] expenditures; hence the term 'tax expenditures.'"). This aspect of tax expenditure theory, distinguishing so-called structural tax benefit provisions from nonstructural ones, is the source of much controversy. See, e.g., Sugin, *supra* note 22, at 418 ("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.").

215. See Sugin, *supra* note 22, at 410 ("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.").

216. See Zelinsky, *supra* note 22; Sugin, *supra* note 22.

217. See, e.g., Sugin, *supra* note 22, at 408 ("Policymakers and scholars have long recognized that direct spending programs and tax subsidies can be economically equivalent.").

218. See Zelinsky, *supra* note 22, at 382. Professor Zelinsky states that it is inappropriate to make categorical statements, as tax expenditure theorists do, about equivalency without some focus on the particular context. See *id.* Zelinsky explains that, for constitutional equivalency purposes, the terms "tax" and "direct expenditure" are not very helpful. The problem

larly calls for a less strict adherence to the traditional view of tax expenditure theory and instead calls for adoption of a qualified version of tax expenditure theory. This qualified version of the theory, she continues, should “applaud[] the important lessons of tax expenditure analysis for policy making . . . and the analytic prescriptions for legislatures that flow from that equivalence.”<sup>219</sup> She adds that the qualified version also recognizes that a pure “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.”<sup>220</sup>

This Part explains how tax expenditure theory is applied to reach appropriate results in interpreting selected statutes and constitutional provisions. Typically, the Supreme Court addresses the equivalence issue in the constitutional law context.<sup>221</sup> In addition, academic

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with these generic terms, Zelinsky continues, is the “diverse and overlapping nature of different tax laws and direct spending programs, the disparate perspectives from which equivalence can be assessed, and the variety of constitutional contexts in which the equivalence issue must be addressed.” *Id.* at 381. Zelinsky concludes that legal decision makers should compare “particular tax and spending programs case-by-case with appropriate concern for particular constitutional provisions.” *Id.* at 433.

219. *See* Sugin, *supra* note 22, at 412. Professor Sugin, like Professor Zelinsky, rejects tax expenditure theory to the extent it commands that non-base-defining tax benefits should *always* be treated as equivalent to direct expenditures by government. *See id.* At the heart of Sugin’s thesis is her critique of what she calls the strong version of tax expenditure theory, subjecting tax expenditures to “the full panoply of constitutional and statutory restrictions on government spending.” *Id.* at 410. She states that tax expenditure theory “imposes inappropriate restraints on adjudication and improperly reduces judicial scrutiny of provisions that are not classified as tax expenditures.” *Id.* at 412. Sugin continues that tax expenditure theory “gives tax expenditures the same legal consequences as economically equivalent direct-spending programs, even where the legal standard does not depend on economic equivalence.” *Id.* at 412–13. Sugin concludes that tax expenditure analysis is better suited for legislatures and not courts because tax expenditure theory “gives economic equivalence too much normative force and [] courts have only limited use for the tax expenditure budget in legal analysis.” *Id.*

220. *See id.* at 412.

221. *See, e.g.*, *United States v. Virginia*, 518 U.S. 515, 558 (1996) (holding that the Equal Protection Clause of the Fourteenth Amendment requires state military college to admit women into traditionally all-male college); *Rosenberger v. Rector of the Univ. of Va.*, 515 U.S. 819, 828 (1995) (holding that state school student activity fund’s refusal to pay printing costs for student organization that published articles with religious themes was content-based regulation of speech violating First and Fourteenth Amendments); *Walz v. Tax Comm’n*, 397 U.S. 664 (1970) (holding that New York’s property tax exemption for various types of property, including religious property, did not violate First Amendment); *West Lynn Creamery, Inc. v. Healy*, 512 U.S. 186, 194–95 (1994) (holding that Commerce Clause prohibited state from refunding milk tax revenues to residents only); *Camps Newfound/Owatonna, Inc. v. Harrison*, 520 U.S. 564, 595 (1997) (holding that Commerce Clause prohibited state from denying local property tax exemption to nonprofit summer camp that predominantly served nonresidents).

commentary on equivalence has focused almost exclusively on constitutional issues, not statutory ones.<sup>222</sup> Though their ultimate concern is with Constitutional results, these decisions and academic commentary provide useful guidance for deciding the statutory issue of whether tax benefits provided to tax-exempt charities should be treated as FFA under federal civil rights statutes. As the analysis in this Part shows, there is no logical (or legal) reason for treating the tax benefits received by charities as anything other than equivalent to government grants or loans for purposes of interpreting relevant civil rights statutes.

*B. The Supreme Court's Uniform Acceptance of Economic Equivalence in Constitutional Decision Making*

Analysis of the Supreme Court's religion clause cases shows that the Court treats tax benefits as *constitutionally* equivalent to government expenditures by accepting *economic* equivalence as a given. Thus, the Court's religion clause cases broadly support a key component of this article's thesis—tax benefits for charities should be viewed as FFA under federal civil rights statutes. These cases show, by analogy, that it is perfectly plausible to treat tax benefits as legally equivalent to grants, loans, and other forms of FFA. In these cases, tax benefits serve as the economic assistance to religion that triggers serious First Amendment concerns about impermissible aid to religion. If the Court did not view tax benefits as economic assistance to religion, there would be no aid in the first place, and the religion clause would presumably not even be triggered. Taken as a whole then, these religion clause cases strongly support treating tax benefits for charities as a form of FFA because the Court uniformly accepts that tax benefits are a form of economic assistance, even when the justices are otherwise divided on the sensitive issue<sup>223</sup> of *constitutional* equivalence.<sup>224</sup>

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222. See Zelinsky, *supra* note 22 (discussing application of tax expenditure theory in various constitutional contexts); Sugin, *supra* note 22 (discussing application of tax expenditure theory in various constitutional contexts). But see Mary L. Heen, *Reinventing Tax Expenditure Reform: Improving Program Oversight under the Government Performance and Results Act*, 35 WAKE FOREST L. REV. 751 (2000) (discussing incorporation of tax expenditures into the program performance review process established by the Government Performance and Results Act of 1993, Pub. L. No. 103-62, 107 Stat. 285 (1993)).

223. See *Tilton v. Richardson*, 403 U.S. 672, 678 (1971) (“[C]andor compels the acknowledgment that we can only dimly perceive the boundaries of permissible government activity in this sensitive area.”).

224. This article does not intend to stretch the analogy of these cases much beyond this point. Once it is accepted that the tax benefit at issue is a form of economic assistance to relig-

### I. *Walz v. Tax Commission*

In the context of the First Amendment's religion clause cases, *Walz v. Tax Commission*<sup>225</sup> is the oldest case in which the Supreme Court closely examined the issue of the equivalence of tax benefits and direct expenditures.<sup>226</sup> *Walz* involved a suit by a real property owner seeking to enjoin the New York City Tax Commission from granting property tax exemptions to religious organizations that used their property exclusively for religious purposes.<sup>227</sup> The property owner complained that the tax exemption "indirectly require[d him] to make a contribution to religious bodies and thereby violate[d] provisions prohibiting establishment of religion under the First

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ion, from that point the decisions turn most on whether the particular type of assistance violates the neutrality norms that animate religion clause jurisprudence. *See, e.g., Walz*, 397 U.S. at 674–75. On this point, the Supreme Court has said:

Granting tax exemptions to churches necessarily operates to afford an indirect economic benefit and also gives rise to some, but yet a lesser, involvement than taxing them. In analyzing either alternative the questions are whether the involvement is excessive, and whether it is a continuing one calling for official and continuing surveillance leading to an impermissible degree of entanglement. Obviously a direct money subsidy would be a relationship pregnant with involvement and, as with most governmental grant programs, could encompass sustained and detailed administrative relationships for enforcement of statutory or administrative standards, but that is not this case.

*Id.* Thus, the focus in these religion cases—on whether the tax benefit increases or decreases government involvement with religion—is a step beyond the focus in civil rights cases involving the existence of FFA.

As with its First Amendment religion clause cases, the Supreme Court would also likely require, at a minimum, a transfer of economic assistance when evaluating the equivalence issue for Fourteenth Amendment Equal Protection Clause purposes. A recent case decided by the Supreme Court brings this issue to the forefront. *VMI*, 518 U.S. 515 (1996). Even though *VMI* did not directly involve a tax/expenditure equivalence issue, it is clear that the case has serious implications for tax expenditure theorists. *See Zelinsky, supra* note 22; *Sugin, supra* note 22.

225. *Walz*, 397 U.S. at 664.

226. Other cases include *Committee for Pub. Educ. & Religious Liberty v. Nyquist*, 413 U.S. 756 (1973); *Mueller v. Allen*, 463 U.S. 388 (1983); and *Texas Monthly, Inc. v. Bullock*, 489 U.S. 1 (1989).

227. *Walz*, 397 U.S. at 666. New York's property tax exemption law provided in relevant part that

[r]eal property owned by a corporation or association organized exclusively for the moral or mental improvement of men and women, or for religious, bible, tract, charitable, benevolent, missionary, hospital, infirmary, educational, public playground, scientific, literary, bar association, medical society, library, patriotic, historical or cemetery purposes . . . and used exclusively for carrying out thereupon one or more of such purposes . . . shall be exempt from taxation as provided in this section.

*Id.* at 667 n.1 (quoting from section 420, paragraph 1, of the New York Real Property Tax Law).

Amendment . . . .”<sup>228</sup> The United States Supreme Court disagreed with the property owner’s conclusion that the exemption amounted to establishment of religion and, accordingly, upheld the property tax exemption law.<sup>229</sup>

While acknowledging that the tax benefit for religion—here a property tax exemption—clearly aided religion in some manner, the Court closely scrutinized the exemption to determine if this admitted financial support of religion exceeded constitutional limits. Chief Justice Burger, for the six justice majority, stated that “the ‘establishment’ of a religion connote[s] sponsorship, financial support, *and* active involvement of the sovereign in religious activity.”<sup>230</sup> Burger continued that the basic objective of the Establishment clause and the Free Exercise clause “is to insure that no religion be sponsored or favored, none commanded, and none inhibited.”<sup>231</sup> Thus, “[s]hort of th[ese] expressly proscribed governmental acts there is room for play in the joints productive of a benevolent neutrality which will permit religious exercise to exist without sponsorship and without interference.”<sup>232</sup> According to Chief Justice Burger, the key lies not in merely determining whether a government act “aids” religion but in determining “whether the particular acts in question are intended to establish or interfere with religious beliefs and practices or have the effect of doing so.”<sup>233</sup>

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228. *Id.* at 667. The relevant portions of the First Amendment to the United States Constitution provide that “Congress shall make no law respecting an establishment of religion, or prohibiting the free exercise thereof . . . .” U.S. CONST. amend. I.

229. *See Walz*, 397 U.S. at 667.

230. *Id.* at 668 (emphasis added).

231. *Id.* at 669.

232. *Id.*

233. *Id.* at 670–71. The majority in *Walz* determined that New York’s legislative purpose for the property tax exemption was neither advancement nor inhibition of religion. Rather, the purpose of the exemption was that property taxes should not inhibit the activities of “certain entities that exist in a harmonious relationship to the community at large, and that foster its ‘moral or mental improvement.’” *Id.* at 672. Included amongst these general types of entities were all houses of religious worship, hospitals, libraries, playgrounds, scientific, professional, historical, and patriotic groups. *See id.* at 673. In addition to determining that the legislative purpose of the New York property tax was not to establish, sponsor, or support religion, the Court in *Walz* concluded that the effect of the property tax exemption was not an excessive government entanglement with religion. *See id.* at 674. While either exempting religious property from tax or imposing a tax on religious property necessarily involves some degree of entanglement, the majority in *Walz* concluded that taxing religion “would tend to expand the involvement of government.” *Id.* Indeed, taxing religion, according to the Court, might give rise to valuation concerns, tax liens, tax foreclosures, and the direct confrontations and conflicts that follow. *See id.* Thus, while “[g]ranting tax exemptions to churches necessarily operates to afford an indirect economic benefit,” it “also gives rise to some, but yet a lesser, involvement than taxing them.” *Id.* at 674–75.

On the issue of constitutional equivalence of this tax benefit to a hypothetical direct expenditure, the Court majority in *Walz* clearly discerned a difference of constitutional significance but never denied that the tax benefit was a financial subsidy for religion. While a “direct money subsidy would be a relationship pregnant with involvement and, as with most governmental grant programs, could encompass sustained and detailed administrative relationships for enforcement of statutory or administrative standards,” a tax benefit subsidy does not share this quality.<sup>234</sup> The majority contended that granting a tax exemption is not sponsorship because the government does not transfer part of its revenue to churches. Instead, it simply does not require or demand that churches support the state.<sup>235</sup>

In their concurring and dissenting opinions, Justices Brennan, Harlan, and Douglas similarly acknowledged that the tax benefit to religion in *Walz* is indeed a form of financial aide to religion. Justice Brennan, in his concurrence, concluded that the tax exemption for religion was not constitutionally equivalent to a direct subsidy to religion.<sup>236</sup> In Justice Brennan’s view, tax exemptions and direct subsidies are very different for constitutional law purposes because of the differing levels of entanglement. So different in fact that a direct subsidy would be clearly unconstitutional,<sup>237</sup> whereas an indirect subsidy by way of tax exemption is completely permissible.<sup>238</sup> In his concurrence, Justice Harlan also discerned a constitutionally significant difference between tax exemptions and direct subsidies.<sup>239</sup> Justice

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234. *See id.* at 675.

235. *See id.* The majority also noted that “[n]o one has ever suggested that tax exemption has converted libraries, art galleries, or hospitals into arms of the state or put its employees ‘on the public payroll.’” *Id.*

236. *See id.* at 680–94 (Brennan, J., concurring).

237. *See id.* at 690 (“General subsidies of religious activities would, of course, constitute impermissible state involvement with religion.”).

238. *See id.* at 691 (“Tax exemptions . . . constitute mere passive state involvement with religion and not the affirmative involvement characteristic of outright governmental subsidy.”).

239. *See id.* at 694–700 (Harlan, J., concurring in the judgment). However, Justice Harlan focused on a procedural difference between tax exemptions and direct subsidies that resulted in subsidies inviting more political controversy (and hence more government involvement) than tax exemptions. *See id.* at 699 (“Subsidies, unlike exemptions, must be passed on periodically and thus invite more political controversy than exemptions. Moreover, subsidies or direct aid, as a general rule, are granted on the basis of enumerated and more complicated qualifications and frequently involve the state in administration to a higher degree, though to be sure, this is not necessarily the case.”). Justice Harlan specifically refused to recognize any substantive or economic distinction. *See id.* (“I agree with my Brother DOUGLAS that exemptions do not differ from subsidies as an economic matter.”). Unlike the rest of the majority, Justice Harlan also refused to draw the necessary conclusion that a direct subsidy to churches would necessarily violate the First Amendment. *See id.* Justice Harlan writes:

Douglas, for the dissent, saw tax exemptions and tax subsidies as constitutionally equivalent, viewing the tax exemption as “financial support” for religion.<sup>240</sup> In evaluating the majority’s uniform conclusion that tax exemptions might or should be treated as anything but direct subsidies, Justice Douglas questioned the meaning of the majority’s analysis.<sup>241</sup> Nevertheless, Douglas, like the Burger majority, the Brennan concurrence, and the Harlan concurrence, never questioned whether the tax exemption was a financial aide to religion.

In sum, the form of the admitted benefit to religion—a tax exemption benefit instead of a direct grant or other expenditure—significantly influenced the Court’s conclusion regarding the constitutionality of New York’s property tax exemption law. The majority and concurring opinions give every indication that, had New York law required religious organizations and the like to pay property taxes and apply to the state for a subsequent refund, the Court would probably have concluded that the law violated the First Amendment. However, because the financial benefit to religion was by way of tax exemption—even though economically equivalent to a direct grant to religion—the Court upheld New York’s tax exemption law as constitutionally permissible since it was the best way to avoid excessive government entanglement with religion. Importantly, there was no issue raised by either the majority or the dissent about whether the tax benefit, here a property tax exemption, was a form of financial assistance to religion.

## 2. *Committee for Public Education and Religious Liberty v. Nyquist*

Another First Amendment religion case in which the Supreme Court addressed the issue of the equivalence of tax benefits and direct expenditures was *Committee for Public Education and Religious*

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Whether direct aid or subsidies entail that degree of involvement that is prohibited by the Constitution is a question that must be reserved for a later case upon a record that fully develops all the pertinent considerations such as the significance and character of subsidies in our political system and the role of the government in administering the subsidy in relation to the particular program aided. It may also be that the States, while bound to observe strict neutrality, should be freer to experiment with involvement—on a neutral basis—than the Federal Government.

*Id.* (footnotes omitted).

240. *Id.* at 704 (Douglas, J., dissenting).

241. *See id.* “A tax exemption is a subsidy. Is my Brother Brennan correct in saying that we would hold that state or federal grants to churches, say, to construct the edifice itself would be unconstitutional? What is the difference between that kind of subsidy and the present subsidy?” *Id.*

*Liberty v. Nyquist*.<sup>242</sup> Contrary to *Walz* where the Court concluded that granting a property tax exemption avoided excessive government entanglement with religion, the Court in *Nyquist* concluded that the income tax benefits offered to parents of school age children increased government entanglement with religion. However, consistent with this article's thesis, none of the Justices in *Nyquist* questioned whether the tax benefits were financial assistance to religion, only whether the degree of assistance was excessive.<sup>243</sup>

In *Nyquist*, an unincorporated association and several individual taxpayers raised Establishment Clause challenges to certain New York laws establishing financial aid programs for private grade schools in the state.<sup>244</sup> The programs included direct grants to private schools,<sup>245</sup> tuition reimbursements to low-income parents paying private school tuition,<sup>246</sup> and income tax benefits for other parents paying private school tuition.<sup>247</sup> The legislative purpose for the amendments was to satisfy the state's "responsibility to ensure the health, welfare and safety of [private school] children" and to "express[] a dedication to the 'vitality of our pluralistic society.'"<sup>248</sup> A substantial majority of the schools benefiting from the various programs were religious.<sup>249</sup> A federal district court invalidated the direct grant and

242. *Committee for Pub. Educ. & Religious Liberty v. Nyquist*, 413 U.S. 756 (1973).

243. Interestingly, the seminal case that defines the phrase "receiving federal financial assistance" as used in federal civil rights statutes also relies on the principal of economic equivalence established in *Nyquist*, *Mueller*, and similar religion clause cases. *See Grove City College v. Bell*, 465 U.S. 555 (1984). Citing *Mueller* and *Nyquist*, the Court in *Grove City College* states that "[t]he economic effect of direct and indirect assistance often is indistinguishable . . ." *Id.* at 565.

244. *See Nyquist*, 413 U.S. at 761–62.

245. The direct grants provisions provided for direct money grants from the State to "qualifying" private schools to be used for appropriate maintenance and repair purposes to ensure the health welfare and safety of private school students. *See id.* at 762. "A 'qualifying' school is any nonpublic nonprofit elementary or secondary school which has been designated during the [immediately preceding] year as serving a high concentration of pupils from low-income families for purposes of Title IV of the Federal Higher Education Act of nineteen hundred sixty-five . . ." *Id.* at 762–63 (citing 20 U.S.C. § 425).

246. The tuition reimbursements provision provided for tuition reimbursements to parents of children attending private grade schools if the parents had an annual taxable income of less than \$5,000. *See id.* at 764.

247. The income tax benefits provision provided tax relief to parents who failed to qualify for tuition reimbursement by permitting these parents to subtract from their adjusted gross income for state income tax purposes a designated amount for each dependent for whom they paid private school tuition. *See id.* at 765. Thus, the tax benefit provision was not a traditional type of tax deduction because the deductible amount was a function of a statutory amount, not the amount actually expended by the taxpayer. *See id.* at 790.

248. *Id.* at 763–65.

249. The Court notes that "[s]ome 700,000 to 800,000 students, constituting almost

tuition reimbursement portions of the amendments as violating the Establishment Clause of the First Amendment but upheld the income tax benefits provisions.<sup>250</sup>

On appeal, the United States Supreme Court invalidated all three portions of the amendments, refusing to insulate the tax benefits provisions from the same scrutiny shared by the other cash expenditure provisions.<sup>251</sup> As a testament to the economic equivalence of tax benefits and direct financial assistance, Justice Powell, for the majority, found little substantive difference between the tax benefits provision and the tuition reimbursements provision invalidated by the lower court.<sup>252</sup> Both provisions, according to Powell, were intended to be comparable and compatible such that all parents of children attending private grade schools would receive roughly equal amounts as a benefit, either in the form of a reimbursement or as reduction in tax liability.<sup>253</sup> Thus, for Justice Powell, there was no practical reason to distinguish one form of aid to religion (tuition reimbursements)

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20% of the State's entire elementary and secondary school population, attend over 2,000 non-public schools, approximately 85% of which are church affiliated." *Id.* at 768.

250. *Committee for Pub. Educ. & Religious Liberty v. Nyquist*, 350 F. Supp. 655 (S.D.N.Y. 1972).

251. *Committee for Pub. Educ. & Religious Liberty v. Nyquist*, 413 U.S. 756, 769 (1973).

252. However, Justice Powell did note that labeling the tax benefits as credits or deductions was helpful but not decisive:

In this Court, the parties have engaged in a considerable debate over what label best fits the New York law. Appellants insist that the law is, in effect, one establishing a system of tax "*credits*." The State and the intervenors reject that characterization and would label it, instead, a system of income tax "*modifications*." The Solicitor General, in an *amicus curiae* brief filed in this Court, has referred throughout to the New York law as one authorizing tax "*deductions*." The District Court majority found that the aid was "*in effect a tax credit*." . . . We see no reason to select one label over another, as the constitutionality of this hybrid benefit does not turn in any event on the label we accord it . . . Instead we must "*examine the form of the relationship for the light that it casts on the substance*."

*Id.* at 789–90 (quoting *Committee for Pub. Educ. & Religious Liberty v. Nyquist*, 350 F. Supp. 655, 672 (S.D.N.Y. 1972) (emphasis in original)).

253. *See id.* at 790. The court stated:

These sections allow parents of children attending nonpublic elementary and secondary schools to subtract from adjusted gross income a specified amount if they do not receive a tuition reimbursement . . . and if they have an adjusted gross income of less than \$25,000. The amount of the deduction is . . . calculated on the basis of a formula contained in the statute. The formula is apparently the product of a legislative attempt to assure that each family would receive a carefully estimated net benefit, and that the tax benefit would be comparable to, and compatible with, the tuition grant for lower income families.

*Id.*

from another (tax deductions, credits, etc.). In both cases, “the money involved represents a charge made upon the state for the purpose of religious education.”<sup>254</sup> Once economic equivalency was established, Powell went on to explain why the tax benefits in *Nyquist* were excessive for First Amendment purposes whereas the tax benefits in *Walz* were consistent with notions of government religious neutrality.<sup>255</sup>

### 3. *Mueller v. Allen*

In *Mueller v. Allen*, the Supreme Court again espouses the view that tax benefits are economically equivalent to direct expenditures, though not constitutionally equivalent.<sup>256</sup> In *Mueller*, a group of Minnesota taxpayers challenged the constitutionality of a Minnesota statute that permitted taxpayers to take a deduction on their state income taxes for certain tuition and transportation expenses incurred in educating their children.<sup>257</sup> The taxpayers claimed the statute vio-

254. *Id.* at 790–91 (quoting *Committee for Pub. Educ. & Religious Liberty v. Nyquist*, 350 F. Supp. 655, 675 (S.D.N.Y. 1972) (Hayes, J., dissenting)).

255. In distinguishing the tax exemptions approved in *Walz* from the tax benefits at issue in *Nyquist*, Justice Powell emphasized the historical roots of the property tax exemptions as compared to the lack of historical support for the tax benefits in *Nyquist*. *See id.* at 792 (“We know of no historical precedent for New York’s recently promulgated tax relief program.”). Further, while the tax exemption in *Walz*, according to Justice Powell, “constitute[d] a reasonable and balanced attempt to guard against” the dangers of taxing religion, the special tax benefits in *Nyquist* “cannot be squared with the principle of neutrality.” *Id.* at 793 (quoting *Walz v. Tax Comm’n*, 397 U.S. 664, 673 (1970)). Thus, if the tax exemption in *Walz* were eliminated, the involvement of government in religion would be expanded “by giving rise to tax valuation of church property, tax liens, tax foreclosures, and the direct confrontations and conflicts that follow in the train of those legal processes.” *Id.* (quoting *Walz*, 397 U.S. at 674). However, the granting of the special tax benefits in *Nyquist* tended to increase the involvement between religion and government by mandating certain actions of religion and government that would not otherwise have to be taken. *See id.* Finally, the tax exemption in *Walz* was available to a broad class of potential beneficiaries, whereas the tax benefits in *Nyquist* were utilized primarily by parents of private religious school students. *See id.* at 793–94.

256. *See Mueller v. Allen*, 463 U.S. 388 (1983).

257. *See id.* at 390–91. Minnesota’s law permitted taxpayers to deduct the following as tuition and transportation expenses:

The amount . . . paid to others . . . for each dependent [in grade school], for tuition, textbooks and transportation of each dependent in attending [a grade school] situated in Minnesota, North Dakota, South Dakota, Iowa, or Wisconsin, wherein a resident of this state may legally fulfill the state’s compulsory attendance laws, which is not operated for profit, and which adheres to the provisions of the Civil Rights Act of 1964 and chapter 363. As used in this subdivision, ‘textbooks’ shall mean and include books and other instructional materials and equipment used in elementary and secondary schools in teaching only those subjects legally and commonly taught in public elementary and secondary schools in this state and shall not include in-

lated the Establishment Clause by providing financial assistance to religious schools.<sup>258</sup> The Commissioner of Minnesota's Department of Revenue agreed, among other things, that substantially all of the private schools in Minnesota at which the deductible expenses were incurred considered themselves religious.<sup>259</sup> The district court and the court of appeals disagreed with the taxpayers and determined that Minnesota's tax deduction statute was neutral with respect to either establishing or inhibiting religion.<sup>260</sup> The Supreme Court agreed with the lower courts and upheld the statute.<sup>261</sup>

The majority in *Mueller* concluded that Minnesota's tax deduction was not *constitutionally* equivalent to a direct government expenditure because the deduction did not have "the primary effect of advancing the sectarian aims of the nonpublic schools."<sup>262</sup> Nevertheless, the Court never questioned the *economic* equivalence of those

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structional books and materials used in the teaching of religious tenets, doctrines or worship, the purpose of which is to inculcate such tenets, doctrines or worship . . . .  
*Id.* at 390 n.1 (citing MINN. STAT. § 290.09 (1982)).

258. *See id.* at 392.

259. *See id.* at 391 ("[A]pproximately 91,000 elementary and secondary students attended some 500 privately supported schools located in Minnesota, and about 95% of these students attended schools considering themselves to be sectarian.").

260. The District Court held that Minnesota's tax deduction statute was "neutral on its face and in its application and does not have a primary effect of either advancing or inhibiting religion." *Id.* at 392 (quoting *Mueller v. Allen*, 514 F. Supp. 998, 1003 (D. Minn. 1981)). The Court of Appeals likewise upheld the statute, concluding that it benefited a "broad class of Minnesota citizens." *Id.* (quoting *Mueller v. Allen*, 676 F.2d 1195, 1205 (8th Cir. 1982)).

261. *See id.* at 391.

262. *Id.* at 396 (quoting *Committee for Public Educ. v. Regan*, 444 U.S. 646, 662 (1980) and *Lemon v. Kurtzman*, 403 U.S. 602, 612–13 (1971)). Justice Rehnquist noted that the tax deduction in *Mueller* was one among many tax deductions available to citizens of Minnesota. Unlike the tax benefits for middle-income taxpayers in *Nyquist*, which tried to approximate the reimbursements to low-income tax payers, Justice Rehnquist pointed out that the "genuine" tax deduction available under Minnesota's tax law reflected the legislature's attempt to achieve "an equitable distribution of the tax burden." *See Mueller*, 463 U.S. at 396 (citing *Madden v. Kentucky*, 309 U.S. 83, 88 (1940)). *Cf.* *Committee for Pub. Educ. & Religious Liberty v. Nyquist*, 413 U.S. 756, 769 (1973) ("The amount of the deduction is unrelated to the amount of money actually expended by any parent on tuition, but is calculated on the basis of a formula contained in the statute. The formula is apparently the product of a legislative attempt to assure that each family would receive a carefully estimated net benefit, and that the tax benefit would be comparable to, and compatible with, the tuition grant for lower income families."). Justice Rehnquist also noted that, unlike the tax benefits in *Nyquist*, the Minnesota education expense tax deduction was available to "all parents, including those whose children attend[ed] public schools and those whose children attend[ed] nonsectarian private schools or sectarian private schools." *Mueller*, 463 U.S. at 397. Additionally, the fact that Minnesota's tax deduction was available to parents—who independently chose whether to send their children to a religious school or not—greatly reduced any potential Establishment Clause objections. *See id.* at 399.

tax deduction benefits to direct expenditures. Indeed, when Justice Marshall in his dissent criticizes the majority's holding, he does so not because the majority failed to find that Minnesota's tax deduction was an economic benefit to religious schools.<sup>263</sup> Rather, Marshall criticizes the majority for failing to abide by the Court's precedent in *Nyquist* that forbids *any* financial benefit—direct or indirect, tax or non-tax—that subsidizes tuition payments to sectarian schools because such benefits have “a direct and immediate effect of advancing religion.”<sup>264</sup> In Marshall's view, there is no difference between a direct government payment and a tax benefit “[for] the purposes of determining whether such aid has the effect of advancing religion.”<sup>265</sup> What matters, according to Marshall, is whether the substantive impact of the benefit is to aid or advance religion.<sup>266</sup>

#### 4. *Texas Monthly, Inc. v. Bullock*

In *Texas Monthly, Inc. v. Bullock*, the Court again relies on the *economic* equivalence of tax benefits and direct expenditures as a basis for engaging in an analysis regarding *constitutional* equivalence.<sup>267</sup> *Texas Monthly* involved the Supreme Court's review of a Texas sales

263. *See id.* at 404–17 (Marshall, J., dissenting).

264. *Id.* at 405.

265. *Id.* at 407 (citing *Nyquist*, 493 U.S. at 790–91).

266. *See id.* at 408 (citing *Nyquist*, 493 U.S. at 793). Justice Marshall dismissed the majority's attempts to distinguish *Nyquist* on the grounds that Minnesota's tax deduction was available to all parents and New York's tax benefit was limited to private school parents. The practical result in both cases is that the government offsets tuition—the largest expense in both states. *See id.* at 408–09 (“The statute is little more than a subsidy of tuition masquerading as a subsidy of general educational expenses. The other deductible expenses are de minimis in comparison to tuition expenses.”). The tuition offsets families who are more religious. *See id.* at 409 (“Of the total number of taxpayers who are eligible for the tuition deduction, approximately 96% send their children to religious schools.”). And for those families with children in private schools. *Id.* at 409 (“Fewer than 100 of more than 900,000 school-age children in Minnesota attend public schools that charge a general tuition.”). Justice Marshall also dismissed the majority's characterization of Minnesota's law as a “genuine tax deduction” as compared to New York's “special tax benefit.” Marshall viewed the majority's argument on this point as a “distinction without a difference” because the financial impact of both tax benefits on religion is the same. *Id.* at 411–12. Justice Marshall states:

Like the tax benefit held impermissible in *Nyquist*, the tax deduction at issue here concededly was designed to “[encourage] desirable expenditures for educational purposes.” Of equal importance, as the majority also concedes, the “economic [consequence]” of these programs is the same, for in each case the “financial assistance” provided to parents ultimately has an economic effect comparable to that of aid given directly to the schools.

*Id.* at 412 (quoting *Nyquist*, 493 U.S. at 396, 397 n.6, 399).

267. *See Texas Monthly, Inc. v. Bullock*, 489 U.S. 1 (1989).

tax exemption applying exclusively to religious periodicals published or distributed by a religious faith.<sup>268</sup> No similar exemption existed for nonreligious publishers and distributors.<sup>269</sup> A nonreligious publisher in Texas challenged the constitutionality of the special sales tax exemption for religious publishers, claiming that it violated the First Amendment.<sup>270</sup> Texas's appellate court upheld the religious exemption statute, claiming that it served a secular purpose, did not advance religion, and did not result in excessive entanglement of religion with government.<sup>271</sup> On appeal, the United States Supreme Court, in a plurality opinion, reversed the state court's ruling and invalidated the religious exemption statute on First Amendment grounds.<sup>272</sup>

As in its previous First Amendment cases addressing tax benefits for religion, the Court in *Texas Monthly* uniformly accepted that tax benefits are economically equivalent to direct government expenditures. Justice Brennan, for the plurality, noted that every tax benefit is a subsidy of sorts that forces non-benefited taxpayers to become "indirect and vicarious 'donors'" to those benefited.<sup>273</sup> Similarly, Justice Scalia, for the dissent, notes that "a sales tax exemption aids re-

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268. *See id.* at 5. "Texas exempted from its sales tax '[p]eriodicals that are published or distributed by a religious faith and that consist wholly of writings promulgating the teaching of the faith and books that consist wholly of writings sacred to a religious faith.'" *Id.* (quoting TEX. TAX CODE ANN. § 151.312 (1982)).

269. *See id.*

270. *See id.* at 6 ("[A]ppellant paid sales taxes of \$ 149,107.74 under protest and sued to recover those payments in state court.")

271. *See id.* at 6-7 (citing *Texas Monthly, Inc. v. Bullock*, 731 S.W.2d 160 (1987)).

272. *See id.* at 7. Justice Brennan, for the plurality, concluded that Texas' sales tax exemption for religious periodicals lacked "sufficient breadth to pass scrutiny under the Establishment Clause." *Id.* at 14. Unlike the broad state property tax exemptions approved in *Walz v. Tax Commission*, which applied to a variety of religious and secular entities, Justice Brennan noted in *Texas Monthly* that Texas' sales tax exemption only applied to religious entities doing religious works. *See id.* at 12. In distinguishing *Walz*, Justice Brennan states:

Finally, we emphasized in *Walz* that in granting a property tax deduction, the State "has not singled out one particular church or religious group or even churches as such; rather, it has granted exemption to all houses of religious worship within a broad class of property owned by nonprofit, quasipublic corporations which include hospitals, libraries, play-grounds, scientific, professional, historical, and patriotic groups." The breadth of New York's property tax exemption was essential to our holding that it was "not aimed at establishing, sponsoring, or supporting religion," but rather possessed the legitimate secular purpose and effect of contributing to the community's moral and intellectual diversity and encouraging private groups to undertake projects that advanced the community's well-being and that would otherwise have to be funded by tax revenues or left undone.

*Id.* (quoting *Walz v. Tax Comm'n*, 397 U.S. 664, 673-74 (1970) (footnote omitted)).

273. *Id.* (citing *Bob Jones Univ. v. United States*, 461 U.S. 574, 591 (1983)).

ligion, since it makes it less costly for religions to disseminate their beliefs.”<sup>274</sup> In *Texas Monthly*, agreement that the tax benefits economically benefit religion is where common ground among the justices ended. According to the plurality, if the tax benefit subsidy is conferred on a wide variety of religious and nonreligious groups for a proper secular purpose, the fact that religion incidentally benefits “does not deprive the subsidy of the secular purpose and primary effect mandated by the Establishment Clause.”<sup>275</sup> According to Justice Scalia, a significant constitutional difference between otherwise economically equivalent tax benefits and direct benefits is the level of state involvement with religion.<sup>276</sup>

Does the “excessive state involvement with religion” issue raised in *Walz*, *Nyquist*, *Mueller*, and *Texas Monthly*, which is extremely important for First Amendment constitutional law purposes, matter for purposes of determining if a private actor is a recipient of FFA under federal civil rights statutes? No. Under the *Grove City College* conception of FFA, the important thing for civil rights statutory purposes is that the private entity receive direct or indirect financial benefit from a government source and that Congress intends to benefit the private entity. In its religion clause cases, the Court is trying to be neutral towards religion by balancing religious liberty with government endorsement of particular religions.<sup>277</sup> In contrast, in the civil rights statutory context, the Court is primarily concerned with remaining true to Congress’s express desires regarding which governmental programs constitute FFA and are, thereby, covered by the relevant civil rights statute. Once it is determined that an economic benefit is transferred from government to a private entity for

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274. *Id.* at 42.

275. *Id.* at 15. According to Justice Brennan, when government voluntarily grants a subsidy exclusively to religion, as Texas did, it “provide[s] unjustifiable awards of assistance to religious organizations.” *Id.* at 15 (citing *Corporation of Presiding Bishop of Church of Jesus Christ of Latter-day Saints v. Amos*, 483 U.S. 327, 348 (1987) (O’Connor, J., concurring in judgment))—especially where the subsidy is targeted at “writings that promulgate the teachings of religious faiths.” *Id.* at 15. Thus, Justice Brennan concluded that “because Texas’ sales tax exemption for periodicals promulgating the teaching of any religious sect lacks a secular objective that would justify this preference along with similar benefits for nonreligious publications or groups,” the exemption violates the Establishment Clause. *Id.* at 17. Justice Brennan did not address the Free Press issue because his resolution of the Establishment Clause issue resolved the case. *See id.* at 17 n.7.

276. *See id.* at 43.

277. *See Mitchell v. Helms*, 530 U.S. 793 (2000) (“In distinguishing between indoctrination that is attributable to the State and indoctrination that is not, we have consistently turned to the principle of neutrality, upholding aid that is offered to a broad range of groups or persons without regard to their religion.”).

non-income-defining purposes, the only remaining issue is whether Congress intended to provide such a benefit. True, the Court “has been reticent to adopt tax expenditure analysis for constitutional decision-making [sic]”<sup>278</sup> and “has equivocated”<sup>279</sup> on the issue of constitutional equivalence.<sup>280</sup> However, the justices would likely uniformly accept that tax benefits are economically equivalent to other forms of government funding under federal civil rights statutes.<sup>281</sup>

*C. Limitations of the Equivalence Concept Espoused by Tax Expenditure Theory*

In sum, the various Supreme Court justices, like many scholars, agree that the equivalence concept espoused by tax expenditure theory has its limits in the constitutional context. Due to concerns at issue in constitutional cases, tax expenditure theory’s equivalence concept may or may not be helpful to a court deciding how to treat tax benefits for constitutional law purposes. For example, a finding of excessive government involvement with religion is critical to concluding that government funding violates the First Amendment. However, excessive government involvement is not a serious concern under federal civil rights statutes. Maybe the scholars’ calls for less strict adherence to tax expenditure theory in constitutional cases is appropriate? This article is not intended to resolve that issue. Rather, this article simply intends to show that economic equivalence for purposes of interpreting federal civil rights statutes is quite different from constitutional equivalence. State involvement is not significant for purposes of defining FFA in the statutory civil rights context. For purposes of appropriately interpreting federal civil rights statutes, what matters is whether the government has provided financial benefit to a private party and whether Congress intended that the financial benefit support the private party’s activities. If so, the relevant statute, for example Title IX, applies, and the private individual is entitled to have her liberties protected. In short, tax expenditure theory

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278. See Sugin, *supra* note 22, at 411 n.20 (“The 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.”).

279. See Zelinsky, *supra* note 22, at 380–81 (“The Court itself has equivocated, equating tax benefits and direct spending in some constitutional cases but not in others without indicating a rationale for such a seemingly inconsistent approach.”).

280. See TWR, 461 U.S. 540, 544 n.5 (1983) (“In stating that exemptions and deductions, on the one hand, are like cash subsidies, on the other, we of course do not mean to assert that they are in *all respects* identical.” (citations omitted) (emphasis added)).

281. See discussion *supra* note 243.

can and should be used to equate tax benefits received by charities with government grants and loans received by various private parties.

#### V. DISTINGUISHING TAX BENEFITS FOR CHARITIES FROM TAX BENEFITS FOR NON-CHARITIES AND INDIVIDUALS

Treating tax benefits for charities as FFA can and should be done. However, one potential problem might arise that must be addressed in the future: how to explain why noncharity and individual recipients of tax benefits should not also be treated as recipients of FFA under federal civil rights statutes.

Tax benefits include more than those tax benefits that are the subject of this article (e.g., the income tax exemption for charities<sup>282</sup> and income tax deductions for persons making contributions to charities).<sup>283</sup> Other types of tax benefits include income tax exemptions for noncharitable entities,<sup>284</sup> income tax deductions for payments other than to charities,<sup>285</sup> income tax credits,<sup>286</sup> and a variety of tax benefits offered by state and local governments.<sup>287</sup> These other tax benefits, like the tax benefits enjoyed exclusively by charities, also provide an economic benefit to their recipients who include individuals and organizations alike. Thus, one might ask: "Should these other tax benefits also be treated as FFA under appropriate federal civil rights statutes?" Could treating these other tax benefits as FFA mean, for example, that individuals receiving home interest tax deductions, business leagues receiving federal income tax exemptions, and individuals receiving various federal income tax credits would be subject to restrictions imposed by civil rights statutes that apply to recipients of FFA?

The analysis in this article is not intended to apply to tax benefits for noncharities or individuals. Although noncharity and individual tax benefits provide economic favor to their recipients, the concern here is whether Congress intended this economic benefit to subject these recipients to coverage under federal civil rights statutes. Unlike

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282. See I.R.C. § 501(a) (2000).

283. See *id.* § 170(a)(1).

284. These include (among others): social welfare organizations, labor organizations, business leagues, social clubs, fraternal beneficiary societies, domestic fraternal societies, non-profit cemetery companies, and mutual credit unions. See *id.* § 501(c)(4)–(8), (10), (13)–(14).

285. See, e.g., *id.* § 163(a) (home mortgage interest deduction).

286. See, e.g., *id.* § 21 (the earned income tax credit).

287. State and local governments offer a panoply of tax benefits, including many of the same type of benefits offered by the federal government plus several others like property tax exemptions (as in *Walz v. Tax Comm'n*, 397 U.S. 664 (1970)) and sales tax exemptions (as in *Texas Monthly, Inc. v. Bullock*, 489 U.S. 1 (1989)).

charities that receive special tax treatment because of the particular public benefit purposes they serve,<sup>288</sup> many noncharities like business leagues are tax-exempt because they are inappropriate objects of taxation and, hence, are not exempt for social policy reasons. Accordingly, these noncharitable mutual benefit organizations that are exempt from the income tax do not receive the type of tax benefit that, under tax expenditure theory, is equivalent to a direct grant of government funds. Similarly, there is no clear indication that Congress intended that individuals receiving tax deductions and tax credits be covered by civil rights statutes applying to recipients of FFA. These civil rights statutes apply to any “program or activity receiving ‘FFA.’” Did Congress intend that an individual would ordinarily constitute a program or activity under these statutes? Likely not.<sup>289</sup>

## VI. CONCLUSION

Courts should treat tax benefits received by charities as a form of FFA under federal civil rights statutes. FFA is a federal statutory term.<sup>290</sup> Like any statutory term, it is subject to definition by either statute, agency interpretation, or court interpretation. No federal statute defines the phrase FFA. The prevailing agency interpretation of the term provides that FFA generally refers to government grants and loans.<sup>291</sup> To date, no agency interpretation, at least in regulation form, indicates whether tax benefits are, or are not, a form of FFA. Nor is it likely that any agency will, of its own accord, adopt the view that tax benefits are FFA. Thus, court interpretation is the only mechanism by which tax benefits might be equated with FFA.

The premier case in which the Supreme Court interpreted the phrase FFA is *Grove City College v. Bell*.<sup>292</sup> The Court there concluded that the term FFA includes direct or indirect financial benefits. Further, the Court stated that this statutory term is not limited in scope, except to the extent that Congress so limits it. Given that Congress has never expressed the view that FFA does not include tax benefits, it is reasonable—indeed, logical—to conclude that tax benefits are a form of financial support.

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288. See discussion *supra* notes 38–48 and accompanying text.

289. Cf. *Soberal-Perez v. Heckler*, 717 F.2d 36, 38–39 (2d Cir. 1983) (concluding that social security benefit recipients are not covered by Title VI as “recipients of federal financial assistants” because Congress did not intend so).

290. See discussion *supra* notes 102–18 and accompanying text.

291. See discussion *supra* note 123 and accompanying text.

292. See *Grove City College v. Bell*, 465 U.S. 555 (1984); see also discussion *supra* notes 130–56 and accompanying text.

Of the few courts that have addressed the issue, only one, *McGlotten v. Connally*, reached the conclusion that tax benefits are a form of FFA.<sup>293</sup> However, *McGlotten* goes too far by concluding that tax benefits are equivalent to government expenditures for civil rights statutory purposes as well as for constitutional law purposes.<sup>294</sup> This article contends that a private party is not transformed into a state actor merely because that party is tax-exempt and has the right to receive tax deductible contributions. Nevertheless, *McGlotten* is useful because it demonstrates how tax expenditure theory can be used to expand statutory civil rights protections to include tax benefits as an indirect form of FFA that the Court recognized as appropriate in *Grove City College*. True to tax expenditure theory, however, the *McGlotten* court does not go so far as to equate tax benefits received by social clubs with government grants and loans because these type of tax benefits merely help to define the tax base and are not intended to accomplish any social policy.<sup>295</sup>

Tax expenditure theory clearly supports the idea that tax benefits received by charities can and should be equated with government grants and loans under certain federal civil rights statutes. While the United States Supreme Court has never had occasion to address the particular statutory equivalence issue raised by this article, it has addressed the equivalence issue in various constitutional law contexts. In each of these contexts, something other than economic equivalence of tax benefits and direct expenditures dictated the Court's conclusion.<sup>296</sup> For example, in its religion clause cases, the Court ultimately decides the equivalence issue based primarily on the effect of the tax benefit on government entanglement with religion, a non-economic matter.<sup>297</sup>

The Court's equivalency decisions are generally consistent with recent academic commentary calling for a restrained or watered-down version of tax expenditure theory similar to that implemented by the court in *McGlotten*. This academic commentary suggests (along the same lines as *McGlotten*) that tax benefits and economically equivalent government expenditures should only be treated as legally equivalent to the extent that other non-economic factors are not of paramount importance. Economic benefit is the ultimate and primary concern when making a legal determination about whether

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293. See *McGlotten v. Connally*, 338 F. Supp. 448 (D.D.C. 1972); see also discussion *supra* notes 160–87 and accompanying text.

294. See discussion *supra* notes 189–91 and accompanying text.

295. See discussion *supra* notes 172–77 and accompanying text.

296. See discussion *supra* Part III.A.

297. See discussion *supra* Part III.A.1.

any form of benefit—tax or non-tax—is FFA under relevant civil rights statutes.

In addition to explaining how the statutory term FFA can be interpreted to include tax benefits received by charities, this article also focuses on why such inclusion is a good thing for society.<sup>298</sup> If a private charity wants to wrongfully discriminate against persons because of their race, gender, disability, or similar personal characteristic, we as a society must face the question of how to prevent it from doing so. If we try to pass federal laws that explicitly prohibit such discrimination, whether or not the charity is receiving federal assistance, we may run into trouble. Congress may not have the power, either under the Commerce Clause or the enforcement clause of the Fourteenth Amendment, to reach such action by charities. Nevertheless, Congress does not have to subsidize such discrimination. Thus, Congress can use the Spending Clause and its taxing power as a form of policy leverage to discourage invidious discrimination by private charities. This is done all the time both in civil rights laws and in tax laws. The approach suggested by this article says to charities: “Discriminate if you choose, but not with federal subsidies.” This approach advances and extends, in a lawful and clear fashion, the moral and political agenda against discrimination the Supreme Court sought to advance in *Bob Jones University v. United States*.

Currently, the only civil rights restrictions imposed on private charities are those that emanate from federal civil rights statutes and the public policy limitation announced by the Supreme Court in *Bob Jones University v. United States*. However, these existing civil rights protections, individually and collectively, are inadequate. For example, many federal civil rights statutes only apply to the extent that a private actor receives FFA. Because courts and agencies do not consistently interpret this statutory phrase as including tax benefits, these federal civil rights statutes do not apply to many charities—at least not those that do not receive traditional forms of federal assistance like government grants or loans. Additionally, the *Bob Jones University* court’s public policy limitation is inadequate because it lacks sufficient legal authority and a clearly defined scope of applicability. These inadequacies combine to create a civil rights framework that does not fully satisfy its protection potential. Using tax expenditure theory as a guide, this article concludes that interpreting FFA as including tax benefits would go a long way towards alleviating this social justice inadequacy.

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298. See discussion *supra* Part I.