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Winn and the Inadvisability of Constitutionalizing Tax Expenditure Analysis

In *Arizona Christian School Tuition Organization v. Winn*,¹ the U.S. Supreme Court decided, by the thinnest of margins, that Arizona taxpayers cannot mount an Establishment Clause challenge to Arizona's state income tax credits for "contributions to school tuition organizations."² Writing for a five-Justice majority,³ Justice Kennedy held that *Flast v. Cohen*⁴ only bestows standing upon taxpayers contesting direct monetary outlays on Establishment Clause grounds. *Flast*, the majority held, does not extend standing to taxpayers objecting under the Establishment Clause to tax provisions such as the Arizona income tax credit.⁵ In dissent, Justice Kagan, joined by three of her colleagues,⁶ concluded that *Flast* does afford standing to the Arizona taxpayers challenging the state's tax credits for contributions to school tuition organizations. Central to Justice Kagan's dissent was her invocation of the academic doctrine of "tax expenditure" analysis.⁷ That analysis, Justice Kagan wrote, recognizes that "targeted tax breaks . . . are just spending under a different name."⁸

1. 131 S. Ct. 1436 (2011).

2. *Id.* at 1440.

3. Justice Kennedy's opinion was joined by Chief Justice Roberts and Justices Alito, Scalia, and Thomas. Justice Scalia also wrote a brief concurrence in which Justice Thomas joined.

4. 392 U.S. 83 (1968).

5. See ARIZ. REV. STAT. ANN. § 43-1089 (2011), available at <http://www.azleg.gov/FormatDocument.asp?inDoc=/ars/43/01089.htm>.

6. Justice Kagan's dissent was joined by Justices Breyer, Ginsburg, and Sotomayor.

7. *Winn*, 131 S. Ct. at 1452 (Kagan, J., dissenting).

8. *Id.* at 1456.

The Court has often confronted the question of whether direct public outlays and tax subsidies are equivalent for constitutional purposes.⁹ However, Justice Kagan's dissent in *Winn* is only the second time that tax expenditure doctrine has formally played such an explicit, prominent role in the Court's decisionmaking.¹⁰

The first such occasion was *Rosenberger v. Rector & Visitors of the University of Virginia*.¹¹ In *Rosenberger*, the University of Virginia denied a religious group monetary support from the "Student Activities Fund."¹² The Court, also in an opinion by Justice Kennedy, held that this denial violated the "neutrality the Establishment Clause requires."¹³

Concurring, Justice Thomas sought support for the Court's conclusion in the teachings of tax expenditure analysis: "A tax exemption in many cases is economically and functionally indistinguishable from a direct monetary subsidy."¹⁴ From this premise, Justice Thomas concluded that property tax exemptions for churches, upheld in *Walz v. Tax Commission of New York*,¹⁵ were constitutionally equivalent to the direct monetary outlay to a religious group challenged in *Rosenberger*. Justice Thomas's invocation of tax expenditure analysis triggered a rebuttal from Justice Souter who cited Professor Bittker, the leading academic critic of tax expenditure analysis, as having "dispatched long ago" the asserted "equivalence . . . between a direct money subsidy and the [avoidance of] tax liability."¹⁶

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9. See, e.g., Edward A. Zelinsky, *Are Tax "Benefits" Constitutionally Equivalent to Direct Expenditures?* 112 HARV. L. REV. 379 (1998) (discussing four cases from the mid-1990s, where the Court confronted the question of whether tax benefits are direct expenditures).
 10. The key premises of tax expenditure analysis are (1) that tax deductions, credits, exemptions and exclusions can be divided into "normative" tax provisions necessary to implement the tax and "expenditure" provisions which deviate from the normative tax, and (2) that such tax expenditures are equivalent to direct government outlays. For a seminal statement of tax expenditure analysis, see Stanley S. Surrey, *Tax Incentives as a Device for Implementing Government Policy: A Comparison with Direct Government Expenditures*, 83 HARV. L. REV. 705, 711 (1970).
 11. 515 U.S. 819 (1995).
 12. *Id.* at 824-27.
 13. *Id.* at 846.
 14. *Id.* at 859 (Thomas, J., concurring) (citing Bernard Wolfman, *Tax Expenditures: From Idea to Ideology*, 99 HARV. L. REV. 491 (1985) (reviewing STANLEY S. SURREY & PAUL R. MCDANIEL, *TAX EXPENDITURES* (1985))).
 15. 397 U.S. 664 (1970).
 16. *Rosenberger*, 515 U.S. at 881 n.7 (Souter, J., dissenting) (citing Boris I. Bittker, *Churches, Taxes and the Constitution*, 78 YALE L.J. 1285 (1969)).

Winn thus resurrects a question which has lain quiescent since *Rosenberger*: Does tax expenditure analysis help to decide the constitutionality of tax and direct outlay programs? I am a skeptic. Whatever its value in other settings, in the context of constitutional decisionmaking, tax expenditure analysis has little to contribute. The Court should not constitutionalize tax expenditure analysis. At the end of the day, we do not know what a tax expenditure is. The problem of defining tax expenditures is not one of borderlines and close questions. Rather, at the very core of the concept, there is no satisfactory definition of a tax expenditure.

At one level, tax expenditure analysis has been enormously successful. Tax expenditure analysis today permeates legal scholarship and legal education. When law students are introduced to the federal income tax, tax expenditure analysis is among the first topics they confront.¹⁷ Federal law and the law of many states require the production of “tax expenditures budget[s],” which enumerate the revenue losses attributable to these provisions.¹⁸ As sunlight is indeed “the best of disinfectants,”¹⁹ this is all to the good, creating additional information for legislators and tax policy decisionmakers, information they may (or may not)²⁰ choose to use.

At another level, however, the flaws in tax expenditure analysis identified by Professor Bittker have never been resolved. The core premise of tax expenditure analysis is that tax provisions can be classified into those that are “normative” provisions necessary for the implementation of the tax and those provisions that are “special”²¹ and therefore treated as expenditures. However, no one has yet devised a principled way to implement the distinction between normative and expenditure provisions. As Professor Bittker observed at the birth of tax expenditure analysis, classifying particular tax provisions as

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17. See, e.g., WILLIAM A. KLEIN ET AL., FEDERAL INCOME TAXATION 16 (15th ed. 2009).
 18. See, e.g., Congressional Budget and Impoundment Control Act of 1974, Pub. L. No. 93-344, § 3(a)(3), 88 Stat. 297, 299 (codified at 2 U.S.C. § 622(3) (2006)); MINN. STAT. § 270C.11 (2011), available at <https://www.revisor.mn.gov/statutes/?id=270C.11>; 32 VT. STAT. ANN. tit. 32, § 306(b) (2011), available at <http://www.leg.state.vt.us/statutes/fullsection.cfm?Title=32&Chapter=005&Section=00306>.
 19. *Buckley v. Am. Constitutional Law Found., Inc.*, 525 U.S. 182, 223 (1999).
 20. See Edward A. Zelinsky, *Do Tax Expenditures Create Framing Effects? Volunteer Firefighters, Property Tax Exemptions, and the Paradox of Tax Expenditure Analysis*, 24 VA. TAX REV. 797 (2005).
 21. 2 U.S.C. § 622(3) (2006); see Edward A. Zelinsky, *James Madison and Public Choice at Gucci Gulch: A Procedural Defense of Tax Expenditures and Tax Institutions*, 102 YALE L.J. 1165, 1165 (1993).

expenditures (or not) necessarily involves the drawing of “debatable lines”²²: “every man can create his own set of ‘tax expenditures,’ but it will be no more than his collection of disparities between the income tax law as it is, and as he thinks it ought to be.”²³

Consider, for example, the income tax treatment of qualified retirement plans. Among tax expenditure mavens, the conventional wisdom is that the Internal Revenue Code’s current treatment of such plans constitutes a tax expenditure.²⁴ However, some tax policy criteria, such as administrability and taxpayer liquidity, suggest that the Code’s current treatment of qualified plans is properly viewed as part of a “normative” tax rather than a subsidy operated through the tax system.²⁵

The quandaries of defining tax expenditures arise not simply at the margins, but rather at the very core of the concept. We thus find adherents of tax expenditure analysis still debating among themselves how to define tax expenditures – nearly two generations after the concept was introduced.²⁶

Tax expenditure analysis has produced useful information for legislators and tax policymakers, highlighting potential tax reforms and revenue raisers. However, if tax expenditure analysis is to be a tool of constitutional analysis, it must meet a higher standard, i.e., it must be reasonably coherent and principled in its guidance to the courts. Tax expenditure analysis does not pass this test.

Consider, for example, a religious group that sincerely concludes that the income tax deduction for ordinary and necessary business expenses²⁷ violates its religious beliefs: the deduction helps the affluent more than the poor, and the affluent support churches that propound a form of Christianity with which this group strongly disagrees. Do taxpayers holding this religious perspective have standing to challenge the deduction under the Establishment Clause?

22. Boris I. Bittker, *Accounting for Federal “Tax Subsidies” in the National Budget*, 22 NAT’L TAX J. 244, 250 (1969).

23. *Id.* at 260.

24. See, e.g., JOHN H. LANGBEIN, DAVID A. PRATT & SUSAN J. STABILE, *PENSION AND EMPLOYEE BENEFIT LAW* 358-66 (5th ed. 2010).

25. See Edward A. Zelinsky, *Tax Policy v. Revenue Policy: Qualified Plans, Tax Expenditures, and the Flat, Plan Level Tax*, 13 VA. TAX REV. 591 (1994).

26. Compare Edward D. Kleinbard, *The Congress Within the Congress: How Tax Expenditures Distort Our Budget and Our Political Processes*, 36 OHIO N.U. L. REV. 1 (2010), with J. Clifton Fleming, Jr. & Robert J. Peroni, *Can Tax Expenditure Analysis Be Divorced from a Normative Tax Base?: A Critique of the “New Paradigm” and Its Denouement*, 30 VA. TAX REV. 135 (2010).

27. I.R.C. § 162 (2006).

If, as Justice Kagan suggests in *Winn*, the touchstone is tax expenditure analysis, then the answer is “no.” Virtually all tax expenditure adherents acknowledge the deduction for ordinary and necessary business outlays as a normative provision rather than an expenditure. On the other hand, the economic implications of the business deduction are, for these religiously objecting taxpayers, identical to the consequences of the Arizona tax credit for the *Winn* plaintiffs: both tax provisions “saddle *all* taxpayers with the cost.”²⁸

Or suppose that another set of equally sincere believers objects on religious grounds to the Internal Revenue Code’s current treatment of qualified retirement plans: the benefits of that treatment are heavily skewed in favor of higher income taxpayers who, in turn, support churches that comfort the rich rather than the afflicted. Do these believers have taxpayer standing under the Establishment Clause on the ground that tax expenditure cognoscenti classify current law’s treatment of qualified plans as a tax expenditure? Will these believers subsequently lose their standing if the contrary argument eventually prevails in the tax expenditure literature?

In short, tax expenditure analysis, despite its contribution to tax policy debate, is ill-suited as a tool of constitutional decisionmaking. Sometimes tax provisions are, for constitutional purposes, equivalent to direct monetary outlays; sometimes they are not. That equivalence can only be evaluated on a case-by-case basis, considering the nature of the specific tax provision and the particular constitutional clause at issue.²⁹ Contrary to the approach of the *Winn* dissent, the Court is ill-advised to invoke tax expenditure analysis as a tool of constitutional decisionmaking. At the end of the day, we do not know what a tax expenditure is.

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28. *Ariz. Christian Sch. Tuition Org. v. Winn*, 131 S. Ct. 1436, 1462 (2011) (Kagan, J., dissenting).

29. See Zelinsky, *supra* note 9.