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Charitable Giving and Utilitarianism: Problems and Priorities

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Charitable Giving and Utilitarianism: Problems and Priorities

MIRANDA PERRY FLEISCHER*

Charitable giving is redistributive at heart. It is thus surprising that scholarship on the charitable tax subsidies focuses on the efficient and pluralistic production of public goods while largely ignoring distributive justice concerns. Existing scholarship and current law leave crucial questions unanswered: How should we prioritize among charities? Should subsidized groups be required to help the poor? Are criticisms that charities do too little to help the poor valid? This Article is part of a series that examines how each common theory of distributive justice would answer these questions.

More specifically, this Article explores utilitarianism and the charitable tax subsidies using the definitions of “utility” most common in legal scholarship: income, happiness, preference satisfaction, and objective-list well-being. It demonstrates that a careful application of utilitarianism as used by tax scholars (which equates income with utility) suggests that charities assisting the underprivileged deserve special treatment. This contrasts with the current structure, which does not prioritize such organizations, and contradicts the conventional wisdom concerning utilitarianism and charitable giving.

Initially, other interpretations of utilitarianism common in the legal literature (focusing on preference satisfaction, subjective well-being, and objective lists) appear to support the conventional wisdom that groups assisting the poor are not special. Each of these approaches, however, has intrinsic drawbacks when it comes to prioritizing among organizations and answering the recurring distributional questions facing the non-profit sector. But viewing these approaches together highlights a commonality: donative organizations that help the poor likely enhance welfare under all of the common welfare-based theories of justice. This is also true of traditional income-based utilitarianism, the leximin, and the most common equality of opportunity theories. This overlap suggests that tax policy should favor such groups, thus reconciling distributional concerns with pluralism by emphasizing what various moral theories have in common.

INTRODUCTION.....	1486
I. THE CHARITABLE TAX SUBSIDIES AND THEIR THEORETICAL FOUNDATIONS	1492
A. WHY SUBSIDIZE CHARITY?	1494

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B. THE BENEFITS OF SUBSIDIZING CHARITY THROUGH THE TAX SYSTEM: EFFICIENCY, PLURALISM, AND DESERVEDNESS.....	1495
C. LINGERING QUESTIONS	1497
D. THE ROLE OF DISTRIBUTIVE JUSTICE.....	1500
II. WHY BENEFICIARY UTILITY MATTERS	1502
III. UTILITY AS INCOME	1505
A. TRADITIONAL DECLINING MARGINAL UTILITY AND THE CHARITABLE TAX SUBSIDIES	1506
B. CHALLENGING THE ASSUMPTIONS OF TRADITIONAL UTILITARIANISM ..	1514
C. FINAL THOUGHTS ON UTILITARIANISM, INCOME REDISTRIBUTION, AND THE CHARITABLE TAX SUBSIDIES.....	1519
IV. UTILITY AS WELL-BEING.....	1522
A. UTILITY AS PREFERENCE SATISFACTION.....	1524
B. UTILITY AS SUBJECTIVE WELL-BEING.....	1530
C. OBJECTIVE LIST CONCEPTIONS OF WELL-BEING	1540
D. CONCLUDING THOUGHTS ON WELL-BEING	1542
V. A BRIEF WORD ABOUT THE LEXIMIN.....	1543
CONCLUSION.....	1543

INTRODUCTION

Charitable giving is redistributive at heart. One person parts with money or property, and others receive a benefit in the form of charitable goods or services. Sometimes that redistribution is downward (a wealthy individual making a donation to a soup kitchen); other times it is among people who are equally situated (a Harvard Business School graduate donating to her alma mater). Despite this inherent redistribution, normative tax scholarship on the charitable tax subsidies (which encourage and subsidize charitable giving) largely ignores distributive justice concerns. Instead, such scholarship emphasizes how having voluntarily-funded public goods enhances both efficiency and pluralism.¹

While identifying these benefits is a necessary and important contribution to our understanding of the charitable tax subsidies, a careful exploration of distributive justice is also necessary.² To that end, this Article is part of a series providing a detailed look at the interaction of distributive justice and the charitable tax subsidies.³

1. See generally Miranda Perry Fleischer, *Theorizing the Charitable Tax Subsidies: The Role of Distributive Justice*, 87 WASH. U. L. REV. 505 (2010).

2. *Id.* at 528–56. See *infra* note 98 for a discussion of how this series can complement the optimal tax analysis work.

3. See Fleischer, *supra* note 1, at 528–56 (illustrating the need to consider distributive justice in addition to pluralism and efficiency); Miranda Perry Fleischer, *Equality of Opportunity and the Charitable Tax Subsidies*, 91 B.U. L. REV. 601, 635–62 (2011) (examining equality of opportunity theories). A future essay will examine libertarianism. Although each article largely examines various theories in isolation, one goal of the series is to compare and contrast the various theories to identify areas of commonality and disagreement. Commonalities among the theories may yield answers to certain questions while differences among the theories may provide contrasting answers to others. Even in the latter case, explicitly identifying which theories undergird the current legal regime will help those wrestling with the question at issue.

More specifically, the series demonstrates how each theory of justice common in tax scholarship would answer crucial questions⁴ that are unresolved in current law and existing scholarship: Should charities that receive tax benefits be required to help the poor? How valid are common criticisms that subsidized groups do “too much” for the wealthy and “too little” for the poor? How should we evaluate the distributional impact of various proposals to reform the tax benefits given to the sector? How should the subsidies be structured?⁵

This Article explores the answers that welfare-based theories of distributive justice provide to these questions.⁶ It focuses on utilitarianism, which—despite falling into disrepute in other areas⁷—continues to exert a strong influence on current tax policy.⁸

Simply put, having a sense of the distributive justice landscape—both what it can and cannot tell us about charitable giving—will enhance our understanding of the charitable tax subsidies.

4. In analyzing these questions, the series takes the existence of the charitable tax subsidies as a given. It therefore does not address, for example, whether increasing direct government programs, instead of subsidizing the charitable sector, would better effectuate a given theory of distributive justice or whether the charitable sector should be left as is, with any unmet distributive needs being addressed through the tax and transfer system. Instead, it takes the charitable sector as a given and then seeks to address what distributive justice can add to our understanding of the charitable tax subsidies. Moreover, this exercise is not meant to suggest that redistribution is either the only goal of or justification for the sector. Rather, this series recognizes the importance of the efficiency- and pluralism-enhancing rationales for the sector and does not dispute their significance. It does argue, however, that distributive concerns are also relevant. The tax benefits granted to the sector are inherently redistributive; some persons are taxed more heavily than otherwise to pay for projects identified by others. At times, society will have to prioritize among the various subsidized groups that further both efficiency and pluralism, and we need some theoretical underpinning for that task.

5. It is also possible that a detailed look at distributive justice yields answers to additional questions concerning the tax subsidies, such as whether there should be limits on lobbying, political activity, and commerciality. It is not possible, however, to also address those questions in this Article.

6. Welfarist theories judge ex post outcomes based on various measures of welfare, such as income or wealth, happiness, preference satisfaction, or objective conceptions of well-being; in tax scholarship, two of the most common such theories are the leximin (which seeks to improve the welfare of the least-advantaged) and utilitarianism. Joseph Bankman & Thomas Griffith, *Social Welfare and the Rate Structure: A New Look at Progressive Taxation*, 75 CALIF. L. REV. 1905, 1915–18 (1987). In contrast, deontological theories such as equality of opportunity and libertarianism focus on ex ante factors (resources, for example) to judge the fairness of a given distribution. Anne L. Alstott, *Equal Opportunity and Inheritance Taxation*, 121 HARV. L. REV. 469, 471 (2007).

7. See Edward J. McCaffery, *Slouching Towards Equality: Gender Discrimination, Market Efficiency, and Social Change*, 103 YALE L.J. 595, 643 n.167 (1993) (citations omitted).

8. See Alstott, *supra* note 6, at 474 (“In taxation, utilitarianism by way of law and economics has dominated normative legal analysis in the last generation.”); Thomas D. Griffith, *Progressive Taxation and Happiness*, 45 B.C. L. REV. 1363, 1366 (2004) (assuming that “improving aggregate social welfare, as measured by the individual utility levels or happiness of the population, remains one important goal of tax policy”); Marjorie E. Kornhauser, *Educating Ourselves Towards a Progressive (and Happier) Tax: A Commentary on Griffith’s Progressive Taxation and Happiness*, 45 B.C. L. REV. 1399, 1401 (2004) (assuming a utilitarian framework for tax policy); Sagit Leviner, *From Deontology to Practical Application: The Vision of a Good Society and the Tax System*, 26 VA. TAX REV. 405, 428 (2006) (“[U]tilitarian principles . . . [have]

Under this theory of distributive justice,⁹ the proper role of political institutions is to maximize the total amount of utility (generally meaning well-being or happiness) across society.¹⁰ This Article demonstrates that a careful application of utilitarianism (as used by tax scholars)¹¹ upends prevailing understandings of the charitable tax subsidies: it suggests that charities that assist the underprivileged deserve special treatment, in contrast to the current structure, which does not prioritize such

been widely embraced by contemporary tax theory.”); Theodore P. Seto & Sande L. Buhai, *Tax and Disability: Ability to Pay and the Taxation of Difference*, 154 U. PA. L. REV. 1053, 1074 (2006) (noting “the dominance of utilitarianism among U.S. tax theorists”); Nancy C. Staudt, *The Hidden Costs of the Progressivity Debate*, 50 VAND. L. REV. 919, 939–50 (1997) (stating that “utilitarianism has been the primary ethical foundation of the tax laws throughout the twentieth century”); Linda Sugin, *A Philosophical Objection to the Optimal Tax Model*, 64 TAX L. REV. 229, 230 (2011) (“[U]tilitarian conceptions of social welfare . . . have become the dominant construct in tax policy analysis.”).

9. Although some debate exists outside of tax as to whether utilitarianism should be considered a theory of distributive justice, this Article follows the majority of tax scholarship in treating it as such. *See, e.g.*, ERIC RAKOWSKI, *EQUAL JUSTICE* 23 (1991) (referring to utilitarianism as a theory of “distributive justice”); Kyle Logue & Ronen Avraham, *Redistributing Optimally: Of Tax Rules, Legal Rules, and Insurance*, 56 TAX L. REV. 157, 158 (2003) (listing utilitarianism as a theory of distributive justice); Daniel N. Shaviro, *Commentary: Inequality, Wealth, and Endowment*, 53 TAX L. REV. 397, 400 (2000) (referring to utilitarianism as a “distributional approach”); Kirk J. Stark, *Enslaving the Beachcomber: Some Thoughts on the Liberty Objections to Endowment Taxation*, 18 CAN. J.L. & JURISPRUDENCE 47, 49 (2005) (referring to utilitarianism as one of “two leading theories of distributive justice”); Linda Sugin, *Theories of Distributive Justice and Limitations on Taxation: What Rawls Demands from Tax Systems*, 72 FORDHAM L. REV. 1991 (2004) (likewise conceptualizing utilitarianism as a theory of distributive justice); Julian Lamont & Christi Favor, *Distributive Justice*, STAN. ENCYCLOPEDIA PHIL., <http://plato.stanford.edu/entries/justice-distributive/#> (last modified Jan. 2, 2013) (including utilitarianism as an example of a welfare-based conception of distributive justice); Lawrence Solum, *Legal Theory Lexicon: Distributive Justice*, LEGAL THEORY BLOG (Nov. 9, 2008), <http://lsolum.typepad.com/legaltheory/2008/11/legal-theory--1.html> (referring to utilitarianism as one of the predominant theories of distributive justice). *But see* Matt Adler, *Risk, Death and Harm: The Normative Foundations of Risk Regulation*, 87 MINN. L. REV. 1293, 1423 (2003) (suggesting that utilitarianism is distinct from distributive justice).

10. *See, e.g.*, WILL KYMLICKA, *CONTEMPORARY POLITICAL PHILOSOPHY: AN INTRODUCTION* 10 (2d ed. 2002); LIAM MURPHY & THOMAS NAGEL, *THE MYTH OF OWNERSHIP* 51 (2002); JOHN RAWLS, *A THEORY OF JUSTICE* 20 (rev. ed. 1999).

11. The philosophical literature, of course, contains a vast debate concerning the meaning of “utility” and how utilitarianism should be implemented. *See generally* UTILITARIANISM AND BEYOND (Amartya Sen & Bernard Williams eds., 1982). This Article largely sets those debates aside (it does not address, for example, rule vs. act utilitarianism), and instead applies utilitarianism in the manner common to tax scholarship—that is, by equating it with the maximization of what is variously called “utility,” “welfare,” or “well-being.” For that reason, some readers may prefer the terms “welfarism” or “consequentialism” instead of “utilitarianism.” I continue to use the term “utilitarianism,” however, because the tax scholarship does so. *See supra* note 9. I also acknowledge that this interpretation of utilitarianism mirrors most closely the views of early utilitarians such as Bentham and Mill while leaving aside later developments in the philosophical literature. Again, this reflects the use of utilitarianism in tax scholarship. *See id.* For an accessible overview of utilitarian theory, see KYMLICKA, *supra* note 10.

organizations. This conclusion contradicts the conventional wisdom concerning utilitarianism and the charitable tax subsidies, which is that utilitarianism suggests there is nothing special about organizations assisting the underprivileged.¹²

This common (but wrong) understanding stems from a variety of sources. As an initial matter, some argue that while utilitarianism might justify the existence of the charitable tax subsidies by increasing the size and scope of the charitable sector, it has nothing additional to say about the content of those subsidies (for example, whether certain organizations should be prioritized).¹³ Although this Article does not disagree with the former,¹⁴ it challenges the latter. Namely, this assumption ignores the inherent redistribution that occurs through the charitable tax subsidies¹⁵ and whether all charitable organizations increase beneficiary utility (however defined) equally. The question still remains whether dividing the subsidized “pie” in different ways affects overall utility.

Other theorists would admit that utilitarianism does have something to say about the content (and not merely the existence) of the charitable tax subsidies, but that there is nothing special about organizations helping the poor.¹⁶ The most common form of this argument derives from scholars who use income as a proxy for utility and focus on the declining marginal utility thereof, as most tax scholars do. According to this view, any charity that redistributes “downward,” even if that redistribution is from a wealthy to a middle-class individual (perhaps a museum), increases utility.¹⁷ Subsidized groups should therefore not be required to help the poor, so long as the organization benefits individuals who are less well-off than the donor.¹⁸ These theorists would thus argue that common criticisms of the subsidies for not doing enough to help the poor are unfounded and that groups that aid the poor do not merit special treatment.¹⁹

12. See, e.g., Boris I. Bittker, *Charitable Contributions: Tax Deductions or Matching Grants?*, 28 TAX L. REV. 37, 55–56 (1972).

13. See, e.g., David E. Pozen, *Remapping the Charitable Deduction*, 39 CONN. L. REV. 531, 560 (2006) (arguing that the charitable tax subsidies are consistent with utilitarianism because they “generat[e] a greater quantity, quality, and diversity of public goods” than otherwise).

14. Defending that proposition, however, is beyond the scope of this Article. As previously mentioned, see *supra* note 3, this Article takes the existence of the charitable tax subsidies as a given and then proceeds from there.

15. As explained in Part III.C.2, there are several levels of redistribution to take into account. With respect to charitable contributions, there is redistribution from the donor to the organization’s beneficiaries; the donation itself is a transfer that effectuates redistribution. And with both the charitable deduction and tax exemption, the subsidy provided to a given charitable organization triggers redistribution from other taxpayers to the group’s beneficiaries. State and local tax exemptions similarly generate redistribution.

16. See Part III.A.1.

17. For example, some early scholars of the deduction have argued that because donors to charitable organizations tend to be better off than the beneficiaries of those organizations, the resulting downward redistribution enhances progressivity. See e.g., Bittker, *supra* note 12. Although Bittker does not specifically cast his argument in terms of utility, his argument implies an underlying utilitarian framework based on declining marginal utility.

18. Bittker, *supra* note 12.

19. *Id.* (rejecting the argument that little downward redistribution occurs via the charitable tax subsidies).

In contrast, this Article argues that, except in cases of donative organizations providing basic needs to the poor, identifying when an organization redistributes downward is almost impossible. How do we determine the utility received by a visitor to an art museum? What if not all individuals, in fact, experience declining marginal utility? These complications show that in many cases, identifying when a group redistributes from donors to beneficiaries in a manner that enhances utility is exceedingly difficult. Moreover, while the common wisdom purports to justify the charitable deduction, it is quite hard to apply to tax exemption. For example, who are the “donors” and “beneficiaries” of organizations such as daycare providers and healthcare organizations that charge for their services? How do we account for the decreased utility of the taxpaying public, who either receive fewer other benefits or pay higher taxes? This challenges the conventional wisdom that the existing structure contains enough downward redistribution, scattered along the income spectrum, to render the current scheme of tax benefits consistent with utilitarian principles.²⁰

As this Article shows, however, these difficulties fall away in the case of donative organizations²¹ providing basic services to the very poorest. The transferor (the contributor to the soup kitchen, for example) is identifiable, as is the beneficiary (the person eating the soup). The donor is almost certainly from a higher income bracket than the beneficiary. And regardless of the extent to which individuals above a given income experience the declining marginal utility of money, the fact that beneficiaries are very poor strongly suggests their marginal utility curve is steeper than that of donors. A careful look at this strand of utilitarianism thus shows that the types of groups we can most comfortably identify as increasing utility via income redistribution are donative organizations that provide basic needs to the poor.

The remaining conventional wisdom concerning utilitarianism and the charitable tax subsidies is more nuanced, as is this Article’s response. These strands of conventional wisdom derive from theories that equate utility with measures other than income. For example, theorists who focus on preference satisfaction implicitly argue that the breadth of the existing structure enhances utility by providing individuals who have minority tastes with funding for their preferred projects.²² If forced to prioritize among charities, these theorists would likely argue that organizations reflecting the preferences of the greatest number of donors should receive priority.²³ Because these theorists do not focus on income, they would not

20. On a broader level, this analysis concretely exemplifies a broader problem in tax policy, identified years ago in a seminal critique on progressive tax rates. *See generally* Walter J. Blum & Harry Kalven, Jr., *The Uneasy Case for Progressive Taxation*, 19 U. CHI. L. REV. 417 (1952). As traditionally applied to tax policy, utilitarianism is too indefinite to be useful because of the interpersonal comparisons it requires.

21. The term “donative organizations” refers to groups that are funded largely by donations, as opposed to by fees for services. *See* Henry Hansmann, *The Rationale for Exempting Nonprofit Organizations from Corporate Income Taxation*, 91 YALE L.J. 54, 60 (1981).

22. These theorists, who emphasize the efficiency gains from the subsidies’ capacity to satisfy the preferences of donors, do not label their analysis “utilitarian” as such. *See infra* Part I.B.

23. As with income-focused utilitarianism, this argument is most frequently used to

prioritize groups that help the poor. Those who equate utility with subjective well-being or with objective-list well-being would likely make similar arguments: organizations that enhance well-being (however defined) the most should receive priority, whether or not they assist the poor.

Each of these additional conceptions of utilitarianism would fund a wide range of activities in addition to poor relief, such as participatory sports groups, churches, and museums and other expressions of high culture. This Article does not challenge that conclusion in the same way it challenges the applicability of income-based utilitarianism to activities other than poor relief. What this Article does show, however, is that each of these conceptions of utility has intrinsic drawbacks that run headfirst into the nondistributional goal of pluralism. Using preference satisfaction as the metric for the charitable tax subsidies does not adequately address the specter of the tyranny of the majority. Nor does it address the preferences of individuals other than donors, which is necessary both when discussing the subsidization from the charitable deduction (separate from the contribution itself) and when discussing nondonative organizations subsidized only via tax exemption. Likewise, defining utility as happiness or objective-list well-being is also problematic; doing so is at direct odds with the goals of enhancing pluralism and protecting individuals with minority tastes. Moreover, choosing among any of these approaches—including income-focused utilitarianism—runs counter to the pluralistic goals of the sector.

This Article argues that prioritizing groups that help the poor offers a way around these problems.²⁴ Although viewing any single interpretation of utilitarianism in isolation is problematic, viewing them together highlights a commonality: donative organizations that help the poor likely enhance welfare under all of the common welfare-based theories of justice. Regardless of the extent to which each theory would subsidize activities in addition to helping the poor, all would help lower-income individuals. In addition, however one might identify the “least-advantaged” for purposes of the leximin (which prioritizes the least-advantaged), the financially poor would be included. Interestingly, this coincides with the equality of opportunity theories.²⁵ Resource egalitarianism, the equal opportunity theory most commonly invoked by tax theorists, is a prime example;²⁶ regardless of how one would treat expensive tastes and talent pooling, the various strands of resource egalitarianism would all assist the poor.²⁷ This overlap suggests

justify the charitable deduction (and not tax exemption), but this should not preclude an examination of the relationship between preference satisfaction and tax exemption. The same is true of happiness or objective-list approaches. In fact, the applicability of those approaches to tax exemption seems more straightforward, since they largely do not depend on comparing donors and donees.

24. For a discussion of how we might prioritize such groups, see *infra* Conclusion.

25. See Fleischer, *supra* note 3, at 636–52.

26. See generally Michael J. Graetz, *To Praise the Estate Tax, Not to Bury It*, 93 YALE L.J. 259 (1983); Edward J. McCaffery, *The Uneasy Case for Wealth Transfer Taxation*, 104 YALE L.J. 283 (1994); Eric Rakowski, *Can Wealth Taxes Be Justified?*, 53 TAX L. REV. 263 (2000); James R. Repetti, *Democracy and Opportunity: A New Paradigm in Tax Equity*, 61 VAND. L. REV. 1129 (2008); Daniel Shaviro, *Endowment and Inequality*, in TAX JUSTICE: THE ONGOING DEBATE 123 (Joseph J. Thorndike & Dennis J. Ventry, Jr. eds., 2002); Stark, *supra* note 9; Lawrence Zelenak, *Taxing Endowment*, 55 DUKE L.J. 1145 (2006).

27. Some strands would also subsidize an array of other groups, but again, an area of commonality emerges. See Fleischer, *supra* note 3, at 636–52.

that competing views of distributive justice can be integrated into charitable-giving policy by focusing on what the various theories have in common.

This Article proceeds as follows. Part I provides a brief explanation of the charitable tax subsidies and their theoretical justifications. Part II illustrates why beneficiary utility matters in addition to donor utility, which is the general focus of current scholarship. Part III explores “traditional utilitarianism,” which measures utility in terms of income or wealth and assumes the declining marginal utility thereof. Part IV moves beyond using income as a proxy for utility. Instead, it examines three conceptions of utility or well-being currently prevalent in legal literature (preference satisfaction, happiness, and objective well-being) to explore what happens when we reframe the utilitarian task as one of increasing overall societal welfare. Part V addresses the leximin theory of justice and the charitable tax subsidies, after which a brief conclusion ensues.

I. THE CHARITABLE TAX SUBSIDIES AND THEIR THEORETICAL FOUNDATIONS

From ancient Egypt to seventeenth-century England to colonial America, charities have enjoyed a special legal status.²⁸ Today’s federal tax system continues this status by exempting charities from the corporate income tax and allowing donors to deduct contributions from their individual taxes.²⁹ To obtain these benefits under sections 170(c) and 501(c)(3),³⁰ respectively, organizations must have an appropriately indeterminate class of beneficiaries³¹ and primarily serve religious, charitable, scientific, literary, or educational purposes. Groups eligible for both provisions are referred to as “charitable” organizations, regardless of whether they further an explicitly enumerated purpose, such as the “educational” purpose, or the catchall “charitable” purpose.

28. JOHN D. COLOMBO & MARK A. HALL, *THE CHARITABLE TAX EXEMPTION* 3–5 (1995).

29. The estate tax provides a similar deduction. *See generally* Miranda Perry Fleischer, *Charitable Contributions in an Ideal Estate Tax*, 60 *TAX L. REV.* 263 (2007). At the state level, most states exempt charities from state property, sales, and corporate income taxes in a manner that generally keys off of the federal tax standards. *Id.* I believe that any discussion of the extent to which federal tax benefits maximize utility (however defined) would also translate to a discussion of those benefits.

30. Groups eligible to receive deductible contributions under I.R.C. § 170 (2012) are almost always eligible for tax exemption under I.R.C. § 501(c)(3) (2012). Analytical interpretations of § 170 therefore generally apply to § 501(c)(3), and vice versa. To be clear, several other types of organizations (such as mutual benefit organizations) are tax-exempt under § 501, but cannot receive deductible contributions. Although these organizations raise their own interesting questions, this Article’s focus is on those groups eligible for both sets of subsidies—generally referred to as “charitable” organizations.

31. This requirement stems from the concern that a group organized to benefit specific individuals or a small, identifiable group may not be benefiting the community at large. *See* J. COMM. ON TAXATION, JCX-29-05, *Historical Development and Present Law of the Federal Tax Exemption for Charities and Other Tax-Exempt Organizations* 63 (2005) [hereinafter *HISTORICAL DEVELOPMENT*] (“The charitable class requirement provides that an organization be organized to benefit a sufficiently large or indefinite class of people.” (citation omitted)); BRUCE R. HOPKINS, *THE LAW OF TAX-EXEMPT ORGANIZATIONS* 166–68 (10th ed. 2011).

Courts and the Internal Revenue Service (IRS) construe these purposes quite broadly.³² In particular, the “charitable” purpose (as opposed to the specifically enumerated purposes) has been held to cover organizations as diverse as environmental preservation, cause-oriented public interest litigation, and support for the arts.³³ Quite generally, groups qualifying under the charitable purpose must provide some type of “community benefit,” often by fulfilling needs unmet by the private market. Little guidance exists, however, as to what exactly constitutes a community benefit. Sometimes, the poor must be benefited (health clubs for the middle class do not serve a community benefit but YMCAs with programs for the poor do);³⁴ other times (as with the arts and many health services), no benefit for the poor is required.³⁵ Similarly broad definitions apply to the enumerated purposes. The educational purpose includes organizations ranging from Harvard to the National Mustard Museum to the Paper Industry International Hall of Fame;³⁶ the religious purpose includes groups such as the Church of Body Modification³⁷ and witches’ covens.³⁸

In addition to these broadly construed positive requirements, a number of negative prohibitions also define the sector. For example, rules against quid pro quo contributions,³⁹ commerciality,⁴⁰ private benefit,⁴¹ and private inurement⁴² also

32. See JAMES J. FISHMAN & STEPHEN SCHWARZ, *NONPROFIT ORGANIZATIONS: CASES AND MATERIALS* 319–69 (4th ed. 2010) (discussing the breadth of the charitable purpose prong and providing an overview).

33. *Id.*

34. See John D. Colombo, *The Role of Access in Charitable Tax Exemption*, 82 WASH. U. L.Q. 343, 358–60, 384 (2004).

35. See *Goldsboro Art League, Inc. v. Comm’r*, 75 T.C. 337 (1980) (arts); Rev. Rul. 83-157, 1983-2 C.B. 94 (specialized hospitals without emergency rooms may qualify for tax exemption without offering free or reduced cost services to the poor); Rev. Rul. 69-545, 1969-2 C.B. 117 (hospitals can qualify for tax exemption without offering inpatient care to indigent patients if they have an open emergency room).

36. Treas. Reg. § 1.501(c)(3)-1(d)(3) (as amended in 2008); *Become a Friend*, NAT’L MUSTARD MUSEUM, <http://mustardmuseum.com/be-a-friend-of-the-mustard-museum/become-a-friend/>; *Donations*, PAPER INDUSTRY INT’L HALL OF FAME, INC., <http://www.paperhall.org/donations/>; *Section 501(c)(3) Exemption*, HARV. U. OFF. CONTROLLER, http://vpf-web.harvard.edu/ofs/tax_services/gen_exe.shtml.

37. *FAQ*, CHURCH OF BODY MODIFICATION, <http://uscobm.com/faq/#501>.

38. I.R.S. Gen. Couns. Mem. 36,993 (Feb. 3, 1997).

39. Treas. Reg. § 1.170A-1(h) (as amended in 2008) (disallowing deductions for transfers made as consideration for goods or services).

40. HISTORICAL DEVELOPMENT, *supra* note 31, at 51 (“If an organization conducts a trade or business that is not related to exempt purposes, the question . . . is whether such activity is substantial. If so, then the organization should lose exempt status under . . . the commerciality doctrine.”); Treas. Reg. § 1.501(c)(3)-1(e) (as amended in 2008) (“An organization . . . organized and operated for the primary purpose of carrying on an unrelated trade or business is not exempt . . .”).

41. HISTORICAL DEVELOPMENT, *supra* note 31, at 55–56; Treas. Reg. § 1.501(c)(3)-1(d)(1)(ii) (as amended in 2008).

42. I.R.C. § 501(c)(3) (2012) (requiring that “no part of the net earnings . . . inure[] to the benefit of any private shareholder or individual”); HISTORICAL DEVELOPMENT, *supra* note 31, at 54–55; Treas. Reg. § 1.501(c)(3)-1(c)(2) (as amended in 2008).

define the sector. These requirements reason backwards: if a group neither benefits specific individuals nor acts “too much” like a for-profit, then it must be benefiting the community at large and thus deserves a subsidy. But since the “good” we want these organizations to do is so vaguely defined, it is hard to craft straightforward rules prohibiting the “bad” we do not want them to do. Not surprisingly, both sets of rules are a mess, creating inconsistent results and much confusion in the law concerning what charities can and cannot do.⁴³

A. Why Subsidize Charity?

Academics and policymakers widely agree that sections 170(c) and 501(c)(3) serve as subsidies for the charitable sector.⁴⁴ That said, less agreement exists as to why the sector should be subsidized.⁴⁵ The oldest explanation (the “traditional subsidy theory”) is that subsidizing the sector is “good” because of the benefits it provides.⁴⁶ Charities often relieve the government of burdens it would otherwise bear, such as poverty relief. Charities offer diverse and creative solutions to societal problems and offer competing viewpoints in the arts and culture.⁴⁷ And lastly, a

43. See John Simon, Harvey Dale, & Laura Chisolm, *The Federal Tax Treatment of Charitable Organizations*, in *THE NONPROFIT SECTOR: A RESEARCH HANDBOOK* 267, 277–78 (Walter W. Powell & Richard Steinberg eds., 2d ed. 2006) (discussing the inconsistency in requiring some groups, but not others, to help the poor in order to qualify for the charitable tax subsidies); John D. Colombo, *The Role of Redistribution to the Poor in Federal Tax Exemption for Charities* 4–13 (2009) (unpublished manuscript), available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2350493.

44. Although in the minority, a few academics justify these provisions on measurement grounds. See William D. Andrews, *Personal Deductions in an Ideal Income Tax*, 86 *HARV. L. REV.* 309 (1972) (arguing that the charitable deduction is necessary to measure individuals’ incomes accurately); Boris I. Bittker & George K. Rahdert, *The Exemption of Nonprofit Organizations from Federal Income Taxation*, 85 *YALE L.J.* 299 (1976) (arguing that tax exemption is justified on the grounds that measuring charities’ net incomes would be too difficult).

45. To see how the charitable deduction subsidizes charities, imagine a taxpayer in the 35% bracket who makes a \$100 donation and receives a \$100 deduction. The deduction lowers her tax bill by \$35, reducing the net cost of her transfer to \$65. The government has subsidized her gift by \$35. The subsidy is thought to increase taxpayer incentives to make such contributions, in turn enhancing the size and scope of the charitable sector. Tax exemption subsidizes charities by leaving them with more funds to use for their charitable programs than they would have in a world where they are taxed. To illustrate, a taxable organization with net revenues of \$100,000 would face a 35% tax bill, leaving it with only \$65,000. But a tax-exempt organization with net revenues of \$100,000 pays zero tax (ignoring the Unrelated Business Income Tax) and thus has all \$100,000 to use for more charitable activities the next year. The \$35,000 not collected from the exempt groups equals its subsidy.

46. See COLOMBO & HALL, *supra* note 28, at 45; Bittker, *supra* note 12, at 39; Nina J. Crimm, *An Explanation of the Federal Income Tax Exemption for Charitable Organizations: A Theory of Risk Compensation*, 50 *FLA. L. REV.* 419, 430 n.34 (1998) (citations omitted); Hansmann, *supra* note 21, at 66; Paul R. McDaniel, *Federal Matching Grants for Charitable Contributions: A Substitute for the Income Tax Deduction*, 27 *TAX L. REV.* 377, 390 (1972).

47. See Rob Atkinson, *Altruism in Nonprofit Organizations*, 31 *B.C. L. REV.* 501, 605 n.291 (1990) (citations omitted); Bittker, *supra* note 12, at 39; McDaniel, *supra* note 46, at 390–91.

vibrant nonprofit sector is thought to counter governmental power and enhance pluralism.⁴⁸

Economic theory provides a newer and more accepted justification for subsidizing charities. This “economic subsidy theory” posits that subsidizing charities helps them provide public goods that suffer from market and governmental failures. Such goods are often subject to market failure due to free rider and informational problems.⁴⁹ At the government level, our majority-rule democratic process tends to supply public goods only at the level demanded by the median voter.⁵⁰ This means that the government funds the public goods favored by the majority (for example, national defense) but not the minority (perhaps a museum). Some public goods, however, remain unfunded. Enter the charitable tax subsidies. They represent an implicit bargain among minority interests favoring undersupplied public goods who agree to provide partial funding (via a subsidy) for one another’s preferred minority projects. The subsidies thus allow individuals with minority interests to redirect some part of the funds otherwise flowing to the federal fisc toward their visions of the public good.⁵¹

*B. The Benefits of Subsidizing Charity Through the Tax System:
Efficiency, Pluralism, and Deservedness*

While the economic theory outlined above explains why charities are subsidized, it does not address why the tax system is the best way to do so. Later work building on the economic subsidy theory fills that gap by identifying a number of benefits from using the tax system to subsidize public-benefiting projects. Some focus on efficiency, arguing that tax deductions (or credits)⁵² are more efficient than direct governmental grants.⁵³ This is so because tax deductions allow the cost of a given project to be allocated among individuals in proportion to the value each places on it.⁵⁴ Direct grants, in contrast, would require

48. See *supra* notes 46 and 47.

49. See, e.g., COLOMBO & HALL, *supra* note 28, at 100–08; Burton A. Weisbrod, *Toward a Theory of the Voluntary Nonprofit Sector in a Three-Sector Economy*, in THE ECONOMICS OF NONPROFIT INSTITUTIONS: STUDIES IN STRUCTURE AND POLICY 21, 21–22 (Susan Rose-Ackerman ed., 1986); Mark P. Gergen, *The Case for a Charitable Contributions Deduction*, 74 VA. L. REV. 1393, 1396–406 (1988) (summarizing the works of Hochman, Rogers, and Weisbrod on both the deduction and exemption); Hansmann, *supra* note 21, at 54.

50. Although majority preferences do not always prevail, the literature generally uses such a model for simplicity. See, e.g., COLOMBO & HALL, *supra* note 28, at 102.

51. See *id.* at 107–08; Weisbrod, *supra* note 49, at 36.

52. Scholars debate, however, whether a tax deduction or a tax credit is more efficient. Compare Jeff Strnad, *The Charitable Contribution Deduction: A Politico-Economic Analysis*, in THE ECONOMICS OF NONPROFIT INSTITUTIONS: STUDIES IN STRUCTURE AND POLICY, *supra* note 49, at 265, 272–76 (supporting a deduction), with Harold M. Hochman & James D. Rodgers, *The Optimal Tax Treatment of Charitable Contributions*, in THE ECONOMICS OF NONPROFIT INSTITUTIONS: STUDIES IN STRUCTURE AND POLICY, *supra* note 49, at 224, 236 (supporting a credit).

53. See Gergen, *supra* note 49, at 1399–406.

54. *Id.* at 1402. This is so because high demanders pay “more” by making a voluntary

across-the-board tax increases, which would almost certainly not reflect how much a given taxpayer values the project in question.⁵⁵

Others highlight how pluralism is enhanced by having individual taxpayers identify which projects deserve subsidies. Most notably, Saul Levmore describes the charitable deduction as allowing individual taxpayers to “vote” on which projects merit subsidies and at what level.⁵⁶ According to Levmore, letting taxpayers “vote” in this manner matches the size of the subsidy to taxpayer enthusiasm for a given project.⁵⁷ In addition, he further posits that taxpayers who have a voice in deciding which projects to fund will be more committed to such projects, be more active volunteers and monitors, and tolerate higher levels of redistribution and government funding of public goods.⁵⁸ David Schizer has similarly argued that giving individual taxpayers leeway in choosing which projects to fund enhances generosity and monitoring.⁵⁹

The donative theory developed by John Colombo and Mark Hall identifies two benefits of having taxpayers determine which activities to subsidize by making donations.⁶⁰ First, the donations signal that the recipient’s services are undersupplied by the market and government, which shows that the project *needs* a subsidy.⁶¹ Second, the contributions demonstrate that the public believes the services are beneficial to the community, which shows that the project *deserves* a

donation to the project, while low demanders pay “less” by refusing to contribute but being forced to indirectly pay something through the tax system. This forced payment is thought to reflect the fact that low demanders do receive some benefit (even if small) from the subsidized project.

55. *Id.* (“People who desire more of a collective good, but who do not place great value on the increase, may refuse to support a subsidy because they fear that they will bear a disproportionate share of the tax cost.”).

56. Saul Levmore, *Taxes as Ballots*, 65 U. CHI. L. REV. 387, 405 (1998). When someone donates to charity and takes the corresponding deduction, she “votes” for that charity to receive a federal subsidy equal to the foregone tax revenue. *Id.* (“[E]ach individual taxpayer’s choice, deduction, or ‘ballot’ . . . triggers a matching government contribution in the form of a reimbursement of part of the taxpayer-donor’s gift.”). Levmore acknowledges two common criticisms of this structure. First, allowing taxpayers to vote this way could be compared to a “poll tax” because one must make an out-of-pocket payment to trigger a subsidy. *Id.* at 405–06. Second, using a deduction (instead of a credit) gives more “votes” to higher-bracket taxpayers because of the upside-down effect of deductions. *Id.*

57. *See id.* at 411–12; David M. Schizer, *Subsidizing Charitable Contributions: Incentives, Information, and the Private Pursuit of Public Goals*, 62 TAX L. REV. 221, 229 (2009).

58. Levmore, *supra* note 56, at 406.

59. Schizer, *supra* note 57, at 229–42, 257–67. Although Levmore and Schizer focused on the charitable contributions deduction, their arguments are somewhat translatable to tax exemption: all a taxpayer needs to do to direct a subsidy to a given project is to start the requisite organization, or purchase goods and services from an existing organization.

60. COLOMBO & HALL, *supra* note 28, at 99.

61. *Id.* at 107. One might wonder why donations alone are not enough to fund the activity at an appropriate level. Colombo and Hall respond that voluntary donations are subject to the same free-rider problems that plague market provision, thus requiring a further subsidy from the government. *Id.* at 104–05.

subsidy.⁶² Colombo and Hall thus reason that donations signal worthiness for both the deduction and tax exemption.

C. Lingerin Questions

Although existing scholarship provides many valuable insights into the charitable tax subsidies, several questions linger. Namely, neither existing law nor current scholarship provides much guidance as to prioritizing which projects deserve subsidies. Sections 170 and 501 contain a list of purposes that are vague and broadly construed, and the heavy reliance on negative prohibitions (such as commerciality or private inurement) does little to clarify why some projects, but not others, merit subsidy.⁶³ Moreover, current law is confused as to whether an organization must help the poor to qualify for the subsidies.

One might wonder why these questions are troublesome in our pluralistic society. Given that citizens have many differing conceptions of the good, why not allow a wide range of groups to qualify for the charitable tax subsidies? Why take the time to explore the interaction of distributive justice and the charitable tax subsidies? This section briefly reiterates a point I have extensively addressed elsewhere: considering distributive justice, in addition to pluralism and efficiency, is necessary for a full understanding of the charitable tax subsidies.⁶⁴

1. Current Law Is Confused

First, current law is inconsistent as to whether organizations must help the poor to qualify for the subsidies. Groups serving enumerated purposes other than the catchall “charitable” purpose (such as educational and religious organizations) are not required to help the poor;⁶⁵ schools, for example, need not offer any scholarship assistance at all in order to qualify for the charitable tax subsidies.⁶⁶ This is so even though the Supreme Court has held that such organizations must be “charitable,”⁶⁷ and “charitable” organizations are sometimes required to help the poor. There is no explanation for distinguishing among the statutory purposes in this manner.⁶⁸ Moreover, only some “charitable” groups must assist the poor to qualify for subsidies. For example, organizations that provide housing assistance must do so.⁶⁹ Helping middle-class families to live in a given area (even if expensive, like Manhattan) is not enough to qualify for a subsidy unless the families are racial

62. *Id.* at 163–64.

63. Roger Colinvaux, *Charity in the 21st Century: Trending Towards Decay*, 11 FLA. TAX REV. 1, 17–18 (2011).

64. Fleischer, *supra* note 1, at 508 (“While identifying these advantages is a necessary and important contribution to our understanding of charitable-giving policy, avoidance of distributive justice concerns ignores the very purpose of charity: voluntary redistribution.”).

65. Colombo, *supra* note 34, at 343.

66. *Id.*

67. *Bob Jones Univ. v. United States*, 461 U.S. 574, 591–92 (1983).

68. *See supra* note 43.

69. *See Rev. Rul. 70-585*, 1970-2 C.B. 115.

minorities or the neighborhood is decaying.⁷⁰ In contrast, arts organizations do not need to help the poor to receive subsidies.⁷¹ And the law concerning whether healthcare organizations must offer reduced-cost services to the poor is a mess: technically, hospitals do not have to provide reduced-cost services on the theory that promoting the health of the community is enough of a benefit.⁷² That said, many scholars believe that hospitals are effectively required to help the poor, by either offering an open emergency room or accepting Medicaid.⁷³ Further, IRS rulings and court opinions essentially require other health organizations (like HMOs and pharmacies) to offer free or discounted medical care for the poor.⁷⁴

This confusion manifested itself quite publicly right after the September 11 attacks, when donors showered disaster relief groups such as the Red Cross with over \$2 billion.⁷⁵ In the past, such organizations were allowed to help only financially-needy victims. The IRS thus initially hesitated when such groups stated they would help families of all the victims, regardless of their financial circumstances. Public outcry ensued, causing the IRS to soften its stance and allow aid to nonneedy families if made “in good faith using objective standards.”⁷⁶

70. *Id.*

71. *See* *Goldsboro Art League, Inc. v. Comm’r*, 75 T.C. 337 (1980).

72. *See* Rev. Rul. 83-157, 1983-2 C.B. 94 (specialized hospitals without emergency rooms offering no free or reduced-cost services to the poor may qualify for exemption); Rev. Rul. 69-545, 1969-2 C.B. 117 (hospitals can qualify for exemption without offering inpatient care to indigent patients if they offer an open emergency room). That said, several states have begun challenging whether hospitals that do not offer free or reduced-cost services to the poor are eligible for property tax exemptions. *See, e.g., Provena Covenant Med. Ctr. v. Dep’t of Revenue*, 925 N.E.2d 1131, 1136 (Ill. 2010) (upholding the revocation of a hospital’s property tax exemption); John D. Colombo, *Provena Covenant: The (Sort of) Final Chapter*, 65 EXEMPT ORG. TAX REV. 489 (2010).

73. John D. Colombo, *The IHC Cases: A Catch-22 for Integral Part Doctrine, A Requiem for Rev. Rul. 69-545*, 34 EXEMPT ORG. TAX REV. 401, 408 (2001).

74. *See, e.g., IHC Health Plans, Inc. v. Comm’r*, 325 F.3d 1188, 1200–02 (10th Cir. 2003) (denying exempt status to an HMO that did not offer free or below-cost medical services); *Fed’n Pharmacy Servs., Inc. v. Comm’r*, 625 F.2d 804, 809 (8th Cir. 1980) (denying exemption to a pharmacy that sold drugs and other items at cost to the poor and elderly); John D. Colombo, *The Failure of Community Benefit*, 15 HEALTH MATRIX 29, 30–37 (2005) (detailing various rulings denying tax exempt status to HMOs). In contrast, art galleries and community theaters need not reduce fees to the poor in order to qualify, *Goldsboro*, 75 T.C. at 344, yet groups that provide other recreational facilities for adults (such as health clubs) are generally required to do so. *See* Colombo, *supra* note 34, at 358–60, 384. In at least one instance, however, an ice rink received exempt status with little more than vague plans to offer some sort of program for disadvantaged children. I.R.S. Priv. Ltr. Rul. 05-32-058 (May 18, 2005) (“A . . . Program shall be offered to provide disadvantaged youth in the local area the opportunity to learn to skate and to attend a day program at Ice Arena.”). In that case, the Service held that simply providing recreation on a nondiscriminatory basis promoted social welfare, thus meriting a subsidy. *Id.*

75. *See generally* Loren Renz & Leslie Marino, *Giving in the Aftermath of September 11: Final Update on the Foundation and Corporate Response*, in SEPTEMBER 11: THE PHILANTHROPIC RESPONSE 85 (Rick Schoff ed., 2004), available at http://foundationcenter.org/gainknowledge/research/pdf/9_11updt04.pdf.

76. I.R.S. Notice 01-78, 2001-2 C.B. 576; *see also* JAMES J. FISHMAN & STEPHEN SCHWARZ, TAXATION OF NONPROFIT ORGANIZATIONS: CASES AND MATERIALS 143–47 (2d ed. 2006)

2. Recent Political Developments Raise Distributive Concerns

A number of recent political developments further highlight the need to address distributive justice directly. First, distributional issues have attracted the attention of a number of various policymakers. The issue of charitable aid to the poor has come up in several recent congressional hearings,⁷⁷ with both lawmakers and witnesses suggesting that incentives for charities to help the poor should be increased.⁷⁸ Outside of Congress, several commentators have echoed these concerns. Former Labor Secretary Robert B. Reich, for instance, has argued that the charitable sector should do more to help the less fortunate and promote equality.⁷⁹ The current debate about university endowments reflects these concerns,⁸⁰ as do state challenges to property tax exemption for nonprofit hospitals: the Illinois Supreme Court recently revoked the state property tax exemption of a prominent nonprofit hospital on the grounds that it did not provide adequate charitable care.⁸¹ And early versions of the Affordable Care Act required hospitals to offer charity care,⁸² although such standards were removed from the final bill.⁸³

(summarizing the status of disaster relief as a charitable purpose); David Barstow & Diana B. Henriques, *I.R.S. Makes an Exception on Terror Aid*, N.Y. TIMES, Nov. 17, 2001, at B1.

77. *Tax-Exempt Charitable Organizations: Hearing Before the Subcomm. on Oversight of the H. Comm. on Ways and Means*, 110th Cong. 4–5, 18–21 (2007) (stating that one goal of the hearings will be to “review . . . charities’ efforts to assist diverse communities”); *To Examine Whether Charitable Organizations Serve the Needs of Diverse Communities: Hearing Before the Subcomm. on Oversight of the H. Comm. on Ways and Means*, 110th Cong. 4 (2007) (statement of Rep. John Lewis, Chairman, Subcomm. on Oversight of the H. Comm. on Ways and Means) (“[T]he resources of the charitable community do not exactly match our needs. Sadly those with the greatest need are not always served.”).

78. *See To Examine Whether Charitable Organizations Serve the Needs of Diverse Communities: Hearing Before the Subcomm. on Oversight of the H. Comm. on Ways and Means*, 110th Cong. 57 (2007) (statement of Rep. Xavier Becerra, Member, Subcomm. on Oversight of the H. Comm. on Ways and Means) (“So, you could probably incent noble activity by providing a better return for your contribution . . . if they are directed at the general welfare, or direct general welfare of serving those who are in need?”).

79. *See* Stephanie Strom, *Big Gifts, Tax Breaks and a Debate on Charity*, N.Y. TIMES, Sept. 6, 2007, at A1; Robert B. Reich, *Revamp Deductions for the Rich’s ‘Charities,’* PITT. TRIB.-REV. (Oct. 7, 2007), http://triblive.com/x/pittsburghtrib/opinion/columnists/guests/s_531422.html#axzz2u6U7CSWa (proposing that donors be allowed to deduct the full amount of contributions to agencies that help the poor, but only half the amount of contributions to other nonprofits); *cf.* Pablo Eisenberg, Op-Ed., *What’s Wrong with Charitable Giving—and How to Fix It*, WALL ST. J., Nov. 9, 2009, at R1 (urging that foundations and wealthy donors direct more of their giving to the poor and disadvantaged).

80. *See* Colombo, *supra* note 43, at 13–14 for a concise overview of this debate.

81. *Provena Covenant Med. Ctr. v. Dep’t of Revenue*, 925 N.E.2d 1131, 1146–51 (Ill. 2010).

82. Robert Pear, *Hospitals Mobilizing to Fight Proposed Charity Care Rules*, N.Y. TIMES, May 31, 2009, at A12.

83. *See* I.R.C. § 501(r) (2012) (provisions of the Affordable Care Act that affect nonprofit hospitals); *New Requirements for 501(c)(3) Hospitals Under the Affordable Care Act*, I.R.S. (Dec. 31, 2013), <http://www.irs.gov/Charities-&-Non-Profits/Charitable-Organizations/New-Requirements-for-501%28c%29%283%29-Hospitals-Under-the-Affordable-Care-Act> (additional requirements affecting nonprofit hospitals as of March 23, 2010).

Second, a number of proposals to reform the charitable deduction are currently circulating: replacing the deduction with a credit, implementing a floor (such as 2% of adjusted gross income) under which contributions would not be deductible, and limiting all itemized deductions (including the charitable deduction) to 28% regardless of a donor's bracket.⁸⁴ Any such change would likely cause some individuals to donate more and others to donate less.⁸⁵ Because donors of different income levels tend to support different causes, these changes would likely affect the level of funding flowing to various types of charitable organizations. These changes will thus create both winners and losers, and we need a way to evaluate whether the pattern of winners and losers is acceptable.⁸⁶

D. The Role of Distributive Justice

Despite these lingering distributive questions, current scholarship on the charitable tax subsidies largely ignores distributive issues.⁸⁷ To fill that gap, this

84. See ROGER COLINVAUX, BRIAN GALLE & EUGENE STEUERLE, EVALUATING THE CHARITABLE DEDUCTION AND PROPOSED REFORMS 12–14 (2012) (collecting and evaluating these proposals), available at <http://www.urban.org/uploadedpdf/412586-evaluating-the-charitable-deduction-and-proposed-reforms.pdf>.

85. See CONG. BUDGET OFFICE, PUB. NO. 4030, OPTIONS FOR CHANGING THE TAX TREATMENT OF CHARITABLE GIVING VIII (2011).

86. A rich body of economic literature, for example, addresses the potential impact of tax changes on giving patterns. See, e.g., Gerald E. Auten, Holger Sieg & Charles T. Clotfelter, *Charitable Giving, Income, and Taxes: An Analysis of Panel Data*, 92 AM. ECON. REV. 371 (2002); Jon M. Bakija, William G. Gale & Joel B. Slemrod, *Charitable Bequests and Taxes on Inheritances and Estates: Aggregate Evidence from Across States and Time*, 93 AM. ECON. REV. 366 (2003); Jon Bakija & Bradley T. Heim, *How Does Charitable Giving Respond to Incentives and Income? New Estimates from Panel Data*, 64 NAT'L TAX J. 615 (2011); Jon Bakija, *Tax Policy and Philanthropy: A Primer on the Empirical Evidence for the United States and Its Implications*, 80 SOC. RES. 557 (2013); Michael J. Brunetti, *The Estate Tax and Charitable Bequests: Elasticity Estimates Using Probate Records*, 58 NAT'L TAX J. 165 (2005); William C. Randolph, *Dynamic Income, Progressive Taxes, and the Timing of Charitable Contributions*, 103 J. POL. ECON. 709 (1995); Michelle H. Yetman & Robert J. Yetman, *How Does the Incentive Effect of the Charitable Deduction Vary Across Charities?*, 88 ACCT. REV. 1069 (2013). An underlying normative theory, however, is necessary to judge the acceptability of these estimated changes.

87. To be fair, that inattention is largely purposeful. Until the 1970s and 1980s, the traditional rationale for subsidizing charities was that they did “good” things—activities such as relieving the government of burdens it normally bears, offering creative solutions to societal problems, presenting alternative viewpoints in the arts and culture, boosting pluralism and experimentation, and promoting altruism. These justifications, however, involve value-based judgments about which activities are “good.” For example, which burdens should the government bear? Which societal problems should we find solutions for? Why are alternative viewpoints and experimentation worthy?

Beginning in the seventies and eighties, scholars attempted to avoid these messy questions by creating objective tests for determining which activities should receive subsidies. Some scholars focus on economic rationales: these theorists would limit the subsidies to public goods that suffer from market and governmental failure. Other scholars focus on pluralism and would subsidize any project that is not self-benefiting and has a

series analyzes each theory of distributive justice common to tax scholarship to see how it would resolve the foregoing issues.

On one hand, considering what various theories of distributive justice imply for the charitable tax subsidies seems obvious: the charitable tax subsidies are inherently redistributive. Some taxpayers pay more than otherwise (in the form of higher taxes or reduced benefits elsewhere) so that charitable organizations and their beneficiaries can receive a subsidy.⁸⁸ The subsidies are part of the tax system,⁸⁹ and the importance of distributive justice is unquestioned in many other tax policy debates.⁹⁰

On the other hand, some readers may question the utility of this project on the grounds that using any of these insights would require us to choose among competing theories of distributive justice—an act at odds with our pluralistic society. As an initial matter, we should know what these insights are before we reject them wholesale. We should at least have a sense of the distributive justice landscape before we can thoughtfully decide what weight to give it, and whether and how to use any of these insights.

Moreover, identifying the implications of various theories of distributive justice is useful even if we acknowledge that we live in a pluralistic world where citizens hold differing conceptions of “the good” and of distributive justice more specifically. This is so for two reasons. First, recognizing we live in a pluralistic world does not necessarily mean that the charitable tax subsidies should themselves be pluralistic (that is, fund anything anyone considers “good”). Respecting the former means that if we subsidize one point of view, we should also subsidize the other (for example, if we subsidize traditional college-prep schools, we should also subsidize Waldorf schools). This does not, however, necessarily mean that we have to subsidize any private school in the first place. Nondiscrimination could also mean that we only subsidize those projects about which there is agreement among

threshold level of support from other individuals. Existing scholarship would thus have us believe that the only questions one needs to ask about what should be subsidized are objective: Is the project a pure or impure government good? Does it suffer from market and governmental failure? Does the project benefit the donor? Does it have support from individuals other than the donor? As I have extensively detailed elsewhere, however, we cannot rely solely on these objective tests when assessing the charitable tax subsidies. *See* Fleischer, *supra* note 1, at 538–48.

88. *See* Eric M. Zolt, *Tax Deductions for Charitable Contributions: Domestic Activities, Foreign Activities, or None of the Above*, 63 HASTINGS L.J. 361, 374 (2012).

89. *See, e.g.*, Thomas D. Griffith, *Theories of Personal Deductions in the Income Tax*, 40 HASTINGS L.J. 343, 345 (1989) (“[A] satisfactory tax policy must make its underlying ethical assumptions and distributional goals explicit.”).

90. *See, e.g.*, Alstott, *supra* note 6, at 470–71; William D. Andrews, *Fairness and the Personal Income Tax: A Reply to Professor Warren*, 88 HARV. L. REV. 947, 947–53 (1975); Bankman & Griffith, *supra* note 6, at 1907; Lily L. Batchelder, *What Should Society Expect from Heirs? The Case for a Comprehensive Inheritance Tax*, 63 TAX L. REV. 1, 2 (2009); Blum & Kalven, *supra* note 20, at 468–79, 486–506; Barbara H. Fried, *Fairness and the Consumption Tax*, 44 STAN. L. REV. 961, 962 (1992); Graetz, *supra* note 26, at 274–78; McCaffery, *supra* note 26, at 291–92; Eric Rakowski, *Transferring Wealth Liberally*, 51 TAX L. REV. 419, 430 (1996); Shaviro, *supra* note 26, at 125; Alvin Warren, *Would a Consumption Tax Be Fairer Than an Income Tax?*, 89 YALE L.J. 1081, 1082 (1980); Zelenak, *supra* note 26, at 1149–72.

citizens who hold differing views. To illustrate, imagine that one group of citizens considers opera and early childhood education to be good and modern dance to be bad. Another group of citizens considers modern dance and early childhood education to be good, but vehemently opposes opera. Pluralism could mean subsidizing only early childhood education, which both groups consider to be good, rather than all three activities. Second, we live in a world of scarce resources. Even if we decide as a matter of theory to fund every project considered worthy under any theory of distributive justice, there are times when tradeoffs must be made. Many current proposals to modify the charitable deduction, for example, will likely decrease the tax subsidies to certain organizations. If different proposals will impact different organizations, how do we choose among them?

For these reasons, respecting pluralism does not necessarily mean that we should (or even can) ignore questions of distributive justice. Nor does respecting efficiency mean we should ignore such questions.⁹¹ Instead, we should explore the insights that various theories of distributive justice hold for the charitable tax subsidies so that we can fully consider how to integrate pluralism, efficiency, and distributional considerations.

II. WHY BENEFICIARY UTILITY MATTERS

The efficiency theorists discussed above essentially offer a utilitarian justification for the existence of the charitable tax subsidies (although they do not label it as such) that focuses on donor utility.⁹² According to their view, the subsidies' role in satisfying the preferences of donors is utility-enhancing. They and other theorists have also identified additional aspects of donor utility that are likely enhanced by the charitable tax subsidies. The donor, for example, likely experiences an increase in utility from the very act of giving.⁹³

91. Indeed, much empirical economic work on the charitable subsidies explicitly notes that distributive justice should also be considered. Economist Charles T. Clotfelter, for example, has stated that “[a]lthough few would argue that redistribution is the most important justification for maintaining nonprofit institutions, distributional impact remains one significant consideration, as it is in most areas of public policy.” Charles T. Clotfelter, *The Distributional Consequences of Nonprofit Activities*, in WHO BENEFITS FROM THE NONPROFIT SECTOR? 1, 3 (Charles T. Clotfelter ed., 1992).

92. See *supra* Part I.B.

93. See, e.g., Louis Kaplow, *A Note on Subsidizing Gifts* 1–2 (Nat’l Bureau of Econ. Research, Working Paper No. 4868, 1994), available at <http://www.nber.org/papers/w4868.pdf>. Specifically, Kaplow argues that charitable giving increases the utility of both the donor and donee, but that donors undervalue the increase in donee utility. He notes that for altruistically-minded donors, giving increases the donor’s utility both directly (the gift must increase donor utility in its own right, or else the donor would have spent his money elsewhere) and indirectly (the donor derives utility from the increase in donee utility), as well as increasing donee utility in its own right. *Id.* But since donors only account for the increase in their own utility, they do not account for the positive externality stemming from the increase in donee utility felt by the donees alone. Kaplow thus reasons that gift giving generates a positive externality that is unaccounted for by donors and that justifies subsidizing charitable gifts regardless of whether the gift funds a public good or furthers redistribution. *Id.* For a summary of contrary views, such as the argument that charitable giving and paying taxes each increases

Altruistically-motivated donors may experience an increase in utility when other donors give to a cause they support.⁹⁴ And some have argued that the charitable sector as a whole “increases utility” without regard to distributive issues because it enhances the size and scope of the sector.⁹⁵

The insights of these theories—that subsidizing charitable giving through the tax system enhances societal welfare by enlarging the pie for society overall⁹⁶—are valuable. But as some efficiency scholars recognize, these theories do not focus on the distributional aspects of the charitable surplus (the positive externalities) generated by giving.⁹⁷ That is, they have ignored how the pie is distributed. But given the fact that charitable giving buys benefits for others via the funding of public goods, it is not enough to look simply at the utility and preferences of donors without also evaluating the utility and preferences of the charitable beneficiaries. The latter must also be considered in order to assess, as a distributive matter, whether the resulting distribution of externalities is just or not.⁹⁸ This is especially

utility to the same extent, see Brian Galle, *The Role of Charity in a Federal System*, 53 WM. & MARY L. REV. 777, 830–31 (2012).

94. LOUIS KAPLOW, *THE THEORY OF TAXATION AND PUBLIC ECONOMICS* 271 (2008) (“[W]ith charitable contributions it seems important to consider another sort of positive externality, that gifts from one donor to a particular donee may simultaneously benefit other donors. This possibility would arise, for example, if multiple donors were altruistic toward a single set of donees, say, the poor or future sufferers from some disease.”).

95. See Kaplow, *supra* note 93, at 8 (“A frequently offered rationale for subsidy to charities also invokes the concept of externalities. It relies on the assumption that institutions receiving gifts use them in a way that creates positive externalities, as with medical research.”).

96. This analogy is commonly employed when discussing overall amounts of societal welfare. See, e.g., DANIEL M. HAUSMAN & MICHAEL S. MCPHERSON, *ECONOMIC ANALYSIS, MORAL PHILOSOPHY, AND PUBLIC POLICY* 145 (2d ed. 2006); RICHARD A. EPSTEIN, *TAKINGS: PRIVATE PROPERTY AND THE POWER OF EMINENT DOMAIN* 3–6 (1985); Edward J. McCaffery & Jonathan Baron, *The Political Psychology of Redistribution*, 52 UCLA L. REV. 1745, 1746 (2005).

97. See Strnad, *supra* note 52, at 71.

98. I emphasize that I am not rejecting the importance of using efficiency when evaluating tax policy, or the insights of optimal tax policy. I am merely trying to tease out certain distributive aspects of charitable-giving policy that complement the insights of efficiency analysis and the use of economics. As applied to charitable donations, for example, the optimal tax analysis framework seeks to determine at what level charitable gifts should be subsidized in order to maximize a given social welfare function, taking into account labor tax rates, cash transfers, and government provision of public goods. See Bakija, *supra* note 86, at 578. My project complements this work in two ways. First, optimal tax analysis requires a choice of distributive function. More specifically, most optimal tax analysis seeks to maximize a utilitarian social welfare function (reflecting a utilitarian theory of distributive justice). See N. Gregory Mankiw, Matthew Weinzierl & Danny Yagan, *Optimal Taxation in Theory and Practice* 3 (Nat’l Bureau of Econ. Res., Working Paper No. 15071, June 2009), available at <http://www.nber.org/papers/w15071>. Optimal tax analysis, however, can incorporate not only other types of welfare functions (reflecting alternative welfarist theories of distributive justice), but can also be configured to reflect nonwelfarist theories of justice (which Saez & Stantcheva refer to as “generalized social welfare weights”). Emmanuel Saez & Stefanie Stantcheva, *Generalized Social Marginal Welfare Weights for Optimal Tax Theory* 4 (Nat’l Bureau of Econ. Res., Working Paper No. 18835, Feb. 2013), available at <http://www.nber.org/papers/w18835>. My hope is that the series as a

true when considering the distributive effects of tax exemption, since exempt organizations may or may not have donors.

For purposes of using utilitarianism to evaluate that distribution, then, one can think of the charitable sector as enhancing utility in an additional manner distinct from those celebrated by the efficiency theorists: the increase in utility resulting from the inherent income redistribution from some individuals to others via the charitable tax subsidies.⁹⁹ Put another way, there are two layers of utility that must be considered in assessing the effects of the charitable tax subsidies. The first (a task I leave to others) is to somehow measure and assess the various utility gains to donors, and to society in general, from having a vibrant charitable sector.¹⁰⁰ The second task (which is my project) is to analyze the inherent redistribution that occurs via the charitable tax subsidies. This involves identifying, to the extent possible, the increase in beneficiary utility from subsidized charity.

The “upside-down subsidy” critique of the charitable deduction highlights this point. According to that critique, the charitable deduction is unfair because it grants a larger deduction to higher-bracket taxpayers.¹⁰¹ Most responses to the upside-down subsidy argument have suggested equalizing the tax benefits to donors, regardless of income bracket, via a credit or matching grant system.¹⁰² But this partially misses the point, for it ignores the fact that even if upper-bracket taxpayers do receive a larger deduction than lower-bracket taxpayers, the diminished utility of the donor must still be compared with the increased utility of the beneficiary to

whole will shed light onto what should go into that distributive function (For example, should it weigh more heavily the interests of the poor? Does any overlap exist among the various theories of distributive justice when it comes to the charitable tax subsidies?). Second, the optimal tax analysis keys off of individuals’ welfare functions. An optimal tax framework that used utilitarianism, for example, would weigh more heavily the utility of a poor person than a rich person; a framework using luck egalitarianism would weigh more heavily gains to those who are worse off due to chance, not choice. *Id.*; see also Mankiw et al., *supra*. Because the charitable tax subsidies flow to groups, however, it is necessary to know which groups act as conduits to these individuals. If an optimal tax framework suggests that the optimal subsidy for charitable transfers is $n\%$ in order to maximize the welfare of a given group of individuals (say, poor people with a high marginal utility of income), we need to know which charitable transfers assist members of that group. Moreover, it may be the case that an optimal tax analysis would suggest that organizations that benefit different groups of people should be subsidized at different rates. What my project adds, therefore, is more knowledge about the content of the distributive function when charitable transfers are assumed to be heterogeneous.

99. Indeed, Kaplow recognizes gifts that aid donees who are worse off than donors likely increase social welfare more than other charitable gifts. KAPLOW, *supra* note 94, at 271 (“Furthermore, to the extent that ultimate beneficiaries are substantially less well off than donors (compare gifts to aid the poor to contributions to the symphony), the contribution to social welfare on account of voluntary redistribution would be greater.”).

100. Of course, it may also be the case that charitable giving creates disutilities as well. See *infra* Part IV.A.3.

101. *E.g.*, McDaniel, *supra* note 46, at 395 (“[I]n a progressive rate system, the benefits of the deduction are distributed regressively up the income scale, thereby negating in whole or in part the fundamental assumption of a progressive tax system.”).

102. *E.g.*, *id.* at 405–06 (arguing that a matching grant system will enhance equity since “each individual’s contribution will be matched on the same basis regardless of his income tax bracket”).

assess whether overall utility has increased or decreased. All that the upside-down subsidy argument tells us is that under a traditional utilitarian analysis, for some taxpayers, we must determine how much their utility diminishes when they give up sixty-five cents for each dollar donated, while for others, we must determine how much their utility decreases when they give up seventy-five cents (or some other portion) for each donated dollar. But, in both cases, we must still compare the utilities of the donor and the beneficiary.¹⁰³ Utilitarianism thus tells us that the upside-down subsidy argument cannot be fully assessed without considering the beneficiaries.¹⁰⁴ Along those lines, the following two Parts examine beneficiary utility from the charitable tax subsidies, using the definitions of utility most common in legal scholarship.

III. UTILITY AS INCOME

Although the philosophy literature contains a longstanding debate about what “utility” or “well-being” actually is,¹⁰⁵ legal scholars have traditionally tried to avoid specifically defining what constitutes utility, happiness, or well-being. Instead, legal scholars use proxies such as liberty and money, which are thought to influence happiness or well-being, regardless of the precise way in which happiness or well-being is defined.¹⁰⁶ To that end, utilitarianism as traditionally applied in tax policy uses income or wealth as a proxy for utility and assumes the declining marginal utility thereof; I shall call this “traditional utilitarianism.” This Part will start by outlining the conventional wisdom concerning traditional utilitarianism and the charitable tax subsidies held by many. It will then explore the implications of

103. A few prior scholars have argued that a full response to the upside-down subsidy critique requires a consideration of charitable beneficiaries. Bittker, for example, suggested that the deduction increases progressivity “by transferring funds from rich taxpayers to those in more moderate circumstances.” Bittker, *supra* note 12, at 55–56.

104. If, for example, donor utility decreases less than beneficiary utility increases under our current system, then the upside-down subsidy argument loses some force, meaning that the current system increases overall utility. It might still be the case, however, that a credit (whereby all donors “gave up” the same portion of each dollar donated) would generate even more overall utility.

105. Does it mean the mental state of happiness or pleasure? Early utilitarians such as Bentham and Mill defined utility as such. HAUSMAN & MCPHERSON, *supra* note 96, at 145; KYMLICKA, *supra* note 10, at 13. Or perhaps it means “non-hedonistic mental-state utility,” which would encompass a range of valuable mental states (such as hard work) even if those states are not pleasurable per se? KYMLICKA, *supra* note 10, at 14. Or is well-being unrelated to mental states, and instead means that one’s preferences are satisfied? If so, must all preferences be satisfied? What if satisfying a given preference does not ultimately contribute to that individual’s welfare due to misinformation (e.g., not knowing the pizza one craves is rancid) or adaptive preferences (e.g., the happy slave)? Or must only informed preferences be satisfied? *Id.* at 14–20. Lastly, perhaps well-being consists of neither mental states nor preference satisfaction, but of living one’s life according to an objective list of criteria (cultivating honesty or virtue, for example), whether or not so doing makes one subjectively happy or is what one desires to do.

106. MURPHY & NAGEL, *supra* note 10, at 52.

work challenging the extent to which individuals actually experience declining marginal utility of income, while continuing to equate utility with income.

This exploration ultimately challenges the conventional wisdom. Operationalizing traditional utilitarianism is far too difficult to support the accepted notion that “enough” giving redistributes downward to further utilitarian ideals, regardless of at what income level this occurs. In contrast, this Part shows that the most this type of analysis supports is that subsidizing charitable groups that provide basic services to the very poor is consistent with these ideals.¹⁰⁷

A. Traditional Declining Marginal Utility and the Charitable Tax Subsidies

The traditional application of utilitarian theory to tax policy (“traditional utilitarianism”) makes three assumptions. The first is that, for purposes of tax policy, measuring income or wealth is the best proxy for measuring utility.¹⁰⁸ The second assumption is that each additional dollar an individual has is worth subjectively less than the previous dollar, a phenomenon commonly referred to as the declining marginal utility (DMU) of resources.¹⁰⁹ As applied to a given individual, this suggests that an extra dollar is subjectively more valuable to someone with an income of \$10,000 than to someone with an income of \$100,000. The final assumption is that all individuals have identical utility curves (that is, all individuals with an income of \$10,000 value their 10,001st dollar equally, all individuals with an income of \$100,000 value their 100,001st dollar equally, and so on).¹¹⁰

Together, these assumptions lead to the argument that downward resource redistribution maximizes total societal utility.¹¹¹ So long as taking a dollar from a rich person decreases her utility less than it increases the utility of the poor person to whom that dollar is given, the transfer has increased overall utility.¹¹² This line

107. In a sense, this reasoning is arguing that act utilitarianism is unworkable in the charitable-giving context and that a broad rule (only organizations helping the poor should be subsidized) is more effective at increasing overall utility. I take no position, however, in the larger debate about the superiority of rule or act utilitarianism, other than to note that I believe both have flaws. For an accessible overview of this debate, see Larry Alexander, *Pursuing the Good—Indirectly*, 95 ETHICS 315 (1985) (terming rule utilitarianism “indirect utilitarianism”).

108. Adam H. Rosenzweig, *Harnessing the Costs of International Tax Arbitrage*, 26 VA. TAX REV. 555, 576 n.37 (2007).

109. Bankman & Griffith, *supra* note 6, at 1947; Sarah B. Lawsky, *On the Edge: Declining Marginal Utility and Tax Policy*, 95 MINN. L. REV. 904, 906 nn.13–14, 915–17 (2011); Shavero, *supra* note 26, at 137.

110. Bankman & Griffith, *supra* note 6, at 1947; Lawsky, *supra* note 109, at 917–19; Lawrence Zelenak & Kemper Moreland, *Can the Graduated Income Tax Survive Optimal Tax Analysis?*, 53 TAX L. REV. 51, 51 (1999). *But see* Blum & Kalven, *supra* note 20 (questioning the assumption that all individuals have identical utility curves).

111. *See* Staudt, *supra* note 8, at 940–41. One criticism of this conclusion is that it ignores the disincentives stemming from high tax rates. The optimal tax analysis literature thus seeks to identify the rate structure that best balances progressivity and minimal economic disincentives. *See, e.g.*, J.A. Mirrlees, *An Exploration in the Theory of Optimum Income Taxation*, 38 REV. ECON. STUD. 175 (1971).

112. DAVID F. BRADFORD, *UNTANGLING THE INCOME TAX* 153 (1986); Griffith, *supra* note

of reasoning has thus been used to justify exemptions for the poor and a progressive rate structure;¹¹³ the latter allows an increasingly greater share of resources to be taken from those with “more” in order to fund projects that help those with “less.”¹¹⁴

1. The Conventional Wisdom

Based on the foregoing, the conventional wisdom is that any charitable giving that redistributes from the donor to someone less wealthy (much like the goal of progressive taxation itself) is consistent with utilitarian principles: the dollar donated by a wealthier individual reduces her utility less than the utility of the individual who receives a dollar’s worth of charitable goods or services is increased.¹¹⁵ To determine which activities merit a subsidy, one would not look at the subjective “goodness” of the activity, but rather the relative income levels¹¹⁶ of the donors and those benefiting from the subsidy.¹¹⁷

In addition to justifying subsidies for groups that help the poor (such as soup kitchens and tutoring programs in low-income areas), this would also justify subsidizing organizations such as museums, theaters, and universities, where many attendees (even if middle- or upper-middle-class) are less wealthy than the benefactors.¹¹⁸ The conventional wisdom thus supports current law, given that such organizations already qualify for the charitable subsidies. Additionally, it would

8, at 1363. If fully implemented, utilitarianism would lead to complete income equality: individuals above the mean would be taxed at a rate of 100%, while cash transfers would be made to those below the mean to lift them to that point. BRADFORD, *supra*, at 154; Bankman & Griffith, *supra* note 6, at 1947–48; Staudt, *supra* note 8, at 942. This, of course, has never been seriously considered for both practical and political reasons. *Id.*

113. *E.g.*, Bankman & Griffith, *supra* note 6, at 1966–67; Zelenak & Moreland, *supra* note 110, at 51–53.

114. This argument and its underlying assumptions are, not surprisingly, subject to criticism. *See, e.g.*, Blum & Kalven, *supra* note 20; Lawskey, *supra* note 109. Many of this Article’s criticisms of using utilitarianism to assess the charitable tax subsidies would also apply to using utilitarianism to justify increasing marginal rates.

115. *See supra* note 17. It would not be enough to say that overall utility is increased if, looking at the nonprofit sector as a whole, donors (as a group) tend to be wealthier than beneficiaries (as a group). It could be the case, for example, that upper-income donors only donate to groups benefiting other upper-income individuals. Upper-income individuals shuffling money among themselves does not increase utility of the type supposed by the conventional wisdom.

116. This analysis uses income as a proxy for utility instead of wealth because it discusses an aspect of the income tax. The same principles would likely apply, however, to an analysis of charitable giving under a wealth tax: the downward redistribution from someone with more accumulated wealth to someone with less accumulated wealth has the same utilitarian effect. For an exploration of charitable giving and the estate tax (which is the closest we come to having a wealth tax), see generally Fleischer, *supra* note 29.

117. In that sense, a utilitarian approach complements those scholars seeking to exclude subjective value judgments from determinations of what should be considered charitable. (Of course, the a priori adoption of utilitarianism is its own value judgment.)

118. *See generally* WHO BENEFITS FROM THE NONPROFIT SECTOR?, *supra* note 91 (presenting papers examining the distributional aspects of nonprofits in a variety of subsectors).

reject as unfounded the argument that such groups should not be subsidized because they do not “help the poor.”¹¹⁹

Further, the conventional wisdom concretely answers the question of when activities benefiting the nonpoor should be considered charitable, a source of much confusion under current law.¹²⁰ To illustrate, groups that subsidize housing for the middle class in expensive neighborhoods do not qualify for exemption under current law unless they improve racial diversity in those neighborhoods.¹²¹ Under the conventional wisdom, groups that assist middle-class individuals to live in areas otherwise out of reach, such as Manhattan, would be subsidized so long as there was some downward redistribution. This type of reasoning similarly suggests that healthcare organizations need not provide free or reduced-cost services to the poor in order to qualify for the subsidies (another area of current controversy), so long as some downward redistribution occurred.

On the other hand, focusing solely on downward redistribution also means that an organization would not be subsidized if its benefactors are of roughly the same income class as its beneficiaries. This might, for example, impact churches and other houses of worship,¹²² as much evidence suggests that these types of organizations are highly segregated by income.¹²³ This implies that a portion of redistribution within churches is horizontal instead of vertically downward, which would not increase utility in the sense discussed above. On the other hand, many—but not all—churches provide social services to less fortunate congregations or to the less fortunate in general. The appropriate subsidy to a church should thus reflect the fact that only a portion of its budget is spent assisting those with less income.¹²⁴

This might also impact some social service organizations, since evidence suggests that donative support for these groups increases as one’s income decreases.¹²⁵ Whether such groups continue to receive a full subsidy would thus turn on the extent to which supporters are better off than the beneficiaries, or roughly the same. We can imagine, for example, a youth baseball team in a lower-middle-class area where donors to the team are financially comparable to the families whose children play on the team. Under a redistribution-focused application of utilitarianism, this would not merit a subsidy.

119. Fleischer, *supra* note 1, at 549–53 (describing such arguments).

120. For example, until IRS clarification after the September 11 terrorist attacks, it was unclear whether material assistance to the nonpoor in the form of disaster relief was considered charitable. FISHMAN & SCHWARZ, *supra* note 76, at 143–47.

121. Rev. Rul. 70-585, 1970-2 C.B.115.

122. Like other charities, churches may well offer benefits beyond those given to their members—for example, moral training and community building. This of course raises the issue of taking into account the increased utility to nonparticipants. *See infra* Part III.A.2.d.

123. Jeff E. Biddle, *Religious Organizations*, in WHO BENEFITS FROM THE NONPROFIT SECTOR?, *supra* note 91, at 92, 109 (“American congregations tend to be segregated on the basis of income . . .”).

124. For a discussion regarding measurement issues of this stripe, see *infra* Conclusion.

125. Gerald E. Auten, Charles T. Clotfelter & Richard L. Schmalbeck, *Taxes and Philanthropy Among the Wealthy*, in DOES ATLAS SHRUG? THE ECONOMIC CONSEQUENCES OF TAXING THE RICH 392, 403–06 (Joel B. Slemrod ed., 2000).

2. Challenges to the Conventional Wisdom

The conventional wisdom outlined above assumes that we can identify whether or not charitable dollars flow down the income spectrum. Even with respect to the income redistribution triggered by a charitable contribution and the charitable deduction, operationalizing these insights proves so difficult as to render them meaningless with respect to anything other than donative organizations providing basic services to the very poor. The conventional wisdom breaks down further when applied to exemption, which is the primary subsidy for nondonative organizations.

a. Comparing the Donor and Beneficiary in Groups Funded by Donations and Providing Free Services

Under the conventional wisdom, charitable transfers from one specific individual to another that enhance the overall utility of those two individuals merit a subsidy under the charitable deduction.¹²⁶ The problem is that, by definition, charitable contributions are from an individual to an organization,¹²⁷ contributions from one individual to another are not deductible.¹²⁸ So how do we know if the contribution is, in fact, benefiting one further down the income scale? To tease this out, we can start by focusing solely on the relationship between the donor (that is, the individual writing the check to the charity in question) and donee (here meaning the recipient charity's beneficiaries), ignoring for the moment that some redistribution may occur to and from others as well.¹²⁹

Imagine a charity funded entirely by voluntary donations whose beneficiaries all have exactly the same income. Perhaps the charity teaches children living in a poor neighborhood to play tennis, and each child's family has an income of \$25,000 per year. How should we determine whether this group redistributes downwards? The simple answer is that it redistributes downwards when it receives donations from individuals with incomes above \$25,000. In theory, then, donations from such individuals should be deductible, and that portion of the group's income that mirrors the portion of its donors above that income level should be tax-exempt. In contrast, donations from individuals with incomes under \$25,000 would not be deductible¹³⁰ since they would not enhance utility as defined solely by the concept of declining marginal utility.

126. *See supra* Part III.A.1

127. The issue of corporate contributions is beyond the scope of this Article. And distributions from a foundation or a charitable trust are ultimately distributions from its founder.

128. *See* I.R.C. § 170(c) (2012) (defining a "charitable contribution" as a gift "to or for the use of" one of five types of organizations).

129. Although this is an admittedly narrow focus, it is a logical starting point given that many prior discussions of the charitable deduction and utilitarianism focused solely on the donor and donee and ignored others. *See* Bittker, *supra* note 12, at 55–56. Although Bittker does not specifically cast his argument in terms of utility, his argument implies an underlying utilitarian framework based on declining marginal utility. *Id.*

130. Of course, this is assuming that they itemize, which is unlikely though not impossible at such a low-income level.

This seems odd. We generally think of the charitable deduction as providing a benefit to groups that engage in activities that somehow benefit society. Why should the activities of a group be deemed beneficial when Bob (with an income of \$100,000) contributes to it but not Anna (with an income of \$20,000)?¹³¹ The answer, of course, is that one contribution is thought to increase utility while the other doesn't. But our system of tax subsidies is based on the activities of groups, not individuals. Is the group doing something good, or not? Maybe one response is that the existence of the group itself enhances utility (even if Anna's donation itself does not increase utility in the way imagined by DMU) if "enough" of the donations it receives increase utility in that manner.

To that end, one can imagine three alternative rules for judging whether enough of the group's donations redistribute downward, so that all donors to it are treated similarly. The most stringent would be to only subsidize the group if *every* donor to it has an income over \$25,000. But this seems unnecessarily narrow; a group could effectuate net downward redistribution so long as, more often than not, the donors had higher incomes than the recipients. Another possibility would be to subsidize the group if the *average* donor income was over \$25,000.¹³² A third alternative would be to create some type of sliding scale. If, for example, half of the group's donors had incomes above \$25,000, then half of a given contribution would be deductible (and half the group's income tax-exempt).¹³³

Identifying groups that redistribute downwards in this manner, however, places a very heavy burden on the organization in question—keeping track of the income of both the donors and the donees so that its status is not jeopardized in some manner. The weight placed on the income of the donors also illuminates an oddity that flows from this analysis. Consider Bob, whose income clearly exceeds those of the beneficiaries: Why should his ability to get a deduction depend on the incomes of other donors? If he can convince other rich friends to donate, he gets a deduction. But if the other supporters of the group are not wealthy, the group might not qualify. This rule thus might have the unintended consequence of encouraging groups to shun lower income donors, thus exacerbating some of the inequality of

131. Some donors are already treated differently than others. Donors who do not itemize, for example, cannot deduct their contributions, while donors who do itemize can. *See* I.R.C. §§ 63(b) (2012) (individuals who do not itemize are allowed the standard deduction), 170 (2006) (providing for a charitable deduction as an itemized deduction). High income donors who itemize also face a reduction in the value of their donation due to the Pease provision. I.R.C. § 68 (2012) (donors with incomes over a certain amount (\$250,000 for individuals in 2013) must reduce their itemized deductions by a certain percentage). But those all turn solely on characteristics of the donor. Here, we are conditioning the donor's deduction on factors that have nothing to do with her, like the incomes of other people.

132. Should this be the median donor, or the mean? All it might take for a group to have a mean donor income of \$25,000 is one really wealthy donor. If some or many of the groups' donors were below \$25,000, then that would mean that downward redistribution is only occurring from a small portion of its donors. This suggests that any criteria focusing on "average" donor income should focus on median donor income.

133. Although information concerning the incomes of donors and beneficiaries of various types of charities is somewhat scarce at the moment, it can be obtained (as demonstrated by the work compiled by Charles Clotfelter in the 1980s). *See generally* WHO BENEFITS FROM THE NONPROFIT SECTOR?, *supra* note 91.

influence already seen in the charitable world. Lastly, what if the income of the donors or the donees changes? That would presumably influence the allowable tax benefits, but what repercussions might result if a group's tax subsidies fluctuated from year to year, for the same group doing the same activities?¹³⁴

b. Identifying the Donor and Beneficiary in Other Situations

In the above example, all funds flowing to the tennis program came from voluntary donations, and the beneficiaries paid nothing for the charity's services. But only a small portion of charities' revenues comes from donations, and focusing on income redistribution from voluntary donors to beneficiaries is inapplicable when discussing tax exemption.

What about organizations that provide goods or services at reduced prices to some individuals: Who are the redistributors in that situation? To illustrate, imagine a nonprofit daycare that charges roughly half of its clientele the prevailing market rate but offers a discount to the other half based on their financial needs. Assume that the profit margin from full-price families is enough to cover the discount for the needier families. Are the families who pay full price the ones subsidizing the poorer families? Or are they simply receiving what they pay for? Or are the daycare owners the ones engaging in redistribution, foregoing some of the profit from families who pay full price in order to offer reduced-price daycare to needy families? So whose income should be treated as the transferor in this situation?

The foregoing assumes that a "market rate" can be established such that those who are receiving some type of discount are identifiable. But this might work only in situations where both nonprofits and for-profits operate (such as schools and hospitals). In other situations where a nonprofit is "selling" something, like an opera performance, there is no real "market rate" and therefore no real way to determine whom, if anyone, is being subsidized. Rich Schmalbeck and Larry Zelenak make this point by discussing the opera: They imagine that it costs the Houston Opera Company \$500 to perform in Durham. One wealthy opera lover who values seeing *Porgy and Bess* at \$200 buys a \$50 ticket and makes a \$250 contribution (resulting in a total after-tax cost, assuming a 40% tax rate, of \$200).¹³⁵ Four professors each pay \$50 and donate nothing, for a total of \$500 from all five individuals. Schmalbeck and Zelenak argue that, since all five individuals are purchasing the chance to attend the opera at exactly the price they value it, nobody is getting subsidized.¹³⁶

134. Similar questions as to the appropriate comparisons arise with respect to the donees. For example, even if all the donors to an organization have, say, an income of \$100,000, must each and every beneficiary fall below that income level, or just the average beneficiary? How do we define average? And what do we do when both the donor class and the beneficiary class comprise a range of income levels? Because a detailed exploration of these concerns would almost certainly mirror those already expressed, suffice it to say that untangling these comparisons would be exceedingly difficult.

135. The after-tax cost of the \$250 contribution (assuming a 40% tax rate) is \$150, plus the \$50 ticket.

136. RICHARD SCHMALBECK & LAWRENCE ZELENAK, *FEDERAL INCOME TAXATION* 417–18 (2d ed. 2007).

On one hand, the mere fact that an individual purchases an item at a price exactly equal to the price she values that item does not necessarily rule out subsidization. For example, I might be willing to only pay \$500 for a \$5000 mink coat because of my other budgetary constraints, but that does not mean I am not getting subsidized if my mother provides the other \$4500. The problem is that there is a working market (not a big one in many hippie college towns, to be sure) for mink coats and thus an identifiable fair market value for them. Although I might not be able to afford one without help, that does not mean there is not a market for them. That analogy, however, is inapt when it comes to the opera. Without the ability to price discriminate, the opera would not perform at all due to its cost structure.¹³⁷ There is thus no single market price that can be used as a yardstick to determine who is reaping a benefit.

These difficulties suggest the following: under a utilitarian framework, subsidies are warranted only when one can easily identify both the subsidizers and subsidizees, as is the case when both voluntary donations and free or discounted services are provided. In some respects, this lends support to the donative theory of John Colombo and Mark Hall, who argue that voluntary donations signal that a group “deserves” the dual subsidies of the charitable deduction and tax exemption.¹³⁸ Colombo and Hall would thus withhold exemption from groups not receiving a certain amount of voluntary donations and would treat exemption and the deduction as one.¹³⁹ Likewise, utilitarianism supports subsidizing (whether by the deduction or exemption) only organizations that receive voluntary contributions.

c. Valuation Issues

Now another complication emerges: valuing what the beneficiary receives (to measure her increased utility) is difficult.¹⁴⁰ Imagine that Bob donates \$100 to a community theater to stage a production of *The Lion King* in the local park. The beneficiaries (the attendees) do not receive cash, however; they receive the chance to watch *The Lion King*. Normally, tax policy assigns a fair market value to the receipt of noncash items.¹⁴¹ If a tourist in New York City pays \$100 to see *The Lion King*, she is assumed to value *The Lion King* at \$100 because she chose to spend her \$100 at that theater on that particular musical (after all, she could have spent only \$25 to see *Cats*). Yet tax policy struggles with this assumption in nonmarket transactions (consider the valuation issues underlying the convenience of the employer doctrine).¹⁴² Even so, we can often make some observations. For example, in many

137. See Henry B. Hansmann, *The Role of Nonprofit Enterprise*, 89 YALE L.J. 835, 854–59 (1980).

138. COLOMBO & HALL, *supra* note 28, at 99, 107, 163–64.

139. *Id.* at 193–225.

140. SCHMALBECK & ZELENAK, *supra* note 136, at 417–18.

141. See Treas. Reg. § 1.61-2 (1997).

142. See, e.g., I.R.C. § 119 (2012); *Benaglia v. Comm’r.*, 36 B.T.A. 838 (1937) (holding that the value of the room and board provided to a hotel manager for the convenience of the employer is not taxable to the employee); JOSEPH BANKMAN, DANIEL N. SHAVIRO & KIRK J. STARK, *FEDERAL INCOME TAXATION* 52, 56 (16th ed. 2012) (discussing why *Benaglia* presents a valuation problem).

instances, we can reasonably assume that an employee values an in-kind benefit from her employer at its fair market value, because she voluntarily agreed to that compensation package with that employer, instead of other packages with other employers.

But these valuation rules break down when it comes to the provision of free or reduced-cost services outside a traditional market.¹⁴³ The beneficiaries' decisions to avail themselves of a given good or service provided free or at a discount by a charity provide very little information about its value to them. This lack of information therefore makes it even more difficult to determine how much the utilities of *The Lion King's* audience members have increased from Bob's \$100 donation. Without this knowledge, it is hard to compare the increase in the patrons' utility with the assumed decrease in Bob's utility from foregoing \$65 (the after-tax cost of his donation).

d. Other Individuals

Complicating matters further, the foregoing has only considered those with some type of direct tie (donor, employee, service recipient) to the charity in question. A fuller account, however, would consider the utility of the public at large. Eric Zolt, for example, argues that the cost of the deduction is either spending that is cut in other areas, or increased taxes on nondonors that are needed to make up for revenue lost because of the deduction.¹⁴⁴ In his view, the deduction is paid for in the form of higher taxes on higher-income nondonors.¹⁴⁵ It is likely that the cost of the subsidy provided by exemption is borne similarly. This suggests that we would have to assess the reduced utility (from the higher taxes) of other taxpayers, aggregate it, and then compare it to the increased utility of the charitable beneficiaries. But how do we know whose taxes are raised in this situation? And by how much?

This, in turn, illuminates yet another complication. It seems obvious that the individual families participating in our hypothetical "tennis program for the poor" should be counted as beneficiaries. Should others also be considered beneficiaries, such as community members who are pleased that a recreational outlet is offered or that value the discipline and skills the tennis program teaches? If so, this essentially returns us to some of the most vexing questions of charitable-giving policy: What should count as a benefit? How should we measure it?

e. Concluding Thoughts on Traditional Utilitarianism

The foregoing has outlined and challenged the conventional wisdom concerning the charitable tax subsidies and utilitarianism. The measurement, identification, and valuation questions explored above show that, in many cases, identifying with any precision who is doing the subsidizing and who is being subsidized is almost

143. Members of the Supreme Court have also identified these valuation difficulties. See, e.g., *Hernandez v. Comm'r.*, 490 U.S. 680, 706–07 (1989) (O'Connor, J., dissenting).

144. Zolt, *supra* note 88, at 374.

145. *Id.*

impossible. The one place where one can comfortably identify downward redistribution, however, is with respect to donative charities providing basic services to the poor. The transferor (the donor) and transferee (the service recipient) are identifiable. The donor is almost certainly higher-income than the beneficiary. And the fact that the beneficiary is very poor strongly suggests that his or her marginal utility curve is steeper than any given donor's, regardless of the specific shapes.

B. Challenging the Assumptions of Traditional Utilitarianism

Even in tax policy, the foregoing conception of traditional utilitarianism is not undisputed. This Part explores the rejection of the underlying assumptions of (1) identical utility curves and (2) constantly declining marginal utility. Rejecting these assumptions lends further support for the challenge to the conventional wisdom discussed above.

1. Rejecting Identical Utility Curves Across Individuals

Even if one assumes the declining marginal utility of income, it may likely decline at different rates for different people.¹⁴⁶ Whether this inconsistency matters in other debates (such as those concerning increasing marginal rates) is beyond the scope of this Article. But it almost certainly matters in this context, when we are judging the effect of a transfer from one individual to another and necessarily engaging in interpersonal comparisons. Imagine that Colette (with an income of \$500,000) donates to an art museum favored by upper-middle-class individuals. Maybe our donor Colette is on a steeper portion of her utility curve than the art-gazing Dan (with an income of \$100,000). If so, that would mean that a dollar given up by Colette decreases her utility more than it increases the utility of Dan. This too challenges the conventional wisdom, since it suggests transfers that redistribute downward do not necessarily increase utility.

2. Rejecting Utility Curves with Constant Declining Marginal Utility

The accepted wisdom breaks down even further when the assumption that marginal utility declines is challenged. This Part explores two alternative grounds for rejecting that assumption and shows that these challenges further undermine the application of traditional utilitarianism to charitable-giving policy.

a. The Friedman-Savage Utility Curve

One challenge stems from work by Milton Friedman and Leonard Savage, who proposed that some individuals experience increasing marginal utility at certain points along the income spectrum.¹⁴⁷ More specifically, their work suggests that

146. Blum & Kalven, *supra* note 20, at 476–77.

147. See Lawsky, *supra* note 109, at 929–39 for an accessible explanation of the theoretical roots of the Friedman-Savage curve.

“[f]or the lowest range of income, marginal utility declines. For a middle range of income, marginal utility increases. And above some level of income, marginal utility declines again”¹⁴⁸ The Friedman-Savage curve illustrates this, with concave sections at the upper- and lower-income levels and a convex section in the middle joining the two.¹⁴⁹

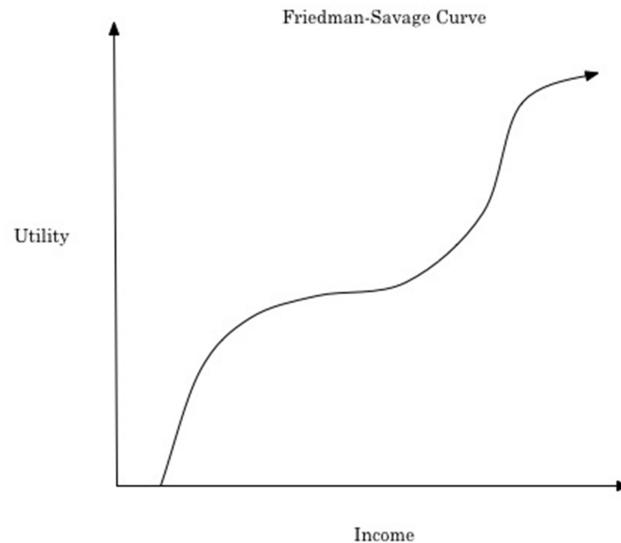


Figure 1. The Friedman-Savage Curve. Reproduced by permission from Sarah B. Lawsky, *On the Edge: Declining Marginal Utility and Tax Policy*, 95 MINN. L. REV. 904, 935 fig.5 (2011). © 2011 *Minnesota Law Review* and Sarah B. Lawsky.

As applied to tax policy, Sarah Lawsky has argued that the Friedman-Savage curve suggests that “there should, in principle, be some upward redistribution from the middle class (say) to the more wealthy.”¹⁵⁰ Even setting aside the difficulty of identifying transferors and transferees, the possibility of alternative utility curves further muddies the use of utilitarianism for assessing charitable-giving policy.

On one hand, if this alternative curve is representative of many people’s utility functions, it defends the current charitable tax subsidies from critiques that they do not do enough downward redistribution. As the Friedman-Savage curve suggests, a transfer that redistributes wealth upwards can, in some instances, actually increase utility. Thus, the mere fact a transfer does not trickle down the income scale would not necessarily mean that it does not increase utility: the \$100 donated by a middle class Yale graduate (for example, a struggling poet) to her alma mater *could* increase utility even if it primarily helps students who are financially better off than she is. The same result would occur with a donation to the opera.¹⁵¹

148. *Id.* at 934.

149. *Id.* at 935. “Concave” and “convex” are determined from the bottom, looking up. *Id.* at 933 n.122.

150. *Id.* at 944.

151. *Id.* at 941.

On the other hand, it will do so only if the beneficiaries (regardless of income) are in fact on a steeper portion of their given utility curve than the donors. And this is an even more daunting task than trying to determine whether an organization redistributes “downwards.” Now we are tasked with determining whether a transfer is from someone with a less steep utility curve to a steeper utility curve. For individuals on the declining edge of the first curve, any downward transfer away from them will satisfy the foregoing. But for individuals on the increasing edge of the second convex curve, a downward transfer may or may not satisfy the foregoing. Thus, simply asking whether a transfer redistributes downward (as we did above) may not answer the question of whether the transfer increases utility, and we already saw how complicated that question is. Likewise, for individuals on the declining edge of the first curve, transfers that redistribute upward—up to a certain point—decrease overall utility, but once those transfers reach individuals with increasing marginal utility, they increase utility.

Moreover, determining whether a beneficiary is on a steeper part of her Friedman-Savage curve than a donor requires even more information than is necessary when declining marginal utility is assumed. If one is assuming declining marginal utility (and identical utility curves across individuals), then you can judge whether a transfer increases or decreases utility without knowing the exact amount of utility associated with any given dollar amount. By definition, you know that utility increases more at \$10,000 than at \$100,000—even if you don’t know how much it increases at each level. All that you need to know, therefore, is whether the dollar donated by the \$100,000 taxpayer goes down or up. If it flows downward, you know it increases the utility of the recipient more than it decreases the utility of the donor. But you do not need to know whether the transfer decreases the donor’s utility by one, three, or ten utils. The declining marginal utility curve tells you that whatever that number is, the utility of the recipient will be increased by more than that amount.

But, if one uses a Friedman-Savage curve, you do need to know where each curve maps onto the income spectrum to determine whether a given transfer increases or decreases utility. For example, you need to know at what point the first concave curve switches into the second convex curve. Before that point, transfers that redistribute upwards decrease utility, but after that point, transfers that redistribute upwards increase overall utility. Thus, to judge the effects of a given transfer from an individual with, say, \$100,000, you need to know where on the various curves he or she is.¹⁵²

If this is, in fact, representative of more than a few individuals’ utility functions, it further undermines the applicability of income-based utilitarianism in most cases.¹⁵³ All we could then say is that if a transfer flows downward, it more likely

152. This task becomes even more complicated if these curves vary across individuals.

153. My goal is not to argue that the Friedman-Savage curve is a superior representation of individuals’ utility curves. Rather, it is to underscore the following: the prior part of this Article showed that even assuming the commonly accepted declining marginal utility curve, utilitarianism requires too much information to be useful on anything more than an exceedingly general level. This Part underscores this lack of helpfulness by showing that (1) challenges exist to the most easily applied expected utility curve and (2) the alternatives to that curve are even more unworkable. In short, the information required to implement this

than not increases utility. If a transfer flows upwards, it may or may not increase utility. And a transfer that mainly benefits those of similar incomes probably has little effect on utility. We would thus have little guidance on whether transfers to groups (like operas or hospitals) that do not provide free or reduced-cost services to the poor increase utility or not. It does seem, however, that the type of transfer most likely to increase utility is one that benefits those furthest down on the income curve, for they likely have steeper curves than anyone else. This suggests that perhaps one way to know for sure that a transfer increases utility is to require some benefit to the very poor, but it does not resolve the possibility that other transfers might also increase utility.

b. Rejecting Static Utility Curves: Prospect Theory and Its Implications

Both the traditional utility curve (with constant declining marginal utility) and alternative expected utility curves (such as the Friedman-Savage model) assume that these curves are static for a given individual, meaning that the expected utility of a transaction should not change depending on whether it is a gain or loss, or how the transaction is framed.¹⁵⁴ Some scholars, however, have challenged the notion that individuals even have a static expected utility curve in the first instance.

This work stems from Kahneman and Tversky's work on prospect theory.¹⁵⁵ According to Kahneman and Tversky, one problem with the traditional application of expected utility theory is that it ignores an individual's starting point.¹⁵⁶ For example, imagine that Ed has \$100. Traditional marginal utility suggests that if Ed's wealth increases by \$10 (to \$110), his utility has increased by some number, X , of utils. Conversely, if Ed starts with \$110 and his wealth decreases by \$10 (to \$100), his utility has decreased by that same number, X , of utils. The absolute change in utility between \$100 and \$110 is assumed to be the same whether Ed starts with \$100 and his wealth increases or starts with \$110 and his wealth decreases.

Under prospect theory, however, the absolute change in Ed's utility depends on whether his wealth increases or decreases. According to prospect theory, an individual weighs more heavily losses from his starting point than gains from that same starting point.¹⁵⁷ Thus, the decrease in Ed's utility when he goes from \$110 to

sort of utilitarianism is so unknowable as to render the theory useful only in an extremely limited way.

154. Eyal Zamir, *Loss Aversion and the Law*, 65 VAND. L. REV. 829, 834–35 (2012) (“Expected utility theory assumes that one's assessment of different outcomes is independent of any reference point.”).

155. Although Kahneman and Tversky were working in a different context—how people make decisions that involve risk and uncertainty—their work sheds doubt on the idea that individuals have static utility curves that reflect constantly declining marginal utility. See generally Daniel Kahneman & Amos Tversky, *Prospect Theory: An Analysis of Decision Under Risk*, 47 ECONOMETRICA 263 (1979).

156. *Id.* at 277; see Zamir, *supra* note 154.

157. Kahneman & Tversky, *supra* note 155, at 280; Zamir, *supra* note 154, at 835–36 (“Gains and losses are defined relative to a reference point. The value function is normally concave for gains (implying risk aversion), convex for losses (reflecting risk seeking), and generally steeper for losses than for gains. This means that the disutility generated by a loss is greater than the utility produced by a similar gain.”).

\$100 will be larger than the corresponding increase in his utility when he goes from \$100 to \$110.

What this means for Ed, therefore, is that his utility curve always depends on his starting point. Whether he has \$50, \$100, or \$1000, his curve will be concave for increases in income (to the right of his starting point) and convex for decreases in income (to the left of his starting point).¹⁵⁸ In prospect theory, this is known as a “value curve”; Ed is always at the center of the following curve, where losses change into gains and all the lines cross:

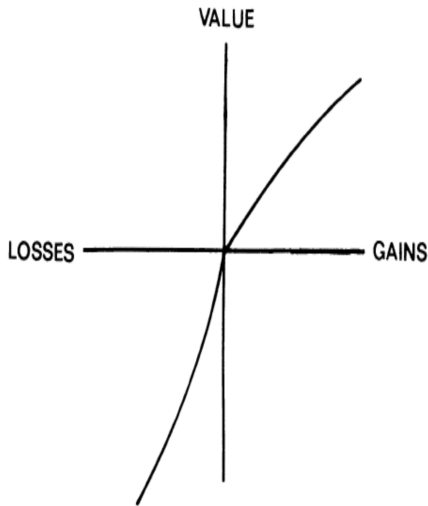


Figure 2. The Value Curve. Reproduced by permission from Daniel Kahneman & Amos Tversky, *Prospect Theory: An Analysis of Decision Under Risk*, 47 *ECONOMETRICA* 263, 279 fig.3 (1979). © 1979 Econometric Society.

Because Ed is always at the point where losses turn to gains, he is effectively always at the point in the Friedman-Savage curve where the curve switches from being convex to concave, no matter his income. What this means is that Ed’s utility curve is constantly changing, minute to minute, for it depends on what he has at that moment. In short, it suggests that Ed does not have one single, static utility curve that can be used to determine the utility of money to him.¹⁵⁹

Like Friedman-Savage, this complicates the application of utilitarianism. First, it’s odd to argue we can make interpersonal comparisons of utility when individuals themselves do not have static curves. But even if one can make interpersonal comparisons, it complicates the comparison. Imagine a transfer from

158. Kahneman & Tversky, *supra* note 155, at 280; Zamir, *supra* note 154, at 835–36. Moreover, Kahneman and Tversky posit that the convex, income decreasing curve will be steeper than the corresponding increasing curve. Kahneman & Tversky, *supra* note 155, at 280.

159. Fried, *supra* note 90, at 991 (stating that the insights of prospect theory “assume[] no generalizable utility curve for money for any individual—indeed, it at least implicitly refutes that such a thing exists”).

Ed to Fiona. Because Ed's income drops, he will move along the convex part of his curve (to the left of his starting point).¹⁶⁰ Because Fiona's income increases, she will move along the concave part of her curve (to the right of her starting point). Ed's change in utility occurs along a part of his curve that reflects decreasing marginal utility and is steeper than the part of Fiona's curve that Fiona will be moving along. Even assuming that Ed's and Fiona's value curves are identical to each other, we do not know whether a redistributive transfer from Ed to Fiona has increased overall utility or not. It might be the case that since the convex portion of Ed's curve is steeper than the concave part of Fiona's curve, Ed's utility decreases by ten utils but Fiona's utility only increases, by say, five. And given that all individuals evaluate changes relative to their own status quo, that means that the foregoing is independent of whether Fiona starts with less income than Ed.

Prospect theory thus offers another ground challenging the usefulness of utilitarianism in tax policy: it challenges the existence of the static utility curves with constant declining marginal utility that provide the most frequent justification for downward redistribution. It may also suggest that how the redistribution is framed will affect how much an individual perceives her utility to be decreased by a loss or increased by receiving a charitable good or service. But other than challenging the foundation of redistribution based on the notion of declining marginal utility, prospect theory itself likely has little to say as a normative matter about the pattern (and not simply the method) of redistribution.¹⁶¹

*C. Final Thoughts on Utilitarianism, Income Redistribution,
and the Charitable Tax Subsidies*

The discussion so far has focused on whether the redistribution of resources from the donor to the beneficiary of charitable goods or services increases overall utility, by comparing the donor's decreased utility with the recipient's increased utility. This Part explains why the donor's utility is assumed to decrease, as well as whether looking at income redistribution is relevant for tax exemption (in addition to the deduction).

160. This treats the redistribution that occurs via Ed's contribution as a loss to Ed, ignoring the consumption value that Ed obtains from it. The extent to which this consumption value should be factored into the analysis is discussed in Part III.C.1. For now, I treat it as a loss because most of the existing literature on charitable giving that uses a utilitarian framework also treats it as a loss of individual consumption (even when still treating the deduction itself as a subsidy), by implicitly comparing the utility loss of the donor to the utility gain of the donee.

161. It is not altogether without positive insights for tax theorists. Prospect theory does have something to say about thinking about the design of various tax systems, *see, e.g.*, Edward J. McCaffery & Jonathan Baron, *Thinking About Tax*, 12 PSYCHOL. PUB. POL'Y & L. 106 (2006), and about tax compliance, *see, e.g.*, Marjorie E. Kornhauser, *A Tax Morale Approach to Compliance: Recommendations for the IRS*, 8 FLA. TAX REV. 599 (2007).

1. Why Speak of a Decrease in Donor Utility?

Until now, this Article has assumed that donor utility decreases from charitable transfers, much like taxpayer utility is thought to decrease by paying taxes. Some might argue, however, that the drop in a donor's income from making a contribution is not the same as a drop when a donor pays taxes, or not the same as a "loss" for purposes of prospect theory, because the charitable contribution is voluntary.¹⁶²

One response might be that charitable giving is not that different than paying taxes, and if theorists assume that paying taxes decreases utility,¹⁶³ they should also assume that charitable giving decreases utility. How are they similar? Most importantly, both pay for public goods, and justifications for both assume that less than 100% of the payment benefits the payor.¹⁶⁴ Thus, both contain some element of redistribution to others. Moreover, both have features that are simultaneously voluntary and involuntary. Taxes are often thought to be "involuntary," but given the extraordinarily low audit rates, many scholars have questioned how true that characterization is.¹⁶⁵ And although charitable giving is thought to be "voluntary," social pressures, hard-sell solicitations, and religious obligations suggest that at least some charitable giving is not wholly voluntary.¹⁶⁶

Assume, however, a distinction between paying taxes and charitable giving. It is true that such a distinction might have certain consequences for the utility of the donor. It does not, however, change the fact that one aspect of a donor's utility has decreased while the same aspect of a recipient's utility increases. A charitable contribution decreases the resources available for the transferor's own consumption while increasing the resources available for the recipient's consumption. There is

162. After all, the basic subsidy theory assumes that charitable giving is consumption just as buying a new sweater is consumption, since both are voluntary. We do not speak of a decrease in utility when someone spends money on a sweater: her utility is thought to remain constant (or even increase). She had \$50 and decided her well-being would be increased by giving up \$50 and receiving a sweater in return. So why speak of a decrease in utility when one makes a charitable contribution?

163. See, e.g., Kornhauser, *supra* note 8, at 1400.

164. To be clear, I am not referring to the measurement theory for the charitable deduction. I am referring to the economic subsidy theory, which posits that the charitable deduction helps pay for public goods that are underfunded by the government. It should also be noted that our current federal tax structure treats paying federal income taxes as consumption as well: federal income taxes are not deductible from income, and the deduction for state and local taxes is thought to be a subsidy.

165. Joel Slemrod, *On Voluntary Compliance, Voluntary Taxes, and Social Capital*, 51 NAT'L TAX J. 485, 485 (1998) ("Given the probability of audit and the penalties typically assessed, evasion seems to be a winning proposition [T]he puzzle is not to explain why people evade, but rather why people pay taxes."); see also Eric A. Posner, *Law and Social Norms: The Case of Tax Compliance*, 86 VA. L. REV. 1781, 1782 (2000) ("A widespread view among tax scholars holds that law enforcement does not explain why people pay taxes.").

166. Weisbrod, *supra* note 49, at 35.

therefore a decrease in the transferor's "self-consumption" utility, even if the donor's utility increases in other ways.¹⁶⁷

To illustrate, when Gail makes a charitable contribution, three things happen. First, she likely experiences an increase in utility from the act of giving and from the recipient's happiness.¹⁶⁸ Second, Gail's ability to consume resources for herself decreases. Third, the beneficiary's ability to consume resources for herself increases, and this redistribution is relevant for utilitarianism. As previously discussed, the increase in Gail's utility from the act of giving is already reflected in the efficiency justification for the initial existence of the charitable tax subsidies,¹⁶⁹ as part of the argument that subsidizing charities enhances societal welfare by enlarging the "pie" for society overall. But the income redistribution that necessarily flows from a charitable gift also affects overall welfare and, as demonstrated above, is separate from these other utilities. Thus, isolating the income aspect of utility while setting aside the other utilities is a valid tool for assessing whether the way the pie is distributed also enhances utility.¹⁷⁰

More importantly, however, the very existence of this question proves my larger point. Prior Parts of this Article emphasized the difficulty of the valuation, measurement, and identification questions inherent in the utilitarian task.¹⁷¹ But this Part raises a question that is even more fundamental concerning the nature of utility, whether it can be disaggregated (and if so, how), and the complexity of making a determination that is as simple as whether a given individual's utility has increased or decreased.

2. Redistribution, Tax Exemption, and the Charitable Deduction

Much of the foregoing has discussed instances in which a donor contributes to an organization, focusing on the difficulties of determining when the donor's gift effectuates income redistribution. Applying a utilitarian analysis to the charitable deduction does not seem like a stretch: there is a transfer from one individual to others (the group's beneficiaries), and the tax benefits the donor receives from the deduction subsidize that transfer. It thus seems logical to ask, in this context, whether the subsidy triggered by the charitable deduction is subsidizing those transfers that most enhance utility or not.

The next question is whether this analysis is relevant to the subsidization that occurs through tax exemption.¹⁷² Although less obvious, I believe it is relevant

167. I emphasize that I am not making a measurement argument to justify the charitable tax subsidies. I am simply arguing that there are multiple components of utility for purposes of measuring a donor's welfare, and that resources available for one's own consumption affect one's utility.

168. See, e.g., KAPLOW, *supra* note 94, at 271; Kaplow, *supra* note 93, at 1–2, 8.

169. See Part I.B.

170. Interestingly, this question exists even if one rejects the assumption that donor utility decreases. In that case, the question still remains: Whose utility will increase the most from receiving charitable goods and services?

171. See *supra* Part III.A–B.

172. Some scholars question whether or to what extent tax exemption acts as a subsidy (as opposed to accurately measuring income). See, e.g., Johnny Rex Buckles, *The Community Income Theory of the Charitable Contributions Deduction*, 80 IND. L.J. 947

nonetheless. The subsidization that occurs through tax exemption still effectuates income redistribution from some individuals to others, albeit more subtly. Take an exempt hospital whose profits are untaxed due to tax exemption. The revenue the government foregoes by not taxing the hospital must be made up somewhere: this could be by providing fewer services elsewhere, or (more likely) by increasing taxes.¹⁷³ Although hard to quantify, there are individuals who are effectively paying for the subsidy to the hospital, meaning that there is redistribution away from those individuals to the hospital's patrons (and perhaps staff). Thus, even tax exemption triggers some income redistribution. It seems logical to compare the decreased utility of all the taxpayers subsidizing a given organization with the increased utility of all the beneficiaries. The fact that the comparison is extremely difficult to make does not undermine the idea that distributive concerns are relevant to tax exempt theory—although it does essentially prove the point that traditional utilitarianism is not the best tool for so doing.

Moreover, this Article's analysis is relevant even if we dodge the difficult question of ascertaining who is doing the subsidizing. Tax exemption provides benefits to the patrons of subsidized organizations (even though identifying the beneficiaries can be difficult at times).¹⁷⁴ Even looking solely at the beneficiaries can be valuable; identifying which types of organizations increase beneficiary "utility" (however defined) the most can help us prioritize among organizations. And that analysis is relevant to both the charitable deduction and tax exemption.

IV. UTILITY AS WELL-BEING

As shown above, tax theorists invoking utilitarianism have traditionally used income and/or wealth as proxies for utility.¹⁷⁵ Recently, however, legal scholarship has taken a renewed interest in the interaction of legal policies and actual well-being (as opposed to the interaction of legal policies and wealth as a proxy for well-being).¹⁷⁶ This interest stems from work pioneered by psychologists and

(2005); Daniel Halperin, *Is Income Tax Exemption for Charities a Subsidy?*, 64 TAX L. REV. 283 (2011). Moreover, the Joint Committee on Taxation does not list tax exemption as a tax expenditure (even though it lists the charitable deduction). See generally STAFF OF JOINT COMM. ON TAXATION, 113TH CONG., ESTIMATES OF FEDERAL TAX EXPENDITURES FOR FISCAL YEARS 2012–2017 (Comm. Print 2013). This Article, however, follows the majority of tax scholarship in considering exemption to be a subsidy.

173. See Zolt, *supra* note 88. Zolt discusses who "pays" for the charitable deduction, but the analysis applies with equal force to exemption.

174. See *supra* text accompanying notes 135–37.

175. See *supra* Part III.A.

176. By refocusing on actual happiness or well-being instead of using wealth as a proxy, academics are in some sense coming full circle. Early utilitarians (such as Bentham and Mill) equated utility with "mental state[s] like happiness or pleasure." HAUSMAN & MCPHERSON, *supra* note 96, at 101; see also Richard Layard, Lecture at the Lionel Robbins Memorial Lectures of the London School of Economics: *What Would Make a Happier Society?* 16 (Mar. 5, 2003), <http://cep.lse.ac.uk/events/lectures/layard/RL050303.pdf> ("[The] right concept [of happiness] is the old Enlightenment one of the greatest happiness. The good society is the one where people are happiest. And the right action is the one which produces the greatest happiness."). Later, legal academics interested in maximizing "welfare" began using income and/or wealth as proxies to avoid the messy questions about "what is welfare" that have plagued philosophers for generations.

economists seeking to understand the myriad factors that affect an individual's happiness, welfare, or well-being.¹⁷⁷ Armed with these findings, a number of legal scholars have begun to mine them for insights into a variety of legal issues, ranging from employment discrimination, family law, and tort law to civil litigation, corporate governance, and shareholder participation.¹⁷⁸ And more relevant to this Article, a few tax theorists have looked toward this literature for insights into estate taxation, cigarette taxation, and progressivity.¹⁷⁹ And on an even broader level, some policymakers have proposed developing a well-being index (similar to Gross Domestic Product) that could help assess whether a given policy would increase or decrease overall happiness.¹⁸⁰

Given this growing interest in the interaction of well-being and public policy, an exploration of utilitarianism and charitable-giving policy would be incomplete without looking directly at well-being itself (instead of wealth and/or income as proxies).¹⁸¹ To that end, this Part lays out the most common interpretations of well-being found in this scholarship and examines whether a distributive goal of maximizing well-being (instead of the utility associated with wealth) could answer any of the recurring distributive questions.

As this Part shows, the initial take on these theories is that while they may offer a way to prioritize among charities, that prioritization has nothing to do with the income-level of the beneficiaries. It further demonstrates, however, that each theory has intrinsic drawbacks that run headfirst into pluralism considerations. Used alone,

177. Although these terms are often used interchangeably, debate exists as to whether they are in fact interchangeable, and if not, what they each mean. See Matthew D. Adler, *Happiness Surveys and Public Policy: What's the Use?*, 62 DUKE L.J. 1509, 1522 (2013).

178. See, e.g., Peter Henry Huang, *Happiness Studies and Legal Policy*, 6 ANN. REV. LAW & SOC. SCI. 21.1, 21.7 (2010).

179. See, e.g., David A. Weisbach, *What Does Happiness Research Tell Us About Taxation?*, in LAW & HAPPINESS 293 (Eric A. Posner & Cass R. Sunstein eds., 2010) (discussing the potential implications of happiness research for taxation but arguing that better data is needed before such insights can be implemented); Mirko Bagaric & James McConville, *Stop Taxing Happiness: A New Perspective on Progressive Taxation*, 2 PITT. TAX REV. 65, 87–91 (considering the implications of happiness research for the tax rate structure under a specifically utilitarian framework); Griffith, *supra* note 8, at 1398 (arguing that the happiness research provides another justification for a progressive tax structure); J.D. Trout & Shahid A. Buttar, *Resurrecting "Death Taxes": Inheritance, Redistribution, and the Science of Happiness*, 16 J.L. & POL. 765, 833–39 (2000) (suggesting that the happiness research lends support for inheritance or estate taxes).

180. See Adler, *supra* note 177, at 1516. Perhaps the most prominent example is the Kingdom of Bhutan's use for several decades of a Gross National Happiness Index to review proposed policies. ARTHUR C. BROOKS, GROSS NATIONAL HAPPINESS: WHY HAPPINESS MATTERS FOR AMERICA—AND HOW WE CAN GET MORE OF IT 2–3 (2008). Although Bhutan's new prime minister is dropping the happiness index, Germany is also considering such an index. *Germany to Develop 'Happiness Index,'* LOCAL (Jan. 17, 2011, 5:59 PM), <http://www.thelocal.de/national/20110117-32487.html#.UQwqr-g5h11>; Gardiner Harris, *Index of Happiness? Bhutan's New Leader Prefers More Concrete Goals*, N.Y. TIMES, Oct. 4, 2013, at A5.

181. Layard, *supra* note 176, at 16–17 (equating the maximization of happiness with a utilitarian moral objective, and tying the two to decisions about how society should allocate its resources).

therefore, any of these well-being theories is unappealing as a tool for assessing the distributive impact of the charitable tax subsidies. Moreover, choosing among them also undermines the pluralism goals of the sector. However, the fact that all such theories would subsidize poor relief suggests that there is something special about groups that assist the poor. This Article shall start with preference satisfaction and then in turn examine subjective well-being and objective list conceptions of well-being.

A. Utility as Preference Satisfaction

One of the most common definitions of well-being prevalent in the philosophical literature is that of preference satisfaction; these views tell us that an individual's preferences illuminate for us what constitutes her well-being. What she chooses is what she considers to be good for her.¹⁸² This conception, of course, is most closely related to the type of utilitarianism traditionally used by tax theorists, which focuses on income or wealth precisely because it is a medium of satisfying preferences.¹⁸³ And in fact, the efficiency and pluralism scholarship on the charitable tax subsidies reflects this view as well by focusing on the deduction's capacity to satisfy the preferences of donors.¹⁸⁴ However, the efficiency literature leaves a few unanswered questions that merit discussion. Namely, current literature does not adequately discuss the preferences of individuals other than the donor. Nor does it satisfactorily address the tyranny of the majority problem that has long been the bane of utilitarianism.

1. What About the Preferences of the Beneficiaries?

Despite the attention paid to the preferences of the donors,¹⁸⁵ much less attention has been paid to maximizing the ability of charitable beneficiaries and nondonors to satisfy their preferences (which is relevant to both the deduction and tax exemption). Much disease research, for example, focuses on diseases that are "trendy" or have garnered celebrity attention (such as AIDS).¹⁸⁶ But it might be the case that a far greater number of people would prefer increased research on say, diabetes or asthma—two less "sexy" diseases. Imagine that Henry shops at a yuppie organic foods grocery store that allows him to purchase various baskets of food for local needy families. For example, Henry might pay \$20 to give a family three boxes of organic macaroni and cheese, one jar of organic peanut butter, and one loaf of organic bread. It might well be the case, however, that a needy family might rather receive five boxes of non-organic macaroni and cheese, and two jars

182. HAUSMAN & MCPHERSON, *supra* note 96, at 101 ("Most contemporary utilitarians take welfare to be the satisfaction of rational and self-interested preference . . .").

183. *Id.* at 120.

184. *See supra* Part I.B.

185. For example, the back scratching analogy used by Colombo and Hall, COLOMBO & HALL, *supra* note 28, at 107–08, focuses on donor preferences: ruffled-grouse lovers and opera lovers agree to subsidize each other's projects in return for a subsidy of their own.

186. *See generally* Vicki Brower, *The Squeaky Wheel Gets the Grease*, 6 EMBO REP. 1014 (2005).

of non-organic peanut butter, and two loaves of non-organic bread with Henry's \$20.¹⁸⁷

The current structure thus prioritizes the preferences of the donors over the preferences of the beneficiaries and the public. One might now be tempted to ask why the preferences of nondonors should matter. After all, couldn't someone who is dissatisfied with the available assortment of charitable goods simply create his own organization or make his own contributions? The answer is that by definition, charitable giving buys public goods. Thus, it seems that the preferences of nondonors who will benefit from these public goods should also matter in assessing the resulting distribution of public goods. This is especially so when approximately two-thirds of Americans do not itemize, and thus cannot "purchase" government funds for their preferred public good.¹⁸⁸

Thus, if preference satisfaction utilitarianism is used to judge the distributive effects of public goods, the preferences of individuals other than donors should be considered in addition to those of donors (and when discussing exemption, there may or may not be donors). But how should this be done? For most goods, markets measure preferences. But charitable giving by definition purchases nonmarket goods, for which preferences are hard to measure.

a. Do Beneficiaries Have a Way to Express Their Preferences?

One response is that perhaps beneficiaries already show their preferences: many charities compete not only with each other, but often with for-profits as well, and beneficiaries can show preferences by patronizing one charity instead of another. Parents can choose a Catholic school or a Montessori school based on their preferences. A recently unemployed factory worker can choose a job training program that teaches computer programming or one that teaches health care services based on his preferences. Fans of the arts can choose to attend either the ballet or the opera based on their preferences. And hypothetically, a soup kitchen that served food no one liked would eventually close its doors. The problem is, however, that not all charitable beneficiaries can vote with their feet in this manner. Two types of situations are illustrative.

i. Unequal Ability to "Shop Around"

First, charitable beneficiaries who are financially disadvantaged have less opportunity than others to express their preferences by shopping around. There may only be one private school that offers scholarships in the beneficiaries'

187. Whether they are physically better off with the organic food is beside the point. What matters is their preferences. The complication, however, is that the public at large may prefer that the poor eat healthier food. And if we are discussing the preferences of individuals other than the donor, why not also factor in the preferences of the public at large? It soon becomes very hard to manage.

188. MICHAEL J. GRAETZ & DEBORAH H. SCHENK, *FEDERAL INCOME TAXATION: PRINCIPLES AND POLICIES* 398 (7th ed. 2013) ("About 65 percent of taxpayers take the standard deduction and do not itemize.").

neighborhood, for example.¹⁸⁹ Or perhaps one job training program is on a bus line and another is not. Maybe there is only one soup kitchen nearby, but it serves food the beneficiaries dislike. It is therefore possible that groups providing these types of social services do not truly reflect their beneficiaries' preferences.¹⁹⁰

This is not to say that such groups do not reflect beneficiary preferences at all, but only to say that they might not reflect a beneficiary's preferences very well. Imagine a soup kitchen. If a beneficiary eats the soup provided, she therefore places some value on it. She prefers eating the soup to not eating it, or prefers eating the soup to going hungry, and therefore overall preference satisfaction has increased. It is also true that lower-income individuals have less of an ability than higher-income individuals to satisfy their various food preferences when they walk into a grocery store.¹⁹¹ But this illustrates the constraints one faces in satisfying one's preference in the market, while charitable giving by definition operates where markets fail. Because of that difference, the argument that the poor frequently have less of an ability to satisfy their preferences than the rich is unappealing when it comes to considering their preferences for charitable goods and services. This is especially true if we are trying to move beyond income in determining well-being. Thus, settling for slight increases in preference satisfaction seems like asking too little. Even if we do not expect to maximize preference satisfaction, we should somehow aim to finance those projects that do more than the bare minimum when it comes to increasing preference satisfaction. But for the reasons just outlined in this Part, it is difficult to identify those projects.

ii. Charitable Goods with No Ascertainable Beneficiary

The problem of beneficiaries' preferences is also relevant when discussing topics like environmental protection and medical research. There isn't really an opportunity for currently healthy individuals to indicate their preferences as to how medical research dollars should be spent without making a donation themselves. It might be the case, for example, that the public at large would prefer more research on heart disease or asthma, rather than on diseases such as AIDS and breast cancer which have captured the attention of the press and many celebrities. It is thus hard

189. This assumes that the parents have already decided that the available public school is not appropriate for their child.

190. One would hope that most such organizations are responsive to their clients' needs and preferences and strive to provide, for example, the best tasting food at a given price. And while this is likely the case in many instances, there are also many charities that provide the services they do precisely because their founders and donors do think they know best. Take Catholic schools, for example, which are often the only private school option available in poor neighborhoods. Many such schools explicitly try to shape the preferences of their students.

191. The money one has when one walks into the grocery store, of course, already reflects one's preferences about whether to work, at what job, and how often. Thus, the choices low-income individuals face at the store, to some extent, already reflect their preferences. Maybe this point answers the question of charitable beneficiary preferences, but I think not. The point of charitable aid to the poor is to address the fact that they live, to some extent, outside the regular market.

to know when these types of charitable expenditures actually increase overall utility.

In theory, ways to measure these preferences do exist. In a number of contexts, welfare polls are used to elicit information about citizen preferences on a range of topics. Such polls have long been used in the environmental context, for example, but have also been used to elicit information about other attributes of well-being, such as recreation, cultural amenities, and health and safety risks.¹⁹² One common method is the use of “contingent valuation” surveys, which elicit such information by asking participants how much they would be willing to pay to have a certain positive benefit or to avoid a certain negative detriment.¹⁹³ A second method, the use of “quality-adjusted life year” surveys (in which participants indicate preferences for living a certain amount of time in perfect health versus another amount of time in less-than-perfect health), appears in the health policy area.¹⁹⁴ Using these and other types of welfare polls could therefore shed light on the preferences of nondonors when it comes to projects involving the environment and medical research. The problem, however, is that using polling information in this manner could lead to a tyranny of the majority problem, which is at odds with the pluralistic goals of the nonprofit sector.

iii. Concluding Thoughts on the Ability of Beneficiaries to Express Their Preferences

There is thus almost no way to structure the subsidies to somehow maximize the ability of beneficiaries to satisfy their preferences. Take the provision of basic goods and services to the needy: pure cash transfers would do more for beneficiary preference satisfaction than providing in-kind goods.¹⁹⁵ But this is likely antithetical to the preferences of many donors, and moreover, solves the beneficiary preference problem only for goods and services that are normally available in the for-profit market.

One response to this dilemma might be to assume that the current array of charitable goods and services represents the preferences of the beneficiaries for the following reason: beneficiaries might be willing to “forfeit” an ability to maximize their exact preferences in exchange for a larger surplus of public and charitable goods. That is, beneficiaries are willing to accept whatever donors are willing to provide, even though the current system prioritizes the preferences of high-income donors, because they are better off doing so than not. But again, this likely conceives of their preferences being satisfied only on a minimal level. Moreover, it raises the question of whether we as a society want to allow individuals to bargain away their preferences like this. Another response might be to assume that beneficiary preferences are better met by the nonprofit sector than the government, or by having both the nonprofit sector and the government provide public goods

192. See generally Matthew D. Adler, *Welfare Polls: A Synthesis*, 81 N.Y.U. L. REV. 1875 (2006) (describing and defending the use of welfare polls in government decision-making).

193. *Id.* at 1882–85.

194. *Id.* at 1885–86.

195. See HAUSMAN & MCPHERSON, *supra* note 96, at 125–26.

and services. This may be so, but again, it seems that beneficiary preferences merit more attention than assumptions such as the foregoing.

To be clear, the point of the foregoing discussion is not to prioritize beneficiary preferences over donor preferences. Both must be considered if the goal is increasing overall preference satisfaction. The point is to highlight the difficulty that arises in many situations when one tries to factor in beneficiary preferences on more than the most minimal level, and to explore the extent to which our current system sometimes fails to do so.

b. When Beneficiaries Are Happy Slaves

A second issue with respect to beneficiary preferences concerns the problem of the “happy slave”—that is, people who are in circumstances very few others would be happy with, but who have either adapted or do not know any different and thus are satisfied and do not want to change their situation.¹⁹⁶ Philosophers who support objective list conceptions of well-being, for example, often point to the problem of happy slaves when criticizing preference satisfaction views of well-being.¹⁹⁷ But if tax law is going to take well-being to mean preference satisfaction, it must address this issue. In the charitable-giving context, the issue is tricky precisely because many groups—especially social justice groups, for example—set out purposely to change people’s preferences. Let’s say a group of workers are happy with their employment situation, but a nonprofit that is unhappy with the working conditions litigates on their behalf. How should that be treated?

2. Which Donor Preferences Should Count?

The philosophy literature discussing preference satisfaction and utilitarianism highlights yet another complication: Should all preferences count? For example, should preferences about affairs that do not directly impact oneself (say, whether a rare squirrel in a remote part of the world that one has never seen survives extinction) be included in the utility calculus?¹⁹⁸ And what about preferences such as racism and homophobia?¹⁹⁹ The former question seems easy enough to answer: given that the point of the charitable giving is to purchase public goods that by definition benefit others, it seems that preferences remote from one’s own immediate well-being should matter. The latter is a tougher question. Unless one starts down the path of laundering preferences,²⁰⁰ it seems that antisocial preferences should generally be honored. In theory, this comports with the

196. *Id.* at 127–28.

197. *See* KYMLICKA, *supra* note 10, at 16.

198. *See, e.g.,* Adler, *supra* note 177, at 1576–80; John Bronsteen, Christopher Buccafusco & Jonathan S. Masur, *Welfare as Happiness*, 98 *GEO. L.J.* 1583, 1625–27 (2010).

199. *See, e.g.,* HAUSMAN & MCPHERSON, *supra* note 96, at 127; Bronsteen et al., *supra* note 198, at 1612–13.

200. Following this path invokes the type of value judgments many proponents of preference satisfaction seek to avoid.

diversity-protecting rationale for the sector, but becomes complicated when preferences contrast with one another.

3. Determining Whether Overall Utility Has Increased in a World with Opposing Preferences

This Part's discussion of welfare has focused largely on which activities increase the well-being (defined as preference satisfaction) of donors and direct beneficiaries. But the complication is that these activities do not occur in a vacuum. Especially when defining well-being as preference satisfaction,²⁰¹ many activities simultaneously increase one person's well-being while decreasing another's; a donor might prefer that a museum be subsidized, but her neighbor may prefer the opposite. This complicates the task of determining when a given charitable activity increase or decreases overall welfare.

a. Noncontroversial Activities

As an initial matter, subsidizing transfers to organizations whose missions do not generate much deeply held opposition probably increases utility. This likely holds true for many charitable organizations. Iris may think a ketchup museum is silly (to borrow from David Schizer) and therefore prefer that it not be subsidized. But the decrease in her well-being from thinking it is silly is likely outweighed from the increased utility of donors and patrons of the museum. On the other hand, maybe the *aggregate* decrease in utility (even though small on a per capita basis) from those who consider a ketchup museum frivolous does, when aggregated, outweigh the increased preference satisfaction of the far smaller number of ketchup enthusiasts. This is difficult to know for sure.

b. Controversial Organizations

This aggregation, however, becomes more complicated when the activities of a given organization generate substantial opposition. Take, for example, a group whose mission is to educate women about the benefits of abortion. Given the substantial presence and activities of groups opposed to abortion and the passion pro-life individuals have on the subject, the pro-choice group's activities make some other people very unhappy. If the pro-choice group has 2000 supporters but

201. Although there may be some instances where the following analysis also applies to welfare defined as hedonic happiness, these situations are probably relatively rare. Take gay marriage, for example. Someone may have an extremely strong preference that same-sex couples not be allowed to marry, and this preference would factor into preference satisfaction views of welfare. But this preference would likely impact her subjective well-being (SWB) very little. She might become upset when reading about gay marriage or seeing a gay couple holding hands on the street. But other than those fleeting instances, her opposition to gay marriage will affect her SWB very little, as the other factors discussed in this Article play a much larger role in her SWB. See E-mail from John Bronsteen to author (Aug. 7, 2012, 19:43 MST) (on file with author). In this sense, then, defining welfare as SWB does protect minority interests.

the pro-life group has 1000 supporters, then subsidizing the pro-choice group likely increases overall welfare, despite the preferences of pro-life individuals. But if the opposite is true, then subsidizing the pro-choice group likely decreases overall welfare.²⁰² Under a framework that focuses on increasing aggregate welfare, groups with smaller numbers that deal with controversial issues would not merit a subsidy. This analysis could also extend to other groups not involved in taking sides on issues about which the public is divided (such as abortion or gay rights), but whose activities themselves some are opposed to. Many individuals, for example, believe that churches have negative effects on society. Others feel that certain kinds of poor relief might breed dependence. But not subsidizing organizations because of opposition to them seems to fly in the face of one of the key nondistributional benefits of the sector, its pluralism.²⁰³ Precluding subsidies to such organizations could result in a tyranny of the majority.²⁰⁴

One might respond as follows: true enough, but the above looks at contributions to controversial organizations in a vacuum. Perhaps a given individual is made severely unhappy by any given organization. But that same individual is likely benefited by enough other organizations, or by the metabenefits of the sector (such as pluralism, diversity, and a vibrant civil society), that overall well-being is still increased by an expansive definition of the sector. Put another way, maybe that individual is willing to accept the tradeoff of having organizations she dislikes be funded in exchange for the benefits of a large nonprofit sector.

Maybe, but maybe not. All we can do is instinctively guess that it is so. And this leaves us right back to vague judgments—what is “beneficial” to society? Ironically, it was frustration with those vague value judgments that led earlier scholars to try to find value-neutral methods (such as efficiency) of evaluating the charitable tax subsidies.²⁰⁵ But as Shannon McCormack recently argued, a full analysis of efficiency that takes into account both positive and negative externalities leads us right back to the same place.²⁰⁶ We are thus stuck needing some type of underlying normative guideline for evaluating charitable transfers, and using only preference satisfaction is antithetical to our pluralistic society.

B. Utility as Subjective Well-Being

Despite the traditional interpretation of “utility” using measures such as income or preference satisfaction, some legal scholars have recently begun equating utility with happiness or subjective well-being (SWB).²⁰⁷ Although happiness is sometimes defined as having a positive affect (that is, with feeling “good” or

202. Shannon Weeks McCormack, *Taking the Good with the Bad: Recognizing the Negative Externalities Created by Charities and Their Implications for the Charitable Deduction*, 52 ARIZ. L. REV. 977, 982–83 (2010).

203. I thank Lloyd Mayer, professor of law at Notre Dame, for bringing these points to my attention.

204. KYMLICKA, *supra* note 10, at 26–27.

205. *See, e.g.*, Gergen, *supra* note 49, at 1396.

206. McCormack, *supra* note 202, at 996–1024.

207. I shall use the terms “happiness” and “subjective well-being” interchangeably.

experiencing positive sensations such as pleasure from moment to moment),²⁰⁸ it is more commonly defined as evaluating one's overall life with satisfaction.²⁰⁹ Although research in this field is still evolving, two components are relevant to the charitable tax subsidies. First, what do we know about the interaction of income and happiness, and do these insights have any relevance for charitable-giving policy? And second, what nonmonetary factors influence one's happiness, and could these be used to judge the impact of the charitable tax subsidies?²¹⁰

1. Insights on the Relationship of Money and Happiness from the Subjective Well-Being Literature

The first half of this Article explored the interaction between income and utility for purposes of determining when a given redistributive transfer increases overall utility.²¹¹ As this Part explores, however, income and utility interact in other ways that may have additional implications for the charitable tax subsidies. Namely, does additional income even increase happiness in the first instance?

Happiness studies suggest that higher-income individuals are generally happier than lower-income, but an extra dollar produces much more happiness to low-income than high-income individuals.²¹² This seems to support the idea of declining marginal utility. However, the average happiness of a given income group (for example, individuals whose incomes are in the twentieth to fortieth percentile) appears to be fairly constant over time even if the cohort as a whole experiences significant income growth.²¹³ In other words, even if one's income grows, one's happiness remains about the same as long as one remains in the same percentile as before. This "happiness paradox" has led many scholars to argue that (with respect to income and happiness) happiness is dependent upon one's relative place in society.²¹⁴ An extra dollar produces more happiness for a poor person than

208. See, e.g., Bronsteen et al., *supra* note 198, at 1586–87 (arguing that "a person's well-being is the aggregate of how she feels throughout her life" and that this measure should guide policymakers (emphasis omitted)).

209. BROOKS, *supra* note 180, at 4–5; see Adler, *supra* note 177, at 1513. This subjective measurement recognizes that everyone's life contains some unpleasantness, but that some people are more satisfied or happier than others when they evaluate their life taken as a whole. BROOKS, *supra* note 180, at 5. Happiness on balance is most frequently measured via large-scale surveys that ask questions such as, "All things considered, how satisfied are you with your life these days?" or, "As a whole, would you say that you are very happy, pretty happy, or not too happy?" Adler, *supra* note 177, at 1512; Huang, *supra* note 178, at 21.4; David G. Myers & Ed Diener, *Who Is Happy?*, 6 PSYCHOL. SCI. 10, 10 (1995). Not surprisingly, those who report high levels of overall life satisfaction also experience more instances of positive affect. Myers & Diener, *supra*, at 11. This overlap, however, should not confuse the point that these are two distinct ways of defining well-being or happiness.

210. Although current research sometimes suggests a causal connection between these factors and happiness, only a correlation can be shown at other times. My exploration, however, proceeds as if a causal connection exists.

211. See *supra* Part III.

212. Griffith, *supra* note 8, at 1379–80 (discussing several such studies).

213. *Id.* at 1381.

214. BROOKS, *supra* note 180, at 120–23; Griffith, *supra* note 8, at 1381–84.

a rich person not because it leads to greater purchasing power for its own sake,²¹⁵ but because it has more of an impact on one's place in the income pecking order.²¹⁶

This nuance in the relationship of happiness to income has several potential implications for charitable subsidy policies. As a technical matter, it might suggest subsidizing charitable transfers more heavily than we currently do, and structuring the subsidy to increase as income rises.²¹⁷ This follows because the more income that Katherine has relative to Jack, the worse off Jack is. But if Katherine's income drops—even if not redistributed to Jack—Jack becomes better off. Therefore, the more money that Katherine gives to charity and does not spend on herself, the better off Jack becomes. We thus would want to encourage higher-income individuals to contribute more than lower-income individuals. In this respect, the “upside-down subsidy” argument loses some force when assessed through a happiness-centered utilitarian lens.

That said, the foregoing analysis might be subject to two objections. The first is that relative positions in society are zero sum.²¹⁸ For every Jack whose utility is increased because he inches upwards closer to Katherine, there is a Katherine whose utility has decreased because she inches downwards closer to Jack. Thus, the mere fact that Jack becomes better off when Katherine's income drops does not necessarily mean that overall utility has increased. Instead, overall utility increases only if Jack's utility increases by more than Katherine's utility decreases—which again requires a nuanced interpersonal utility comparison.

Second, the “relative position” reason for subsidizing more giving by higher-income individuals would also be undermined if charitable giving is itself a positional good, that is, a good whose value comes from the fact that it signals the owner's status in society.²¹⁹ This could be so to the extent that charitable giving signals social status or wealth, as is often the case when a donation enables one to attend exclusive galas and dinners or to have a building named after oneself. In that situation, Jack might not necessarily feel better off if Katherine foregoes buying a new Rolls Royce in order to have her name hung by a painting at the local art museum. Jack is still just as aware as ever that Katherine has more income than he does.

215. This paradox does not apply to those lacking basic necessities. For the poor, additional dollars *are* important for their purchasing power. BROOKS, *supra* note 180, at 117; DANIEL GILBERT, STUMBLING ON HAPPINESS 217–18 (2006); Myers & Diener, *supra* note 209, at 13 (“Wealth, it seems, is like health: Its absence can breed misery, yet having it is no guarantee of happiness.”). For such individuals, therefore, a dollar is valuable for its ability to purchase such necessities. This suggests that the traditional take on redistribution is true up to the point where individuals attain a basic subsistence level; but once one reaches the “middle class” and can afford basic necessities, the paradox begins to kick in. GILBERT, *supra*, at 217.

216. Griffith, *supra* note 8, at 1384.

217. David Schizer has suggested a similar structure. *See* Schizer, *supra* note 57, at 234.

218. *See* Galle, *supra* note 93, at 830–31.

219. Such goods signal the owner's relative position because they are more expensive than comparable goods in the same class. Take luxury cars: they perform the same task as less expensive cars, but signal that the owner can afford to pay more for a car. Griffith, *supra* note 8, at 1384; *see also* ROBERT H. FRANK, CHOOSING THE RIGHT POND: HUMAN BEHAVIOR AND THE QUEST FOR STATUS 7–11 (1985); Robert H. Frank & Cass R. Sunstein, *Cost-Benefit Analysis and Relative Position*, 68 U. CHI. L. REV. 323, 337 (2001).

To that end, SWB utilitarianism provides additional support for the argument that charitable donations with this type of quid pro quo do not merit a subsidy. Prior scholars making that case have reasoned that because of the quid pro quo, donors would make such gifts without a tax subsidy, rendering a subsidy at best pointless²²⁰ and at worst inefficient.²²¹ Distributive justice thus complements efficiency analysis in suggesting that fewer kinds of gifts deserve a subsidy than under current law.

2. Using the Charitable Tax Subsidies to Enhance Subjective Well-Being

Part III of this Article explored the extent to which utility can be maximized by the income redistribution inherent in the charitable tax subsidies.²²² This Part redefines utility as happiness to ask whether prioritizing certain types of charities over others generates more happiness. Could that approach help answer some of the recurring distributive questions? Initially, the answer seems to be yes. We would prioritize those groups that contribute to the elements associated with the largest increases in SWB, and charitable groups would not be required to provide free or reduced cost services to the financially disadvantaged to receive a subsidy. The problem, however, is that this disadvantages individuals whose SWBs are increased by less common factors, and this flies in the face of two of the key nondistributional attributes of the nonprofit sector: diversity and protection of minority tastes.

To flesh out this reasoning, this Part identifies a few factors frequently associated with increased happiness. It then explores how charitable-giving policy might influence well-being, assuming that such factors cause increased happiness.²²³

Friendship. Studies suggest that people with several close relationships are happier than those without such ties and that a lack of such ties increases depression.²²⁴ This suggests prioritizing organizations whose missions are to promote such ties in some ways—for example, groups that enable people with similar hobbies and interests to engage in those activities together in a shared community setting. This would include social clubs for bridge and Scrabble players, as well as sports leagues for bowling, tennis, and golf athletes. Choirs, art

220. John D. Colombo, *The Marketing of Philanthropy and the Charitable Contributions Deduction: Integrating Theories for the Deduction and Tax Exemption*, 36 WAKE FOREST L. REV. 657, 662 (2001) (arguing that such transfers should not receive a deduction).

221. See, e.g., Gergen, *supra* note 49, at 1409 (describing the overbuilding of capital projects on many university campuses).

222. See *supra* Part III.

223. For example, although current research has found a correlation between religion and happiness, whether the former *causes* the latter is still unclear. BROOKS, *supra* note 180, at 45–46. However, some research suggests that friendship causally increases happiness. *Id.* at 73–74.

224. *Id.* at 73–74; Myers & Diener, *supra* note 209, at 14. To some extent, this is circular—happier people are also more likely to make friends in the first instance than unhappy people. That said, evidence does suggest a causal link between friendship and happiness and that additional friends increase happiness. BROOKS, *supra* note 180, at 73–74.

classes, knitting circles, and book groups would also likely make the list. We would also assist groups that provide opportunities for people to make new friends or to find support during potentially lonely times of life. This might include, for example, camps and activities where children can make friends, as well as support groups for the bereaved, the unemployed, new parents, and so on.²²⁵ On the other hand, this suggests that nonprofits providing nonparticipatory goods and services (such as the opera) would not be subsidized as heavily, but for reasons beside that such organizations help the rich and not the poor.

Faith. Much work has also found a link between religion and happiness.²²⁶ More specifically, people who actively practice a religion, whether by attending services or praying on their own, tend to be happier.²²⁷ This holds true regardless of the religion practiced and does not vary with age, sex, or education.²²⁸ Assuming causation, structuring the charitable tax subsidies to maximize happiness would therefore subsidize churches and other places of worship that promote the practice of religion. While this is not a new proposition (indeed, the earliest recipients of tax exemption were churches),²²⁹ these subsidies often draw heavy criticism.²³⁰ Applying a happiness-theory-focused variant of utilitarianism, therefore, helps us assess one of the most common criticisms of the charitable tax subsidies as currently structured.

A more controversial implication—and one that would change current law—is that groups advocating complete secularism in the public sphere would potentially no longer merit a charitable subsidy. This is so because, at minimum, we would not want to discourage the practice of religion by keeping it out of view. Instead, we would want to allow glimpses of religion to appear in noncompulsory settings so that society knew religious practice was one of many lifestyle choices.²³¹ On the other hand, many religious organizations promote policies that create unhappiness in others (for example, promoting public prayer or opposing same-sex marriage), and these complications must be addressed.²³²

Work and “Flow.” Another contributor to happiness is absorption in meaningful activities. Whether at leisure or at work, being immersed in a project or activity that focuses one’s mind and causes time to fly increases happiness.²³³ And in addition to creating opportunities to become lost in the flow of an activity, work can also contribute to one’s personal identity, give one’s life purpose, and create a network and feeling of community for a working individual.²³⁴ Together, these findings

225. This would likely also include churches and other places of worship. Moreover, this conclusion is also buttressed by the research on marriage—many of the same organizations that would provide an opportunity to meet friends would also provide chances to meet potential mates. *See infra* text accompanying notes 236–39.

226. BROOKS, *supra* note 180, at 41–56; Myers & Diener, *supra* note 209, at 16.

227. BROOKS, *supra* note 180, at 43–44.

228. *Id.*

229. COLOMBO & HALL, *supra* note 28, at 4.

230. *See, e.g.,* Gergen, *supra* note 49, at 1434–43.

231. *See, e.g.,* BROOKS, *supra* note 180, at 52–56.

232. *See infra* Part IV.A.3.

233. Myers & Diener, *supra* note 209, at 15.

234. *Id.* To be sure, an overwhelming or unchallenging job can cause great distress. *See,*

suggest prioritizing groups that provide opportunities for people to engage in “flow”-producing activities, whether related to leisure or work. With respect to the former, this suggests aiding groups that encourage people to learn and engage in hobbies, sports, and similar leisure activities (in many respects, this would overlap with the groups discussed above with respect to friendship). For example, community centers and recreational facilities would be subsidized (such groups are not currently subsidized unless they help the poor).²³⁵ Moreover, this well-being factor, like that of friendship, suggests that nonparticipatory services (such as the opera) would not be subsidized as much as other organizations, but not because they help the rich instead of the poor; this is not to say that watching an opera does not bring one happiness, just that so doing might not maximize the bang for one’s happiness buck.

In regards to job-focused activities, these findings encourage funding programs (such as job training and vocational programs) that help people obtain and keep fulfilling jobs. We would also subsidize career counseling services that help people determine the best occupational “fits” for them and counseling for the recently unemployed (since doing nothing is often a contributor to unhappiness). Lastly, we might also fund daycare providers that allow people for whom full-time child raising is not satisfying to engage in a more pleasurable occupation. And again, these findings seem independent of income levels, which suggests that such programs would be subsidized for all, not simply those who are financially disadvantaged.

Marriage. Studies suggest that well-matched married people are happier than never-married, divorced, or separated people.²³⁶ Although the intersection of marriage and happiness is somewhat of a two-way circle, some evidence suggests that a happy marriage increases (and not just correlates with) happiness.²³⁷ The flip side, unfortunately, is that a poorly matched marriage can significantly contribute to unhappiness.²³⁸

What might these insights (assuming causation) suggest for charitable giving? First, they suggest expanding the institution of marriage to include same-sex marriages, as doing so would greatly increase the happiness of a number of individuals who cannot currently marry.²³⁹ To that end, groups opposing marriage

e.g., BROOKS, *supra* note 180, at 159; Myers & Diener, *supra* note 209, at 15. Almost 90% of Americans, however, have reported being satisfied or very satisfied with their jobs. BROOKS, *supra* note 180, at 157. For many then, a job does indeed bring happiness. *See also* Ed Diener & Martin E.P. Seligman, *Beyond Money: Toward an Economy of Well-Being*, 5 PSYCHOL. SCI. PUB. INT. 1 (2004) (reviewing factors in the workplace that influence well-being and showing how well-being on the job acts as a predictor for positive work behaviors and perhaps even profitability). The converse is also true: unemployment is strongly correlated with unhappiness, separate and apart from the effect unemployment has on income. Layard, *supra* note 176, at 3–4.

235. Griffith, *supra* note 8, at 1391.

236. BROOKS, *supra* note 180, at 60–65; Myers & Diener, *supra* note 209, at 15.

237. BROOKS, *supra* note 180, at 62. That said, at least one study has suggested a causal connection. *Id.* Causation is not inconsistent with a two-way effect; it may be the case that happier people are more likely to get married and that once they do, their pre-existing happiness increases.

238. *Id.* at 63–64.

239. Griffith, *supra* note 8, at 1390 n.139. Whether other individuals’ opposition to same-sex marriage should be considered is discussed in Part IV.A.3.

equality would not be subsidized.²⁴⁰ Second, these insights suggest that while we should encourage marriage, we should not do so willy-nilly, but instead encourage only good marriages. We thus might want to subsidize groups that counsel and educate unmarried couples who are contemplating getting married to help ensure that a higher percentage of marriages are good marriages. Along those lines, we would also want to subsidize groups that offer marriage counseling and work in other ways to strengthen existing marriages.²⁴¹ This is so because divorce, like a bad marriage, often brings unhappiness, and to the extent a bad marriage can become good, such a transformation should be encouraged.

These types of education and counseling groups have long been subsidized.²⁴² That said, viewing such groups through a happiness-maximizing utilitarian lens adds to our understanding of them because it can help resolve a recurring question: must these groups (which likely have tax-exempt status now as either “charitable” organizations providing a community benefit or as “educational” organizations) provide free or reduced-cost service to the poor? Under a happiness-maximizing framework, that question becomes moot. They would be subsidized because they maximize happiness, and the income levels of the beneficiaries would be irrelevant. Moreover, the question of marriage equality for same-sex couples illustrates another way in which using SWB helps narrow the charitable tax subsidies: groups that actively seek to prevent other individuals from taking part in activities or institutions which enhance SWB should not receive a subsidy.

Children. The relationship of children to happiness is more complicated. At first glance, it seems that the stress of raising children initially makes people less happy, not more.²⁴³ Under a utilitarian view of happiness as positive affect, a superficial implication would be that we should subsidize groups that discourage childbearing (abortion clinics and abstinence programs) and stop subsidizing groups that encourage childbearing (including childcare facilities, which one might argue encourage people to have children by making life easier after they do).

This result, of course, seems odd. One alternative is to recognize that people have children despite the predicted initial decline in happiness, which makes it appropriate to subsidize groups that will minimize the unhappiness that accompanies parents with young children. This could mean subsidizing new parent groups, counseling for new parents and those with postpartum depression, parks, children’s play groups, childcare providers, and so on. Another alternative is to focus on happiness as overall life satisfaction, in which one could feel that having children is satisfying, even if it does not immediately produce a pleasant mental state in the parent.²⁴⁴ Regardless, many of the groups just mentioned are already subsidized²⁴⁵—but focusing on happiness instead of income removes the question

240. This may or may not mirror the conclusion that one would come to using preference satisfaction as a metric. Under preference satisfaction, whether pro- or antigay marriage groups would be subsidized depends on which side has the largest number of supporters.

241. See BROOKS, *supra* note 180, at 74.

242. See Rev. Rul. 70-640, 1970-2 C.B. 117.

243. BROOKS, *supra* note 180, at 65–66.

244. *Id.* at 69–70. Defining utility as preference satisfaction or under an objective-list approach would also treat having children as welfare enhancing.

245. For examples of such groups, see BOULDER DAY NURSERY, <http://>

of whether such groups should be required to offer free or reduced-cost services to the poor.

Short Commutes. Another determinant of happiness—one that may initially surprise many—is the effect of commuting: the longer one’s commute, the more it contributes to unhappiness.²⁴⁶ Conversely, decreasing one’s commute time increases happiness. Upon reflection, however, this makes sense. In addition to the actual stress of driving, the more time one spends in the car, the less time one has left for other activities that do increase happiness. For example, less time with one’s spouse may make it harder to maintain a happy marriage, and more time in the car may also mean less time for friends and hobbies. This might suggest that certain housing opportunities (such as those near places of employment) should be subsidized regardless of income (current law generally requires housing assistance groups to either help the poor or foster integration).²⁴⁷

Health and Disability. Some studies suggest that after a period of adaptation, people’s general levels of happiness seem to adjust after losing a leg or experiencing a similar disability.²⁴⁸ If true,²⁴⁹ these results suggest that aid to the disabled simply because they are disabled would not enhance utility understood as happiness—a result which likely surprises many. However, disabilities can often lead to other experiences which do impact happiness, including long periods of chronic pain and under- or unemployment.²⁵⁰ These experiences should be viewed separately from the disability per se, and instead be addressed via charitable-giving policy. On the health side, severe and chronic pain, as well as mental disorders, are strongly correlated with unhappiness; in light of this finding, such disorders should likely merit more of a subsidy than they currently receive.²⁵¹ On the flip side, exercise is strongly associated with happiness,²⁵² which supports the subsidizing of rec centers and gyms such as the YMCA without regard to whether they help the poor or not.

3. Using Subjective Well-Being: Complications

Given the increasing number of studies addressing the relationship of public policy and SWB,²⁵³ one’s initial instinct is that the foregoing has potential to offer

www.boulderdaynursery.org; NURSE-FAM. PARTNERSHIP, <http://www.nursefamilypartnership.org/about>; POSTPARTUM RESOURCE CENTER N.Y., INC., <http://www.postpartumny.org/>.

246. See, e.g., Alois Stutzer & Bruno S. Frey, *Stress That Doesn’t Pay: The Commuting Paradox* 3 (Inst. for the Study of Labor, Discussion Paper No. 1278, 2004).

247. See Rev. Rul. 70-585, 1970-2 C.B. 115.

248. GILBERT, *supra* note 215, at 153; Myers & Diener, *supra* note 209, at 16; David A. Weisbach, *A Welfarist Approach to Disabilities* 20 (Univ. of Chi. Law Sch. John M. Olin Law & Econ., Working Paper No. 355, 2007), available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1008985.

249. See Weisbach, *supra* note 248, at 20–21 for a critique of these studies and results.

250. *Id.* at 17.

251. Layard, *supra* note 176, at 8.

252. See Daniel Mochon, Michael I. Norton & Dan Ariely, *Getting Off the Hedonic Treadmill, One Step at a Time: The Impact of Regular Religious Practice and Exercise on Well-Being*, 29 J. ECON. PSYCHOL. 632, 632 (2008).

253. For an example, see generally DEREK BOK, *THE POLITICS OF HAPPINESS: WHAT GOVERNMENT CAN LEARN FROM THE NEW RESEARCH ON WELL-BEING* (2010).

very concrete guidance for charitable-giving policy: the types of activities associated with the largest increases in SWB would receive higher subsidies. Furthermore, efficiency and pluralism could still be respected in that individual donors would still decide how best to promote the activity in question (be it more exercise, say, or participation in an arts program). That said, a few complications must be addressed.

a. Defining SWB

Although the foregoing discussion has equated subjective well-being with one's overall life satisfaction, some SWB theorists subscribe to alternative conceptions of well-being. For example, a related but distinct conception of subjective well-being is "positive affect," which is the actual experience of feeling positive sensations (such as pleasure) on a moment-to-moment basis.²⁵⁴ Under this view of well-being, a person's life is comprised of a series of moments. At each moment, one is experiencing either a positive sensation (pleasure from eating a chocolate chip cookie) or a negative one (pain from touching a hot stove).²⁵⁵ Welfare thus consists of "the aggregate of a person's moment-by-moment experiences of positive and negative feeling."²⁵⁶

Although happiness as reported by life satisfaction surveys often correlates with happiness as measured moment to moment, this is not always true. And although many factors associated with happiness on balance are also associated with positive affect, not all are. To illustrate, some evidence suggests that although married people report higher levels of overall life satisfaction, they do not report higher levels of moment-to-moment happiness.²⁵⁷ Likewise, having children correlates with decreased affect but positive overall life satisfaction. Thus, choosing a

254. This conception of well-being is favored by Daniel Kahneman, among others, who is considered the father of scholarship on SWB. See Bronsteen et al., *supra* note 198, at 1587. Although this framework divides feelings into "positive" and "negative" ones, it recognizes that a variety of different feelings (love, joy, and awe, for example) all contain a "sensation of positivity—being drawn to the feeling rather than away from it." *Id.* at 1592.

A hybrid approach favored by some is that of "authentic happiness," which stems from the work of psychologist Martin Seligman. Under this view, "well-being comes from engaging our strengths and virtues" and engaging in valuable activities, whether or not they produce a positive affect. In a sense, the theory combines a number of conceptions of welfare. It recognizes that pleasurable feelings are valuable (as does positive affect) but also that there is value in using one's strengths for purposes other than making oneself happy (as do objective list conceptions of welfare). Peter H. Huang, *Authentic Happiness, Self-Knowledge and Legal Policy*, 9 MINN. J.L. SCI. & TECH. 755, 755–56 (2008).

255. Bronsteen et al., *supra* note 198, at 1590.

256. *Id.* at 1591. Two methods are generally used to measure this type of happiness. The first is the experience sampling method, in which subjects randomly receive signals throughout the day on a palmtop computer. Each time participants receive a signal, they indicate what they are doing and how they are feeling at that moment. *Id.* at 1597. The second method is known as the day reconstruction method. At the end of each day, subjects identify all the activities in which they engaged and label the emotions accompanying each activity. *Id.* at 1597 n.45.

257. Huang, *supra* note 178, at 21.5.

definition of SWB could affect which groups are subsidized; for example, groups that encourage childrearing might be subsidized under the overall life satisfaction definition, but not the positive affect model.

b. Measuring SWB

A second problem in using these insights for charitable-giving policy is that debate exists as to their validity. In addition to the potential errors and biases noted above, critics note that the way questions are framed can affect responses.²⁵⁸ It might also be the case that people are afraid to answer honestly. On the other hand, several indicators exist to show that well-being can be measured by the methods discussed. First, there seems to be a large overlap between moment-to-moment affect and overall life satisfaction,²⁵⁹ which suggests that the two are measuring something in common, whatever it may be. Second, people who report themselves as being happy are usually also described as such by those who know them.²⁶⁰ And lastly, self-reported mood during a variety of activities is strongly correlated with brain measurements²⁶¹ and with facial expressions.²⁶² These measurement doubts undermine the use of SWB to judge the impact of the charitable tax subsidies, much like Part III.B illustrated why similar measurement problems plague the use of traditional utilitarianism in this context.

c. Genetics and Adaptation

Assuming SWB could be measured, two further problems arise. First is the question of how much one's SWB is determined by genetics as opposed to environmental factors. If the role of genetics far outweighs that of outside influences, it seems odd to design institutions to maximize a fairly immutable attribute.²⁶³ Second, people often adapt to new circumstances after a period of time, reverting to their prior levels of happiness.²⁶⁴ This too suggests that policy attempts to increase happiness might not have lasting effects.

258. See, e.g., Adler, *supra* note 192, at 1918.

259. See Bronsteen et al., *supra* note 198, at 1599.

260. *Id.*

261. Richard Layard, Lecture at the Lionel Robbins Memorial Lectures of the London School of Economics: *Happiness: Has Social Science A Clue?* 8–9 (Mar. 3, 2003), <http://cep.lse.ac.uk/events/lectures/layard/RL030303.pdf>

262. Bronsteen et al., *supra* note 198, at 1599.

263. Current evidence suggests that genetics account for roughly 50% of one's happiness. BOK, *supra* note 253, at 53–54. If future studies indicate that genetics play a greater role, this would suggest that policies to improve happiness have less of an impact.

264. See Shane Frederick & George Loewenstein, *Hedonic Adaptation*, in WELL-BEING: THE FOUNDATIONS OF HEDONIC PSYCHOLOGY 302, 302 (Daniel Kahneman et al. eds., 1st papercover ed. 2003); John Bronsteen, Christopher Buccafusco & Jonathan S. Masur, *Hedonic Adaptation and the Settlement of Civil Lawsuits*, 108 COLUM. L. REV. 1516, 1534 (2008).

d. People Are Unique

The main problem, however, in attempting to implement the charitable tax subsidies to maximize happiness is that different things give different people pleasure and pain. While some find great pleasure in the opera, for example, I find attending the opera quite painful. But I enjoy the ballet, which others might find painful. And even though most people are made happier by close social groups, a true introvert might not be. Likewise, although most people are made happier by marrying, some are happier remaining (or becoming once again) single.

Yet if we use SWB-based utilitarianism to prioritize those activities which most commonly increase happiness, people whose welfare is affected by less common factors are disadvantaged.²⁶⁵ So what? one might ask. Doesn't every government policy decision create winners and losers? And given our majoritarian system of government, aren't those with unusual or minority tastes usually the losers?

Although true, this is precisely the problem with importing SWB analysis to the charitable sector. One key nondistributional role of the sector is to protect those in the minority when it comes to the funding of public goods. Maybe the majority votes to fund public parks and pools that give them pleasure; the minority uses the charitable tax subsidies to partially fund the opera houses that make them happy. So a distributive metric for the charitable tax subsidies that anchors them to elements that most commonly make people happy directly undercuts the diversity provided by the sector. And more disturbingly, importing SWB analysis to the charitable sector disadvantages individuals based on immutable, intrinsic characteristics—what makes them happy. Thus, using happiness as the sole anchor for judging the distributive consequences of the charitable tax subsidies is problematic.

C. Objective List Conceptions of Well-Being

A final—and very different—strand of well-being theories holds that well-being consists of more than just feeling happy or having one's preferences satisfied. Instead, these "objective list" theories provide an inventory of "goods" that are considered necessary for individual well-being or welfare, whether or not they make a given individual happy or reflect her desires.²⁶⁶ Although not characterized as such, the capabilities identified by Nussbaum are indicative of what such a list might look like.²⁶⁷ As articulated by Nussbaum, society should provide the following basic capabilities to ensure the welfare of each citizen:

265. This might be done, for example, by subsidizing more heavily than others those ten (or some other number) activities that are correlated with the largest increases in SWB. *See generally* Layard, *supra* note 176.

266. MATTHEW D. ADLER, *WELL-BEING AND FAIR DISTRIBUTION: BEYOND COST-BENEFIT ANALYSIS* 165 (2012).

267. Martha C. Nussbaum, *Capabilities as Fundamental Entitlements: Sen and Social Justice*, 9 *FEMINIST ECON.* 33, 41–42 (2003). Nussbaum is extending the work of Sen, who argues that a person's capabilities (that is, his ability to achieve certain functionings such as adequate nourishment) are the best measure of well-being. *See generally* AMARTYA SEN, *COMMODITIES AND CAPABILITIES* (1999); AMARTYA SEN, *INEQUALITY REEXAMINED* (1992).

- life (“[b]eing able to live to the end of a human life of normal length”);
- bodily health (having good health, including adequate nourishment and adequate shelter);
- bodily integrity (freedom of movement, security from assault and violence, sexual choice and opportunity);
- senses, imagination, and thought (using the senses to think, imagine, reason, and create and having the education necessary to do so);
- emotions (having “attachments to things and people” and being able to love and experience other emotions);
- practical reason (“[b]eing able to form a conception of the good”);
- affiliation (“[b]eing able to live with and toward others . . . to engage in . . . social interaction,” as well as being treated as an equal of dignified worth);
- other species (concern for other species and the environment);
- play (“[b]eing able to laugh, to play, to enjoy recreational activities”); and
- control over environment (participating in political choices as well as opportunities to hold property and employment).²⁶⁸

Other lists contain a number of themes in common with Nussbaum’s. David Braybrooke lists a life-supporting relationship to the environment, food and water, exercise, rest, excretion, bodily preservation, companionship, sexual activity, education, recreation, social acceptance, and freedom from fright and harassment.²⁶⁹ John Finnis includes “life, knowledge, play, aesthetic experience, sociability, practical reasonableness, and religion.”²⁷⁰ George Sher mentions “moral goodness; rational activity; the development of one’s abilities; having children and being a good parent; knowledge; and the awareness of true beauty.”²⁷¹

Although these examples are just that—examples—and not a definitive recital of objective list theories, they illustrate the pros and cons of turning to an objective list conception of welfare for purposes of fleshing out charitable-giving policy. The capabilities approach provides an illustration. On one hand, using such an approach for distributional guidance supports a broad conception of charity by subsidizing a number of disparate activities (a conception much like our current structure). In particular, it defends the current structure against criticisms that the sector does not

Although Sen and Nussbaum do not couch their approach as utilitarian, it has certain welfarist characteristics, for it seeks to identify what capabilities are necessary for individual welfare. Their approach is not consequentialist, however, for it seems to allow differences in functionings based on individual choices once basic capabilities are met. For that reason, I address the capabilities approach in more depth alongside the equality of opportunity theories, which also tolerate differences in outcomes. *See* Fleischer, *supra* note 3, at 631–32.

268. Nussbaum, *supra* note 267, at 41–42.

269. DAVID BRAYBROOKE, MEETING NEEDS 33–36 (1987) (synthesizing lists of needs that must be met to ensure human welfare created by the United Nations, the Organisation for Economic Co-operation and Development, and various philosophers).

270. ADLER, *supra* note 266, at 165.

271. *Id.* at 166.

do enough to benefit the poor and disadvantaged. Take the capability of “senses, imagination and thought.”²⁷² If art museums or the opera would not exist but for the charitable tax subsidies,²⁷³ then subsidizing such groups promotes aggregate welfare because having the opportunity to enjoy art is intrinsic to one’s well-being, regardless of financial status. It may be the case, however, that the wealthy already have a chance to develop that capability without tax-subsidized museums; in that case, such organizations would be required to somehow assist the poor in order to qualify. Put another way, offering opportunities to develop capabilities that would be absent—even for the wealthy—in a pure market setting enhances well-being under these definitions. But if the wealthy could purchase such opportunities in the market, then groups such as the opera would not enhance welfare unless they offer those opportunities to individuals unable to purchase them in the market.

On the other hand, choosing to use an objective list conception may create the most tension with the other goals of the sector. It requires two sets of value judgments: first, that an objective list approach is better than SWB or preference satisfaction, and second, that a given list is the best approach to implement. Choosing the capabilities approach, for instance, prioritizes that list’s conception of “the good” over other conceptions. In one sense, however, it still leaves some room for pluralism. Take the capability of “senses, imagination, and thought.” Encouraging the charitable sector (in addition to the government) to provide opportunities for the development of that capability is pluralistic in that it increases experimentation and variety in the way such opportunities are provided. Moreover, each of these lists seems to countenance such a broad range of charity that while they may defend the current structure from detractors, they do not do much to help us prioritize.

D. Concluding Thoughts on Well-Being

This exploration of the underlying attributes of well-being illustrates a dilemma. Prior scholars aimed to avoid value judgments by focusing on the seemingly value-neutral goals of efficiency and pluralism.²⁷⁴ But as argued previously, those goals often implicitly celebrate the welfare gains from preference satisfaction.²⁷⁵ And as this Part has shown, looking more explicitly at preference satisfaction has its own problems, for the current structure adequately addresses neither the preferences of beneficiaries and the public at large nor the dilemma of donors with contrasting controversial preferences.

Moving beyond preference satisfaction to an objective list approach or to SWB is somewhat more helpful, but still challenging. Maximizing SWB provides more protection against some individuals imposing their preferences about societal problems on others than does a preference satisfaction approach, but also disadvantages individuals made happy by quirky or unusual activities. It thus furthers one aspect of the minority-protecting role of the charitable tax subsidies

272. Nussbaum, *supra* note 267, at 41.

273. See Hansmann, *supra* note 137, at 854–59.

274. See Gergen, *supra* note 49, at 1396; *supra* notes 52–62 and accompanying text.

275. In some cases, they may be prized on equality of opportunity grounds.

while undercutting another aspect of that same role. And lastly, using an objective list approach requires choosing among objective lists, although it does leave room for experimentation in the way the various items on the list are provided. But it seems a bit heavy-handed to tie the charitable tax subsidies to such a specific vision of the “good,” given our pluralistic society.

V. A BRIEF WORD ABOUT THE LEXIMIN

Although utilitarianism is the most common welfarist approach in tax policy, it is not the only such framework. A second welfarist theory of justice commonly invoked by tax theorists is the leximin, under which a just system of distribution maximizes the well-being of the least advantaged.²⁷⁶ Such an approach would simultaneously result in a narrower deduction than under the models explored above, for it suggests that groups must be required to assist the least advantaged in order to merit a deduction. And if the least advantaged were defined in financial terms (as is most often the case),²⁷⁷ the leximin would be much easier to apply than traditional utilitarianism. Instead of looking at the relative incomes of donors and beneficiaries, one would only need to determine if individuals under some defined income level were benefited.²⁷⁸

The catch, however, is determining who qualifies as the “least advantaged.” Should it be defined solely in terms of income or wealth, as is traditionally done? Or should it be defined in terms of one of the alternative measures of welfare explored above? For example, it may be the case that the unhealthy or the perpetually depressed should be considered disadvantaged. And under some metrics, it seems quite plausible to consider families fleeing Hurricane Katrina or reeling from the death of a loved one after the September 11 attacks (to name but two examples) as among our country’s least advantaged. Prospect theory’s emphasis on loss also supports this interpretation.²⁷⁹ But as we saw in Part I.C, current law struggles with the treatment of financially well-off disaster victims. Regardless of which definition is used, however, we see the same paradox again: even though some interpretations of the leximin might suggest that charities should not be required to help the poor, value-laden definitional issues undercut the theory’s guidance.

CONCLUSION

This Article has explored the interaction of utilitarianism and charitable giving for insights into some of the recurring distributional questions concerning the

276. See, e.g., Bankman & Griffith, *supra* note 6, at 1949–50; Zelenak & Moreland, *supra* note 110, at 53.

277. This is basically how Rawls defines the least advantaged when discussing the difference principle. See RAWLS, *supra* note 10, at 65–70 (emphasizing income and wealth when illustrating the difference principle); Mark S. Stein, *Rawls on Redistribution to the Disabled*, 6 GEO. MASON L. REV. 997, 999 (1998) (noting that Rawls “almost exclusively” focuses on income and wealth when interpreting the difference principle).

278. Perhaps the poverty line, or some percentage thereof, could demarcate this level.

279. See Part III.B.2.b.

charitable tax subsidies. When it comes to utilitarianism as traditionally applied in tax policy, this Article contradicts the conventional wisdom that there is nothing special about organizations that assist the poor. In contrast, this Article has argued that a nuanced analysis of traditional utilitarianism suggests that charities assisting the underprivileged do deserve special treatment. This is not to say that only organizations that help the poor should be subsidized given the important roles the sector plays in enhancing pluralism and efficiency—just that there is something special about those organizations.

In theory, other conceptions of utilitarianism common in legal scholarship (preference satisfaction, subjective well-being, and objective list approaches) initially support the conventional wisdom. This Article has also shown, however, that each of these theories has intrinsic drawbacks that damage the sector's pluralistic goals. As a result, none of these well-being theories—when viewed in isolation—is a useful tool for answering the distributive questions faced by the sector.

However, looking at these theories in conjunction with one another offers a way around these problems: donative organizations that help the poor likely enhance welfare under all the welfare-based theories just discussed. Such giving almost certainly enhances utility as traditionally defined by tax theorists. And while the SWB theories suggest that past a certain point money does not buy happiness, they suggest the opposite for individuals below a subsistence amount.²⁸⁰ This makes intuitive sense, as we can imagine that lacking funds for basic life necessities such as food, clothing, and shelter would create misery and stress. Thus, assisting the very poorest almost certainly increases SWB.²⁸¹ Moreover, the very poorest almost certainly need assistance from the nonprofit sector to access the capabilities and goods that most commonly appear on objective list approaches. (To be sure, each theory would subsidize a unique range of organizations, so long as the organization increased aggregate utility as defined by that interpretation.) But the important point is that what each theory has in common with each other—and with equal opportunity theories and the leximin—is the funding of groups that help the poor. Thus, acknowledging that such groups are special does not contradict the sector's pluralism goals.

Deciding what it means to prioritize such organizations, however, does involve making decisions about the relative weight to give pluralism, efficiency, and distributive concerns. Should prioritizing the poor mean requiring organizations that provide goods and services to identifiable beneficiaries²⁸² to offer some

280. BOK, *supra* note 253, at 13–14; Griffith, *supra* note 8, at 1372–74; Myers & Diener, *supra* note 209, at 13.

281. It is also the case that lower-income individuals, for whatever reason, do not participate in several other activities that correlate with high levels of SWB, such as marriage and engagement in social and civic groups. *See generally* CHARLES MURRAY, *COMING APART: THE STATE OF WHITE AMERICA 1960–2010* (2012). This provides another ground for thinking that aid to the poor could do more to increase aggregate happiness than other types of aid.

282. Groups that provide goods and services to identifiable beneficiaries include schools, hospitals, museums, and so on—in contrast to environmental or medical research groups, which do not really have identifiable beneficiaries.

percentage of free or reduced-cost services?²⁸³ Should it mean subsidizing groups that assist the poor more heavily than other groups, while still continuing to subsidize other groups passing the public goods test?²⁸⁴ Or should it mean nothing more than requiring policymakers to expressly consider the impact on the poor of proposed changes to the tax subsidies? Unfortunately, these questions—as well as defining who qualifies as poor and disadvantaged—require more attention than this Article can give. To that end, they are left for the last part of this series. This Article’s contribution to the literature is to illustrate, in the first instance, that utilitarianism suggests such groups are special—an issue about which current law and scholarship is confused.

283. Texas, for example, requires nonprofit hospitals that wish to qualify for tax-exemption to provide a specified amount of charity care. TEX. TAX CODE ANN. § 11.1801(a) (West 2008).

284. For a short discussion of how this might be implemented as a practical measure, see Fleischer, *supra* note 3, at 660–61.