Personal Deductions Revisited: Why They Fit Poorly in an “Ideal” Income Tax and Why They Fit Worse in a Far from Ideal World

Mark G. Kelman*

This article is an extended comment on Professor William Andrews’s Personal Deductions in an Ideal Income Tax.1 Professor Andrews essentially argues that the tax base should take into account the different uses to which people put their money, and that the tax system ought to treat taxpayers who use their money for charitable contributions or medical care as if they had never received that money at all.2

Professor Andrews rejects the common argument for building a concept of uses into the tax base that relies on social or economic purposes “extrinsic” to the tax system.3 Under that view, if Congress favors charity and health, it can use tax law to encourage charitable giving or purchases of medical care, or finance charitable giving or medical expenditures that would occur regardless of the tax laws. Though Congress could encourage or finance charitable or medical services through direct grants to the proper parties, it can achieve the same goals, perhaps at lower administrative cost, by allowing taxpay-

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2. I use the term “received” rather than “earned” deliberately; distinctions between earned and unearned items are unimportant in determining whether an item ought to be included in the tax base. See Commissioner v. Glenshaw Glass Co., 348 U.S. 426 (1955); I.R.C. § 61. It is plausible, but irrelevant to my argument, that unearned income should be taxed at a higher rate than earned income, since the latter requires a sacrifice of leisure while the former does not. See generally H. Simons, Personal Income Taxation 111 (1938).
3. The idea that there are “intrinsic” and “extrinsic” (or, as Professor Andrews says, “extraneous,” Andrews, supra note 1, at 311–12) purposes to a single taxing statute is implausible. I simply follow the conventional language in this regard.
ners to deduct the amount they spend on such favored uses. For example, if a 40 percent marginal-rate taxpayer makes a medical expenditure that costs $10,000 pretax, it will cost her only $6,000 after tax: The government might believe that the prospect of such savings will encourage the taxpayer to purchaser a higher, more desirable level of medical care, or simply might be willing to finance the medical expenditure to the extent of $4,000. The $4,000 that the deduction scheme takes away from the government is called a "tax expenditure" to distinguish it from a direct grant to the favored party.

The shortcomings of supporting social and economic goals through "tax expenditures" rather than direct grants are now familiar. As a way of encouraging the purchase of medical care, for example, the deduction scheme is irrational: To encourage low-income taxpayers to purchase more medical care, the government has wasted a great deal of money by setting the price for richer taxpayers lower


This "tax expenditure" rationale has probably been the most important influence in the development of the charitable contribution deduction provision, I.R.C. § 170. See Liles & Blum, Development of the Federal Tax Treatment of Charities, 39 Law & Contemp. Prob. 6 (1975). Most of the literature supporting the charitable deduction has assumed that the government should support philanthropic institutions; the question has been whether the use of a tax deduction, rather than direct government support, is the best means. The classic antideduction position is that taken in McDaniel, Federal Matching Grants for Charitable Contributions: A Substitute for the Income Tax Deduction, 27 Tax L. Rev. 377 (1972) (charitable contribution deductions are both an inefficient and inequitable method of funneling government money to private philanthropies). The argument that the deduction effectively encourages charitable giving at comparatively low cost to the government is made most forcefully in Feldstein, The Income Tax and Charitable Contributions: Part I—Aggregate and Distributional Effects, 28 Nat'l Tax J. 81 (1975). For further discussions of the efficiency and fairness of the charitable deduction, see Bittker, The Property and Vitality of a Federal Income Tax Deduction for Private Philanthropy, in Tax Impacts on Philanthropy 145 (1972); Surrey, Tax Reform, supra, at 384-87; Taussig, Economic Aspects of the Personal Income Tax Treatment of Charitable Contributions, 20 Nat'l Tax J. 1 (1967); Wolkoff, Proposal for a Radical Alternative to the Charitable Deduction, 1973 U. Ill. L.F. 279.

5. Even if the demand for medical care were completely price inelastic—that is, the taxpayer would demand the same quantity of care regardless of cost—a medical care deduction would act as a mandatory federal insurance program. Those without medical bills would pay higher taxes than those with such bills, and some of the financial risks of disease would be automatically pooled.

than necessary to encourage them to purchase an appropriate amount of medical care. As a way of financing medical care, the scheme is simply unfair. If $A$, a 50 percent bracket taxpayer, and $B$, a 20 percent bracket taxpayer, each spend $10,000 on doctors, the government will support $A$'s expenditure by $5,000 and $B$'s by only $2,000. It is hard to imagine Congressmen advocating a direct welfare spending program that would reward people for being rich.

In place of the tax expenditure concept, Professor Andrews approves the charitable and medical deductions for reasons "intrinsic" to the tax system: The government can measure the taxpayer's very capacity to pay taxes, and the extent of the claims the tax system can justly make on her, only after excluding certain categories of uses from the tax base. My basic dispute with Professor Andrews concerns what constitutes the appropriate tax base.

Professor Andrews relies on Henry Simons's well-accepted principle that taxpayers ought to be taxed on income, which equals the sum of consumption and accumulation (or savings). But Professor Simons's definition does not illuminate my difference with Professor

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7. Assume that there are two classes: poor people (20% bracket taxpayers) and rich people (50% bracket taxpayers). A full 20% drop in medical care prices may be necessary to induce the poor to purchase the "appropriate" level of medical care, and so Congress allows full deductibility. But the full deductibility scheme for the rich does not induce purchase of the "appropriate" amount of medical care if the rich already purchase the appropriate amount of care at full price or with a 20% discount (the price drop will result in over-purchase) or if the additional 30% drop beyond the initial 20% discount caused little additional medical care spending (demand for medical services became relatively inelastic as prices dropped below the 20% discount level). Only if the rich require greater discounts to purchase more medical care than the poor would a deduction scheme plausibly work to induce an appropriate level of medical care spending by all taxpayers.

The arguments against financing charitable activities through tax deductions parallel the arguments in the medical deduction case. If Congress considers changes in the after-tax price of donating to have no effect on aggregate donations, then its goal is simply to finance charities. If we assume, for example, that total donations by itemizers equal $10 billion and that the average tax rate of donors, weighted by their level of contribution, is 30%, then Congress makes a tax expenditure of $3 billion by allowing the charitable contribution deduction. Yet, although Congress did not so intend, this $3 billion will be distributed perversely; those charities that the higher bracket taxpayers favor will receive more federal funds. If, however, the charitable deduction is viewed as a legislative attempt to encourage giving, the targeting problems that arise in the medical care context surface here also: Prices are dropped more for the rich than the poor.

A tax expenditure program that funnels federal money to religious organizations also raises serious first amendment problems. See, e.g., McDaniel, supra note 4, at 409–11; Stone, Federal Tax Support of Charities and Other Exempt Organizations: The Need for a National Policy, 1968 S. CAL. TAX. INST. 27, 54–55.

10. Id. at 313.
Andrews. My view is that a taxpayer's net receipts, receipts minus the cost of obtaining the receipts, *tautologically* consists of consumption plus savings. All money the taxpayer controls or "voluntarily" disposes of must go to either consumption or savings. The critical problem is to define "consumption" (using money to obtain satisfaction).12

Professor Andrews has narrowed the meaning of consumption and, in effect, has identified certain uses of money which are strictly neither savings nor consumption. A use is not consumption unless it is a "private preclusive appropriation" of resources. And even uses that are private preclusive appropriations will not constitute consumption unless they improve the taxpayer's position beyond a baseline psychic condition of tax-free health. Thus, charitable donations are not consumption, even though they may give the donor as much personal satisfaction as ordinary spending, because the donor does not appropriate goods or services for her private preclusive use. Medical expenditures, even though they clearly involve the private preclusive appropriation of goods and services, are not consumption because they simply restore the level of health that the taxpayer enjoyed, tax-free, before illness or injury occurred.

I hope to demonstrate that Professor Andrews's notion of private preclusive appropriation is unconvincing, and in any event would not logically justify the charitable deduction. And while some deduction for medical care might be supportable, Professor Andrews's argument, which allows deduction for all actual expenditures on what is conventionally deemed medical care (and which falls back on a dubious assumption that Congress can alter rates to correct vertical inequities caused by the deduction) is ultimately unpersuasive. Moreover, Professor Andrews regularly makes unfounded empirical assumptions to suppress the weaknesses of his case, and these assumptions consistently contravene progressivity and ignore the effect of differences in economic class on the nature of charitable and medical spending.

11. For a more complete discussion of what constitutes a "voluntary" disposition, particularly in the difficult context of defending a casualty loss deduction, see note 87 infra and accompanying text.

I will affirmatively argue that a net receipts tax base would respond to two major concerns in designing a tax system: The tax system ought to measure inequality in earnings capacity, and yet respect a taxpayer’s decision not to fulfill her earnings capacity. While the tax system should not force a taxpayer to take dominion over as many resources as she is able, once she voluntarily takes control of resources, her particular subsequent uses of those resources are irrelevant to tax law.

I. THE CHARITABLE DEDUCTION

Section 170 of the Internal Revenue Code allows itemizing taxpayers to deduct a certain portion of their contributions to religious, educational, and charitable organizations falling within the definitions of Subchapter F. (The mechanics of the section are unimportant here.) I will examine variations on Professor Andrews’s strongest case for deductibility: a taxpayer who anonymously donates money to a charitable organization which acts as a conduit, sending money to poor people who spend it however they wish.


14. Andrews, supra note 1, at 347–56. Professor Andrews never explicitly deals with three conditions that characterize the strongest case for deductibility. First, the donor must be anonymous with respect to the donees, charitable organizations, and his community in general. If the donor is not anonymous, he will “purchase” deference or respect with his donation. Professor Andrews’s argument that the tax system can ignore purchased deference because pure deference does not have a production cost is set out and criticized at notes 44–57 infra and accompanying text. Sometimes, of course, acting deferentially and respectfully does have a production cost to charitable recipients or others. Testimonial dinners or even thank-you notes cost something.

Second, the donor must not restrict the donee’s use of the funds, or he will be redirecting economic resources to his satisfaction. See notes 62–64 infra and accompanying text. Third, the donor must not receive direct services from the donee. Professor Andrews concedes that in the dominant form of deductible giving, donations to nonconduit philanthropies like museums and symphonies, benefits may flow directly to the donor. Andrews, supra note 1, at 346. He argues, though, that because philanthropic organizations provide “common” or “public” goods, services received by the donor therefore do not correspond to the amount of his donation. Thus, this sort of spending also differs from “ordinary” consumptive spending. Id. at 357–70. If, as I will argue, the donor should not receive a deduction when he receives no concrete services from the donees, as in the almsgiving case, then, a fortiori, deductibility cannot be defended simply because the value of the concrete services he receives is not a direct function of the amount he spends. Although I will not directly discuss the propriety of deducting philanthropic donations, my comments on restricted grants are relevant to philanthropic donations. See notes 58–61 infra and accompanying text.
Assume two taxpayers: $X$, with net receipts of $60,000$ a year, donates $10,000$ to a conduit charity, while $Y$, with net receipts of $50,000$, donates nothing. Section 170 dictates that $X$ and $Y$ be taxed alike, as if each had receipts of $50,000$. Professor Andrews supports this approach by noting that $X$’s special use of his funds justifies their exclusion from his income. In donating the $10,000, X$ is not using the money to privately and preclusively appropriate any of society’s goods or services.\textsuperscript{15}

A. Professor Andrews’s Arguments for the Charitable Deduction: A Capsule View

Professor Andrews begins by distinguishing charitable from ordinary giving. He suggests that, in principle, ordinary gifts should, like charitable gifts, be deductible for the donor, but included in the tax base of the donee, who presumably consumes goods and services with the donated money. However, since ordinary gifts do not shift income outside the household,\textsuperscript{16} two factors argue against deductibility: administrative convenience and the need to protect the progressive rate structure by blocking high-bracket household members from assigning their income to lower-bracket members.\textsuperscript{17} But this argument assumes the chief point of contention between Professor Andrews and myself: that the donor does not consume what he donates, and thus that the gift should be included only in the consuming donee’s income.\textsuperscript{18} I will therefore not deal with this argu-

\textsuperscript{15} Andrews, supra note 1, at 346, 356.

\textsuperscript{16} Id. at 348-49. Professor Andrews argues that the household is the appropriate unit for rate-determination, if the income tax is understood as “an indirectly measured tax on personal consumption,” because “consumption and accumulation are largely household functions.” Id.

\textsuperscript{17} “[I]ntrafamily gifts . . . often go from a high bracket adult to a child in a lower bracket.” Id. at 348.

\textsuperscript{18} Id. at 347. Professor Andrews argues that if $X$ gives money via a conduit charity to a poor person, the poor person consumes the goods and services or saves the money. To tax such consumption or savings at $X$’s higher rates would violate congressional intentions about vertical equity. Id. He recognizes that in the case of ordinary gifts, the donor, rather than the donee, is taxed, id. at 348, but correctly notes that the charitable case can be distinguished because in the case of most ordinary gifts consumption is not shifted outside the household. Id. at 348-49. If the household is generally the appropriate taxpaying unit, or if gifts within households can never be scrutinized to determine the genuineness of the transfer, then it might be administratively sensible to ignore such transfers.

All Professor Andrews is noting is that if there is to be only one tax there are reasons in the ordinary gift case which do not apply in the charitable area to deny the donor a deduction and exclude the transferred funds from the donee’s income instead. This argument says nothing about whether both donor and donee ought to be taxed, as they would be under a net receipts tax system. In essence, this first argument is a tautology: if one assumes both that
ment directly at length, but will concentrate on his two other key arguments.

Assume $X$ is a doctor working 4 days a week in private practice for $50,000 per year, and 1 day per week in a free clinic for the poor. Now assume she decides to spend the 5th day in her private practice and give the income from that day to the poor. Professor Andrews believes that since the doctor is ultimately putting her services to the same use in the two situations—benefiting the poor—the tax treatment should be the same.\footnote{19}

But what should that tax treatment be? In seeking an answer, we might look to the treatment of an analogous situation: a doctor providing services without charge within her own household. The tax system allows the doctor to exclude from her taxable income the imputed income from these services. But Professor Andrews notes a special reason for this treatment: The potential to generate income from these household services is ultimately trivial:

The goods or services one can produce for use within his own household are limited in value because the processes employed cannot be brought to bear upon a large enough volume of production to generate the kind of high pay that the performance of specialized services will command in an exchange economy. A doctor performing services within his own household, for example, will not usually find enough sickness to be able to produce a large volume of medical services. . . . \cite{Andrews}While an entertainer may earn large fees for performing before large audiences, the imputed income that escapes tax when he performs at home for his family is very limited if measured by the relative size of his audience. . . .

But there is no such built-in limitation with respect to the performance of services in kind for a charity. . . . \cite{Andrews}An entertainer

\footnote{taxable income equals some narrowly defined consumption plus savings, and that charitable giving is not consumption, then charitable giving should be excluded from the tax base. This article will not discuss whether, as a general matter, it is appropriate to include transferred funds in the income tax base of both donor and donee, because the donee clearly has an accretion to wellbeing upon receipt and the donor presumably has spent his money as he wanted. I.R.C. \S\ 102 mandates single inclusion in the case of gifts. I do not think an attempt to distinguish between transfers of funds as purchases as opposed to gifts will help us decide whether taxing both the transferor and the transferee constitutes unjust "double taxation." A "household-as-taxpaying-unit" principle better explains our instincts about what constitutes a double tax than does a "gifts-are-not-consumption" principle.}

The Carter Commission tax reform proposal in Canada would have double-taxed \"gifts\" when the transfers went outside "households," which were defined rather narrowly in terms of ages and family relationships. \cite{Carter}See \textit{1 Report of the Royal Comm\'n on Taxation} 19 (1966).

\footnote{Andrews, \textit{supra} note 1, at 347-48.}
may perform for charity before a large audience.\footnote{Id. at 352–53 (footnote omitted). The fact that the income lost from the tax base is small, of course, dictates exclusion for reasons of administrative convenience.} Obviously, these reasons could not justify exclusion of the imputed income from the doctor’s work at the free clinic. Therefore, Professor Andrews must look for another principle to justify excluding the value of both charitable services and donations, and he finds it in the notion of “private preclusive appropriation”:\footnote{Id. at 354–55.} Only uses which divert resources away from the satisfaction of other people’s wants constitute taxable consumption. Professor Andrews thus focuses on the supply side of the economy rather than the demand side in establishing a tax base. The charitable provider and donor may satisfy their personal demand for satisfaction (or “utility”) as much by donating as by ordinary consumptive spending, but they purportedly do so without making any claim on the economic resources society supplies.

Professor Andrews’s chain of reasoning can be broken down at both key links. First, I will argue that an important tax principle, which Professor Andrews ignores, justifies the exclusion of imputed income from the provision of services both to the household and to charities, and thus eliminates the need for the fallback concept of private preclusive appropriation. It is simply the principle that the trigger to taxability ought to be a person’s voluntary entrance into the market.

Second, even if a secondary explanation were needed, the private preclusive appropriation concept cannot suffice. The concept is ultimately without content. Even if it had discernible content, charitable giving would still have private preclusive elements. And even if we could find content in the concept and explain why charitable giving falls outside its boundaries, Professor Andrews has given us no satisfactory explanation of why that which is not private preclusive appropriation should not be part of the tax base.

The following sections elaborate these arguments.

B. \textit{Imputed Income: The Equivalence of the Decision to Donate Money or Services and the Principle Against Forced Marketing}

Professor Andrews argues that a voluntary decision to donate money ought to be treated the same as a voluntary decision not to earn money in the first place.\footnote{Id. at 348.} In general, people do not pay taxes
on income-earning capacity. If, after completing a residency program, Dr. X decides to become a beachcomber, she will not be taxed on the $60,000 per year she could have earned as a doctor, even though she presumably obtains as much personal satisfaction from leisure as she would from $60,000, or she would not make the trade. The tax system does not try to directly measure "satisfaction" or utility.

Professor Andrews's argument requires some elaboration beyond this principle that the tax system does not tax utility: It would indeed be inconsistent with other principles of the tax system to argue that the charitable service provider ought to pay tax on earning capacity simply because she would not have traded income for the joy of services unless she valued that joy as highly as the income. But ordinarily, a person becomes an appropriate target of taxation when she actually takes money in. Neither the person who chooses to receive psychic income rather than money through good deeds, nor the person who chooses to receive psychic income through leisure, pays any tax.

In the world of leisure-work trades, however, the person who

23. See I.R.C. § 61. The tax tables refer to earnings, not earnings capacity. I.R.C. § 1. Even in those cases where a taxpayer holds a readily marketable asset that has appreciated in value and "earning capacity" is thus easily transformed into earnings, tax is not paid on the appreciation until "realization"—until the asset is in fact marketed. Eisner v. Macomber, 252 U.S. 189 (1920). In his casebook, Professor Andrews implicitly defends the intuitive appeal of some realization requirement by posing hypothetical cases in which taxing prior to realization seems unjust. W. Andrews, Federal Income Taxation: Cases, Problems and Notes 149 (1968); see Mullock, The Constitutional Aspects of Realization, 31 U. Pitt. L. Rev. 615, 622 (1970) (16th amendment embodies realization requirement because word "incomes" used in "ordinary meaning"). For a critique of the realization requirement, at least in the context of certain readily marketable assets, see Slawson, Taxing As Ordinary Income the Appreciation of Publicly Held Stock, 76 Yale L.J. 623 (1967).

24. "[I]f a person's surroundings change in such a way that he could increase his satisfactions by altering his behavior, he will do so." R. Posner, Economic Analysis of Law § 1.1, at 4 (2d ed. 1977). Thus, any voluntary decision is "utility-maximizing." But utility in modern economic thought is not a psychological concept; it is simply the definition of what the voluntary trader "maximizes." See P. Samuelson, Collected Scientific Papers 3 (1966). Therefore, it is a technical error to say that the doctor-turned-beachcomber is as "well-off" in a psychic sense simply because she traded. Yet the normative pull of technical efficiency arguments, the ideal that Pareto-optimal movements are "optimal," is based on imparting some psychological meaning to the concept of utility.

25. See I.R.C. §§ 1, 61. The rate tables are based on money income, not happiness, and only receipts which can be valued in money terms are taxed. For critiques of hedonistic views of income, see H. Simons, supra note 2, at 5. Fagan, Recent and Contemporary Theories of Progressive Taxation, 46 J. Political Econ. 457 (1938); Kendrick, The Ability-to-Pay Theory of Taxation, 29 Am. Econ. Rev. 92 (1939).
forgoes psychic income by converting it into money does pay tax. Professor Andrews makes a 3-stage argument for reversing this presumption that trading psychic income for money should trigger taxability. First, he argues that while the tax base does not include the psychic income from leisure, it should as a matter of principle include imputed income from the provision of services.26 Generally, the form of receipt of income does not and should not matter in determining taxability.27 Thus, even when a taxpayer provides services within his own household, the household should in principle be taxed.28 While a doctor receives no taxable gain when she chooses to enjoy leisure rather than provide services, she does earn taxable income for her household when she performs marketable services for it.

Second, Professor Andrews notes that the only reason the tax system generally ignores the taxable income the doctor earns in treating family members is that the family’s limited capacity for illness severely limits the doctor’s opportunity to provide such medical service.29 This limit on potential taxable income does not exist in the charitable area, where the market of potential recipients of the service is wide. Thus a doctor’s provision of medical service to a charity would trigger taxability unless there were a separate principle excluding taxability for all charitable donations—whether of services or money. Professor Andrews argues that such a principle exists: The doctor should not be taxed unless she or her household consumes either the medical services she provides (imputed income) or the goods and services her money can buy (ordinary consumption).

The following diagram summarizes Professor Andrews’s reasoning:

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Nontaxable In Principle
leisure (purely psychic)
joy of giving (purely psychic)
services provided for other households (gains, if any, are purely psychic to taxpayer)
money provided to other households (gains, if any, are purely psychic to taxpayer)

Taxable
leisure, sacrificed and transformed into money used by taxpayer’s household

Taxable In Principle, But Administratively Nontaxable
leisure, sacrificed and transformed into household services
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27. See, e.g., Reginald Turner, 23 T.C.M. (P-H) ¶ 54,142 (1954) (steamship tickets received by taxpayer considered income though not received as cash or marketable property); S. Rep. No. 1622, 83d Cong., 2d Sess. 168 (1954) (although § 61 of 1954 Code omitted phrase “gains . . . in whatever form paid” found in § 22(a) of 1939 Code, “statutory gross income will continue to include income realized in any form”); Treas. Reg. § 1.61-1(a) (1957) (“Gross income includes income realized in any form, whether in money, property, or services.”).
29. Id. at 353.
I would argue that the appropriate lines are:

<table>
<thead>
<tr>
<th>Nontaxable In Principle</th>
<th>Taxable</th>
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<tbody>
<tr>
<td>leisure (psychic only, no forced marketing) services provided within the household (no forced marketing) services provided for charities (no forced marketing)</td>
<td>leisure sacrificed and transformed into money, regardless of use (tax system presumes each taxpayer’s use makes him as well off as any other use; no marketing has been forced)</td>
</tr>
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A central concern of the tax system is to tax people on their actual earnings rather than their *earning capacity* though the latter may be the ideal measure of ability to pay. An earnings capacity tax might best achieve the tax system’s goal of measuring the inequality of economic power. Looked at before the taxpayer earns income rather than after he has earned a determinable sum, an earnings capacity tax might also best assess the sacrifices a particular taxpayer is making when he is asked to give a certain sum of money to the state.

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30. An “earnings” capacity test must be refined to be a test of “income” (or “net receipts”) capacity. An earnings “capacity” test is nothing more than a prediction of what the taxpayer will receive if he exercises his capacity. Windfalls, from inheritance, gambling, or other sources, will never be predictable but must nevertheless be included in taxable income. It would be difficult to argue sensibly that a taxpayer received more than he had the capacity to receive; rather, receipts beyond predicted capacity simply demonstrate the limits of our prophetic abilities.

31. I do not find traditional accounts of the exclusion of “income that could have been earned” particularly cogent. In fact, many who assert the connection between ability to pay and capacity to make money quickly proceed to ignore it. For example, the *Report of the Royal Comm’n on Taxation*, supra note 18, at 10, declaims, “By adopting a base that measures changes in the power, *whether exercised or not*, to consume goods and services, we obtain . . . equity.” But it then simply urges narrowing the realization requirement for appreciated properties, not taxing capacity so that the taxpayer must choose to treat his potential labor time as a commodity. See generally J. Stamp, *The Fundamental Principles of Taxation* 25–54 (1918); Marsh, *The Taxation of Imputed Income*, 58 Political Sci. Q. 514 (1943); Musgrave, *In Defense of an Income Concept*, in *A Comprehensive Income Tax Base? A Debate* 62 (1967).

32. By “sacrifice” I refer to the debatable utilitarian principle that a graduated income tax will cause people to make equal “sacrifices” because the marginal utility of money declines. Thus, the loss of a fixed dollar amount will result in less utility loss for the wealthier taxpayer. See W. Blum & H. Kalven, *The Uneasy Case for Progressive Taxation* 56–64 (1953). Modern economics has generally dismissed the possibility of making interpersonal comparisons of utility. See, e.g., L. Robbins, *The Nature and Significance of Economic Science* 138–51 (2d ed. 1935). However, there have been significant attempts to resurrect the intuitively appealing concept that we inevitably make at least approximate interpersonal comparisons. For example, John Rawls views the extreme skepticism over making interpersonal utility comparisons as a subset of a questionable skepticism about the
However, there is a fundamental flaw in any capacity tax: The tax system ought not to force people into the market. To force the beachcomber to work as a doctor, to force people to work 5 days a week when they only want to work 3 days, or to force people to work in a location they dislike in order to earn the prevailing market wage so they can pay taxes—all this would violate the simple libertarian principle that the state should not require people, directly or indirectly, to engage in particular activities. But once the taxpayer has decided to enter the market, the tax system can certainly disregard how he chooses to use his money.

The widespread principle that people ought to be taxed only when they voluntarily convert property rights into marketable form may seem simply a matter of neutrality, a reluctance to force people to make nontax decisions for tax reasons. But this principle, in more refined form, may really be a political recognition of a basic human resistance to commoditization. This subtler form of the principle is far more useful than the “neutrality” form in explaining a number of related tax rules.

For example, a taxpayer pays no tax on the proceeds of a tort judgment for invasion of privacy, while a person who voluntarily markets his privacy rights will pay income tax on his receipts. Ar-
arguments that tort judgments "replace" or "restore" the untaxed benefits of privacy\textsuperscript{36} cannot alone explain this distinction. Even the taxpayer who voluntarily markets his privacy loses the previously untaxed benefit of privacy. The generally appealing neutrality argument—that we do not want to force people to sell their privacy just to pay tax—is also insufficient: When a taxpayer receives a tort payment, a third party has \textit{already} converted the privacy right into cash. Ultimately, it is the involuntariness of the conversion that bars taxability.\textsuperscript{37} The tax system must confirm a person's refusal to treat his privacy as a salable object.\textsuperscript{38}

Similarly, if the taxpayer receives books from a publisher, which obviously have a potential market value, the tax system will respect his desire to treat the books in a noncommodity relationship. If he sells the books or gives them away and takes a charitable deduction, he will be taxed, but as long as he holds them as noncommodities, he need not pay tax on their potential commodity value.\textsuperscript{39} This is not of the right to privacy. \textit{E.g.}, Meyer v. United States, 173 F. Supp. 920 (E.D. Tenn. 1959) ($2,500 received by taxpayer as "liquidated damages for possible future injuries" resulting from unfavorable portrayal in movie about to be made held taxable as ordinary income).

\textsuperscript{36} \textit{See} United States v. Kaiser, 363 U.S. 299, 311 (Frankfurter, J., concurring) ("[P]ayment which compensates for a loss of something which would not itself have been an item of gross income is not a taxable payment."). For a review of the cases in which this principle has been applied, \textit{see} \textit{id.} at 317–25. Earlier interpretations of the exclusion of receipts from tort judgments focused on the alleged absence of a "property right" in privacy or reputation and the requirement that income be "derived from capital, from labor, or from both combined." Eisner v. Macomber, 252 U.S. 189, 207 (1920). \textit{Eisner} was limited to its facts in Commissioner v. Glenshaw Glass Co., 348 U.S. 426, 430–31 (1955).

\textsuperscript{37} Where the taxpayer realizes income by the involuntary conversion of property, such as through insurance recovery for fire or flood damage, I.R.C. \textsection 1033 allows the taxpayer not to recognize gain so long as he reinvests the proceeds in property "similar or related in service or use to the property so converted." Again, the fear is not of forcing the taxpayer to sell property in order to pay taxes, because the property has already been reduced to money, but rather of taxing an involuntary marketing.

\textsuperscript{38} For the classic exposition of the view that treating labor as a commodity dehumanizes workers, see K. Marx, \textit{Economic and Philosophic Manuscripts}, in \textit{Early Writings} 280 (1963). For the classic critique of treating tangible goods as commodities, see K. Marx, \textit{Das Capital} ch. 1, \textsection 4 (O. Meisner ed. 1867). The abolition of the commodity form and money as an evaluating medium has also been a theme of non-Marxist utopian literature. \textit{E.g.}, Tobin, \textit{On Limiting the Domain of Inequality}, 13 J.L. & ECON. 263 (1970); Walzer, \textit{In Defense of Equality}, in \textit{The New Conservatives} 107 (L. Coser & I. Howe eds. 1974). Utopian communities have experienced some pressure to eliminate money altogether—to distribute all goods without regard to the distributee's earlier work commitments or his relative preference for goods. \textit{See}, \textit{e.g.}, H. Barkai, \textit{Growth Patterns of the Kibbutz Economy} 21 (1977) (describing "distribution technique controversy" between "traditional" demonetizers and "reform" market-oriented elements in Israeli kibbutzim).

\textsuperscript{39} Rev. Rul. 498, 1970-2 C.B. 6 (value of unsolicited books received by taxpayer must be included in gross income only if charitable deduction is taken; \textit{superseding} Rev. Rul. 330,
simply a result of realization requirements: Items that are inevitably treated as commodities, like marketable securities, are included in income upon receipt, not upon later sale. Nor can the result be explained as a result of valuation difficulties: If the tax system forced the book recipient to treat the books as a commodity, they could be readily valued by an appraiser or auctioneer. Only in their noncommodity form, as reading matter, do they seem incapable of valuation.

C. Private Preclusive Appropriation

Professor Andrews argues that the consumption component of the tax base should not include everything taxpayers spend their money on. There are ways of spending money which do not make claims on the distribution of "real goods and services." If the taxpayer does not exercise such claims, he ought not pay tax. Professor Andrews asserts that charitable donations exemplify nonappropriative spending; only the recipients of charity appropriate goods or services—when they spend the donated funds.

1. What is preclusive appropriation?

Diversion. Professor Andrews never precisely defines private preclusive appropriation, but I take him to believe that it is activity that diverts resources "away from the satisfaction of other people's needs." In donating, almsgivers may obtain utility, some feeling of pleasure or power equal to the utility other people get from ordinary consumptive spending. But Professor Andrews argues:

Taxable consumption in the end does not and cannot provide an accurate reflection of either power or pleasure. It is, rather, simply the accumulation or utilization of economic resources, measured at market value, for private consumption within the taxpayer's household. That definition is consistent with the practical purposes of the tax—to divert some economic resources to public uses in a manner that will reduce disparities in standards of living and saving.

Professor Andrews's apparent assertion that consumption is the diversion of real economic resources requires the assumption that one

1970-1 C.B. 14 (mere retention of unsolicited books makes them includible in gross income); see Haverly v. United States, 513 F.2d 224 (7th Cir.), cert. denied, 423 U.S. 912 (1975).
40. I.R.C. § 83(a) (property received in connection with services includible in income of person performing services).
42. Id. at 346.
43. Id. at 348; see note 18 supra and accompanying text.
44. Id. at 356 (emphasis in original).
45. Id.
cannot "consume" anything that lacks a production cost. In the almsgiving case, even if the donor receives such benefits as deference (clearly "supplied" by either donees, charitable conduit organizations, or his peers) or satisfaction at the donee’s improved fortune (an unintended externality of the donee’s consumption), Professor Andrews argues there has been no appropriation of time, energy, or natural resources.

But a notion of consumption tied to production cost is wholly inconsistent with uncontroversial tax decisions in other areas. Taxpayers’ activities are readily labeled consumption when the benefits received far exceed production costs, which may well be zero. For example, an airline executive may fly for free when seats are available, under a plan not available to all employees. The marginal cost of such flights is zero—no resources are used up when the executive enjoys his free flight. But such flights nevertheless are income to the executive—he clearly has greater economic power and personal satisfaction than those unentitled to such privileges. Whenever a taxpayer purchases a product produced by a monopolist, part of the purchase price reflects the monopolist’s profits, rather than long-term production cost, and yet taxpayers are not allowed to deduct the part of their purchase price attributable to the monopoly profit. Similarly, the price of any good or service purchased during a period of disequilibrium reflects transfer payments as well as production

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46. The deference may be "supplied" whether or not it has production costs. Examples of deference with clear production costs are: A donor gives a large amount of scholarship money to a law school; he is honored at a testimonial dinner given by other lawyers; he is recognized by the law school dean and staff; the scholarship recipients send him thank-you notes. On the other hand, the respect of donees, charitable managers, or other members of the donor’s community is a benefit a donor may expect to receive which is not physically costly.

47. Andrews, supra note 1, at 354–56.

48. "Employees do not have taxable compensation where the benefit... costs nothing additional to provide... and it is not limited to top executives." Office of the Assistant Secretary for Tax Policy, Summary and Explanation of Discussion Draft of Proposed Regulations on Fringe Benefits (Sept. 2, 1975) (emphasis added).

49. If appropriation involves any claims on activities with "costs," monopolists’ profits represent a transfer of surplus—from consumer surplus to monopoly surplus—rather than private preclusive appropriation. An assumption that consumers face monopoly pricing in proportion to their incomes (so that a deduction for monopoly profits would not alter taxpayers’ relative income positions) may well be empirically false. For example, victims of racial discrimination, unable to gain access to all housing markets, may well pay a monopoly-profit-based premium for their housing. See Kain & Quigley, Housing Market Discrimination, Homeownership, and Savings Behavior, 62 AM. ECON. REV. 263 (1972) ; Yinger, The Black-White Price Differential in Housing: Some Further Evidence, 54 LAND ECON. 187 (1978). But see R. MUTH, CITIES AND HOUSING: THE SPATIAL PATTERN OF URBAN RESIDENTIAL LAND USE (1969).
costs, but none of the price is deductible. A consistent application of Professor Andrews's apparent principle that the taxable base ought to include only the production costs of goods that the taxpayer preclusively appropriates would require allowing the taxpayer to deduct the component of price in excess of long-term production costs. Obviously, the tax system does not allow such deductions; it does not consider production costs at all in determining taxable consumption.

We can see the inadequacy of the production cost argument more clearly in an analogy to the charitable gift: the Veblenesque good, a special case of monopoly in which the good is valued precisely because it is scarce.50 Because the supply of deference from potential donees is limited, the price of deference will always exceed production cost and will be determined by demand.51 For example, a taxpayer bribes a beauty contest judge to name his daughter Miss Tulips Pageant. The vote itself has zero production cost, but both the briber and the judge have income.52 It would be hard to argue that the bribe should be excluded from the briber's taxable income, even though the briber claims no good or service requiring time, energy, or natural resources to produce.

Reciprocity. In trying to give some content to the concept of preclusive appropriation, it might be helpful to focus on what I would call "reciprocity" rather than on diversion of resources. (Professor Andrews himself never suggests this alternate focus.) Perhaps the most "nonreciprocal" donation, where the donor is anonymous to all people who might intentionally respond to him more favorably knowing that he has donated,53 is "nonappropriate" because the donor fails to receive anything but an unintended external benefit of the donee's activity. If private preclusive appropriation can be de-

50. The price of a Veblenesque good, like a unique painting, is not set by production cost but by the highest bidder's demand for it. See Kelman, The Social Cost of Inequality, in The New Conservatives 154 (L. Coser & I. Howe eds. 1974).

51. "For goods in totally inelastic supply, price is not fixed by supply cost, even in the long run; it is fixed by demand. Ordinarily, if five items costing $1 each are offered at Time 1 and there are five buyers willing to pay $10 (as well as a sixth willing to pay $9.99), the price will be $10, but production will increase immediately until demand=supply=cost . . . . If the supply is fixed at 5, though, the price will remain $10; it will remain as far above cost as the demand price for the number of available goods." Id.

52. I will ignore the question of whether the daughter has income as well. This problem relates to the question of whether both donor and donee have income when the donor transfers money to the donee. See note 18 supra.

53. For simplicity, I will ignore the question of whether the donor may be "purchasing" something from either the charitable conduit organization or peers. I will assume the donor is anonymous vis-à-vis donees, the charitable organization, and his community-at-large.
fined as the receipt of benefits by a party when and only when the benefactor intentionally betters thespender’s position in response to the spending, perhaps there is some ideal, if atypical, charitable dona-
tion that is nonappropriative.

Even though this reciprocity concept of appropriations seems stronger than the production cost/diversion argument, it is not without problems. How do we decide unarbitrarily that the donee’s consumption is the primary act and the donor’s pleasure at watching the consumption is external? Ordinarily, the person who does the initial spending is regarded as the primary actor, regardless of who makes the final appropriation of goods and services. For example, when a taxpayer gives a dinner party, the food is consumed by the guests. One could argue that unless the guests intended to thank the host in response to his spending, the host’s pleasure at watching his satisfied guests is a pure untaxed external benefit. But this result is hardly compelling: The tax system ordinarily considers the guests to be untaxed beneficiaries of the host’s decision to give a party.

Admittedly, in the dinner party case, the host has clearly appropriated goods with a production cost in the first instance. Perhaps we could then sharpen our sense of the scope of private preclusive appropriation by adding a step to account for both appropriation and reciprocity: If (1) the spender does not appropriate goods or services with a production cost, and (2) the spender does not receive benefits intended for him by a recipient of his spent receipts with whom he shares a reciprocal relationship, then there is no private preclusive appropriation.

Yet even this refined definition is flawed. In the earlier example, even if the judge intended to vote for the briber’s daughter all along, and thus never intended to confer a benefit in response to the briber’s spending, common sense tells us that the briber would have consumed. The key factor seems to be that the briber spent money in order to receive a benefit.54

Taxpayer’s intent. We could therefore add yet a third refinement in our attempt to discover content in private preclusive appropriation: There is appropriative consumption when the taxpayer intended, as he initially spent the money, to cause the recipient of the

54. A deduction for the briber here would be clearly inconsistent with the principle that taxpayers cannot deduct the amount of money wasted in an unsatisfactory purchase. See Treas. Reg. § 1.165-7 (1977) (casualty losses do not include wasteful consumption expenditures).
money to confer a benefit upon him, whether or not the recipient actually did so.

Unfortunately, the concept of appropriation—designed to reflect objective claims on supply—has now become an inquiry into the purely subjective attitude of the spender. And it is hard to imagine what sort of subjective claim by the briber, for example, would remove all imputation of intent to receive some benefit from others, at least in the longrun.55

Application to the strongest case—almsgiving. Examining even the case where the donor gives anonymous unrestricted grants, where he receives only the reassuring knowledge that he has helped a poor person,56 gives us no guidance in defining private preclusive appropriation. The argument that such a donor has "appropriated" nothing would be:

(1) Even though the donor must spend money to feel he has helped the donee, the donee does not spend time, energy, or natural resources being helped.

(2) The donee does not deliberately confer on the donor the sense he has been helped as a quid pro quo for the donation; the donor’s sense of having helped is external to the primary act of consumption—the donee's spending of the money.

(3) The donor does not give the money with the intent of causing the donee to confer on him the sense of having been helped.

Arguments (1) and (2) are irrelevant. In many transactions routinely classified as consumption, the benefactor neither expends productive resources nor intentionally benefits the spender in response to

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55. Presumably, the briber would argue: "(1) Votes in beauty contests have no production cost, and (2) the judge did not confer a benefit on me as a result of my spending, and (3) I never thought he would. I simply wanted the utterly private, nonreciprocal satisfaction of thinking I had done all that I could for my daughter." After the fact, such an argument seems strained. The supposedly private idea that one has "done all one could" depends on the socially created possibility that one could influence votes—that is, on the general social practice of reciprocity. The only alternative subjective standard, however, would consider whether the spender's intent to receive should be equated with some level of probability of receipt.

56. The anonymous gift is, of course, exceptional. In calendar year 1978, Stanford Law School received roughly 1,400 gifts. None of the gifts was fully anonymous: In each case, the fund-raising staff at the Law School knew the identity of the donor. In only three cases (gifts totalling well under 1% of the total), the donor requested anonymity vis-à-vis the outside world; in a fourth case (accounting for roughly 30% of total gift income), the extent of publicity for the donor will be limited.
the transfer of funds.\textsuperscript{57} Argument (3) is inadequate to define nonappropriative situations: As we have seen, it requires speculation about the spender's private motivation, while the purpose of a concept of appropriation is to provide some objective measure of taxability. Moreover, argument (3) ignores the fact that in a broader context the "utility" a charitable donor gets from his donation derives from a \textit{general} cultural approval of charitable giving. Even if the donor is indifferent whether any particular donee (or charitable conduit or even social peer) responds to his gifts, his private feeling of satisfaction depends on some general reciprocal relationship between his inner self and his society's traditional recognition of the worthiness of giving.

2. \textit{Is charitable giving nonpreclusive?}

Even if we could assign clear content to private preclusive appropriation, it would remain hard to prove that charitable giving was not itself within the definition. The almsgiver may give money in the form of either tied or unrestricted grants. The tied grant, the commonest form,\textsuperscript{58} is clearly appropriative under any defensible meaning of the term. And it would be hard to characterize even unrestricted charitable grants as "nonappropriative," given the great likelihood that donees expend \textit{some} resources to demonstrate their gratitude.

\textit{Tied grants.} A donor, $D$, gives scholarship money to a law school. The student-donees must spend the money on legal education. $D$ is thereby appropriating educational services, using his money to redirect people's time and energy into the provision of legal education. Watching education be consumed is no less an act of consumption than any other form of voyeurism.\textsuperscript{59}

Professor Andrews argues that we can exclude this redirection of resources from the tax base because the government chooses not to tax redirection of resources in a number of other situations, such as

\textsuperscript{57} See notes 53–55 supra and accompanying text.

\textsuperscript{58} It is difficult to generalize about the conditions that donors acting through charitable conduits put on the receipt of grants, since almsgiving charities are inevitably decentralized. Most organizations that are eligible for exempt contributions do not simply disperse funds to the poor, but fund particular restricted projects. For lists of restricted purpose activities funded by eligible organizations, see \textit{THE FOUNDATION CENTER, THE FOUNDATION DIRECTORY} (5th ed. 1975). Public welfare programs which give flat grants frequently put conditions on the receipt of money. \textit{See} W. Bell, \textit{AID TO DEPENDENT CHILDREN} (1965); K. Gronbjerg, \textit{MASS SOCIETY AND THE EXTENSION OF WELFARE} 1960–70 (1977).

\textsuperscript{59} Since hiring a prostitute is clearly an act of consumption, hiring a hooker and/or a john and watching them must be also.
when the taxpayer exerts political power. But the point may simply be that the government only taxes redirection of resources that operates through the market medium of spending, rather than other modes of influence. When dealing with the sources of well-being, Professor Andrews is not dismayed that market and nonmarket phenomena are treated differently, that the tax base includes marketable receipts while excluding consumer surplus and various types of utility that give taxpayers as much satisfaction as income. It is thus peculiar for him to suggest that market and nonmarket redirections of resources be treated the same.

Unrestricted grants. Even when the donor assumes no control over the donee’s spending, I would argue that his donations are likely to be appropriative.

Though I find it difficult to identify any nonappropriative spending, Professor Andrews and I would agree on this: If the donees, the charitable conduit, or other members of the donor’s community expend any time or energy ensuring that the donor enjoys his donation, at least some of the donation ought to be included in the tax base. But can we reasonably restrict the amount of taxable income to the cost of the time and energy expended, or is the proper measure of the “appropriative spending” the entire donation? The difficult issue is joint causation. If a donor is motivated both by a desire to receive reciprocal benefits with clear production costs and by a desire (assumed for the moment to be “nonappropriative”) to feel better because of the donee’s improved fortune, the government must either attribute a single transaction (the observed transfer of funds) to one cause or the other, or allocate.

Donors often receive concrete, costly symbols of gratitude and deference in return for their donations. Even if his grant is unrestricted, D, who donates the law school scholarship money, may

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61. See W. Andrews, Federal Income Taxation: Cases Problems and Notes 2 (Supp. 1978) (unpublished manuscript on file with Stanford Law Review) (“Suppose, on the other hand, it could be shown that [the taxpayer] Benaglia had a passion for hotels and that living in a hotel was worth much more to him than the price of a room. (Suppose, for example, that he had turned down other higher-paying jobs in order to live in the hotel.) Would it then be justified to tax Benaglia on more than the established room rent? Economists use the term ‘consumer surplus’ for the excess of satisfactions derived from a product over its market price. Are there convincing reasons for categorically excluding consumer surplus from taxable income?”).
62. For a detailed discussion of joint causation problems in the medical deduction case, see notes 129–40 infra and accompanying text.
receive the privilege of friendly discussion with the dean and faculty, who certainly do not chat with everyone. While in any particular case the donor may not have "spent" as much as he "donated" to purchase directly all the symbols of gratitude were that the explicit market price for such purchases,63 the size of the donation may equal the price the donor would in fact pay for the concrete benefit received.

With this assumption, it becomes difficult to argue that any of the donation ought to be excluded from the consumption base, because the taxpayer received benefits having some production costs whose value equaled the price he paid for them. There is, as we have seen, no principle that taxpayers can deduct the excess of price or value over cost. Even if we bother to make subjective inquiries that reveal that the donor would not have "spent" as much as he donated to purchase the concrete benefits he receives, allowance of any charitable deduction requires adopting the dubious proposition that if a taxpayer pays more for concrete benefits than their cost or value, he ought to be allowed to deduct the excess.

It might be argued that purchased deference and gratitude do not represent a major portion of all the deference in society. But this view does not justify excluding purchased deference from the tax base any more than excluding the rewards of redirecting resources through political power dictates excluding redirection through market spending.64 Perhaps it follows from Professor Andrews's assertion that the tax base should focus on uses that if a taxpayer uses his money to obtain a pleasure that is untaxed most of the time, the taxpayer should not be taxed on the money so spent. But this view seems inconsistent with other principles of the tax system. For example, most sexual pleasure in the world is not purchased, but the small portion that is can hardly be excluded from the consumption base.

3. Who cares about appropriation?

Even if private preclusive appropriation were a useful concept and charitable giving were nonappropriative, Professor Andrews would still have to prove that nonappropriative spending should be excluded from the tax base. As he concedes, if the tax base at-

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63. If there were a separate market for conversations with the dean, the price donors would pay to purchase those conversations might be lower than the amount that people have to donate to obtain the privilege of free access to the dean. But there is no such separate market. Since the benefits acquired through donation—such as time with the dean and the satisfaction of being a community pillar—are inseparable, it is not possible to ascertain the price of the dean's time.

64. See note 60 supra and accompanying text.
tempted to measure how well-off the taxpayer was as a result of his command over money, the government would treat the charitable donor just as it would any other spender. But Professor Andrews shifts our attention from a “demand” perspective on consumption to a “supply” perspective, for reasons that become less and less clear the more one scrutinizes them.

Professor Andrews advances three basic arguments:

(1) “The primary intended effect of a direct, personal tax must be to divert economic resources away from personal consumption and accumulation. Some part of the national output which would otherwise be consumed or accumulated by private individuals is to be devoted to public purposes.”

(2) “If the primary intended effect of the tax is to cause a reduction of private consumption and accumulation of real goods and services, then it makes sense to distribute the reduction in some kind of uniform (though graduated) relationship to the amount of consumption and accumulation people would otherwise enjoy.”

(3) “This is all equally true, perhaps ever more clearly so, if we think part of the purpose of a graduated tax is relative redistribution. What we mean to redistribute, ultimately, must be shares of real goods and services which persons otherwise would be consuming or accumulating; the disparities we mean to mitigate are disparities in aggregative distributive shares of real goods and services.”

Professor Andrews then rejects with a rhetorical question the alternative tax base—that I previously suggested:

(4) “There is a more familiar way of stating the purpose of the income tax that may seem to point in a somewhat different direction: taxes are to be levied according to ability to pay, and such ability is shown by the receipt of income whether or not it is devoted to personal consumption and accumulation. . . . Another way [to measure ability to pay] is in terms of power or wealth, because to the extent a man has

66. Id. at 325–26.
power in excess of his personal consumption and accumulation he can pay the tax without curtailing them. . . . Unexercised earning power is a source of ability to pay, but it would be very difficult to measure. Moreover, it is not clear we would want an income tax that would compel people to take higher paying jobs than they would otherwise choose in order to raise the funds to pay the tax. But if we do not tax a man on what he declines to earn, then why should we tax him on what he does earn but does not devote to his own personal consumption or accumulation?67

Professor Andrews’s reasoning strikes me as uncompelling at every turn.

**Intended effect of the tax.** Professor Andrews’s first argument says little. It is true that the government taxes in order to have funds available to use for public purposes. This is the aim of any tax and says nothing about the appropriate tax base or distribution of tax burdens. If GNP is fixed, public spending invariably replaces private spending, regardless of the type or incidence of the tax.

**Distribution of reduction in spending.** In the first part of argument (2), Professor Andrews misstates his first argument in the guise of restatement, claiming now that the primary effect of the tax is to reduce private consumption rather than to provide funds for public purposes. The argument is not sensible. Assume that there are two goods in the world: cake and pie. If the government intends to supply or purchase only cake, Professor Andrews’s argument implies that the primary effect of a tax intended to raise the necessary revenue would be to reduce the consumption of cake, even if the state could fund purchases by taxing those with pie. The fact that the government appropriates goods with positive production costs in no way implies either that they cannot fund such purchases by taxing those who purchase goods without such production costs, or that the “primary effect” of the tax is to reduce private appropriation of goods with positive production costs.

The next step in argument (2) is even harder to fathom. Professor Andrews argues that the tax burden must be distributed among taxpayers in proportion to their enjoyment of the good that is inevitably taken away from them, that is, in proportion to their appropriate

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67. *Id.* at 327 (emphasis added).
consumption. Aggregate consumption tautologically equals private plus public consumption; therefore, if public consumption rises, private consumption must fall. Thus, says Professor Andrews, the only appropriate way of increasing public consumption is to have private consumers share proportionally the inevitable drops in their private consumption.

This argument is a non sequitur, as a simple example will show: Assume there are four people sharing a single pie, and a fifth with no pie. Aggregate consumption equals the consumption of the four (plus zero consumption attributable to the fifth). If the consumption of the fifth rises, the consumption of the other four must fall: therefore, the other four must give up pie in proportion to their previous consumption of pie. This is hardly a logical necessity: All Number Five's pie could be taken from one of the first four. This could be someone in a special relationship to Five, such as a parent, or all the pie could be taken from the one who liked pie least, or all the pie could be taken from the person who could acquire more pie with the least effort, such as a baker or a very wealthy person. It simply does not follow that changes in burdens must be proportional to their initial distribution. Having picked out some "target" level of public spending, which requires a certain amount of tax revenue to be raised, tax authorities should allocate burdens among taxpayers by measuring taxpaying ability in as coherently equitable a fashion as possible.68

Professor Andrews's argument about the appropriate distribution of tax burdens might be justified under an alternative interpretation. If the public sector69 were assumed to have claims over all income, it might evaluate the uses of income as follows: Private necessity spending is "better" than public spending, which in turn is "better" than private luxury spending and saving. Increasing "good spending" requires that the public sector use taxation to shift money that would ordinarily be used for luxury spending and saving to the public sector, but that funds already in the hands of private necessity spenders remain there.70

Although this argument is more persuasive than that actually

69. This situation and analysis assume that the public sector is a monolithic actor.
70. A real model of this process would note that at a certain level of government and luxury spending, the marginal dollar spent on public goods would be viewed as "better spent" than the same dollar devoted to luxury use and at lower levels, and more resources would be appropriately shifted to the public sector. The nonmarginalist simplified model here is simply a heuristic metaphor.
provided by Professor Andrews, it too is problematic. The appropriate tax to achieve such results would combine differentiated sales and savings taxes rather than a direct personal income tax. Moreover, the idea that revenue needs ought to grow as people get richer, because public programs would take precedence over increasingly discretionary luxury spending, is not obvious.71

Most important, the argument is difficult to distinguish from the tax expenditure arguments which Professor Andrews and I both explicitly reject.72 In essence, the argument assumes that the taxpayer with high net receipts should be taxed rather than be allowed to squander her money on luxury goods, but that if she makes high merit nonluxury purchases (purchases the government would like her to make), there is no reason to tax her because the public sector feels the same effect it would from taxing and spending. This raises the most troublesome tax expenditure question: whether the public sector ought to scrutinize each donation to ensure that the money is better spent than the marginal public dollar forgone would be.73

Inevitable redistribution of goods and services. Professor Andrews’s argument (3) is that the tax system must intend to redistribute shares of real goods and services. This assertion is not obvious, but he makes no further attempt to justify it. Other significant disparities, such as earning capacity, might be equally suitable targets of redistribution.

Dismissal of ability-to-pay-oriented tax system. Professor Andrews does not support his dismissal of an ability-to-pay-oriented tax system. Although he correctly asserts that an earnings capacity tax is both nonadministrable and unwise in principle, a refined net receipts tax is not such a tax, since it taxes only voluntarily exercised capacity. Professor Andrews questions those who would tax the person who earns money but does not use it for his own consumption when he does not pay tax on what he declines to earn. However, his previous sentence

71. For instance, there is no reason to believe that demand for a collective good, such as defense spending, is income-elastic. If the government set revenue needs according to demand for income-inelastic collective goods, it would increasingly prefer luxury spending to public spending as income rises.
72. See notes 3-8 supra and accompanying text.
73. “[M]any of the organizations and activities would not be supported by taxation ....... This is the basis of a strong criticism of the deduction. The taxpayer, by making a deductible contribution, forces the government, in effect, to make a partially matching grant for a purpose of his own choosing and to an organization whose operations are not subject to governmental review or control. Sectarian, provincial, eccentric, or frivolous uses of money may be aided along with the most worthy.” R. Goode, supra note 68, at 162.
contains one reasonable response to his perplexity: The tax system
does not want to compel people to take the highest paying job they
could get in order to raise funds to pay taxes on their earning capac-
ity. Taxing those who use their already-earned money “nonpreclus-
ively” certainly does not compel them to do this.

D. A Very Brief Note on the Suppression of Contradiction

While I think that even Professor Andrews’s paradigm case for
deductibility—the anonymous almsgiver who gives out money abso-
lutely without restriction—is itself weak, Professor Andrews would
have even greater problems with charitable donations by known par-
ties, purchasing known services, where the donors receive direct ben-
efits (like deference). Yet nearly all charitable donations are of this
latter sort: The almsgiving paradigm, while it may seem like a rea-
sable device for clarifying the issues, may largely serve to suppress
important difficulties in Professor Andrews’s reasoning.

The real world of charitable deductions has several significant
characteristics: First, the charitable deduction is a serious tax issue
only to the rich. In 1968, those with incomes over $1 million a year
gave gifts averaging 25.9 percent of income.74 Those with income
from $500,000 to $1,000,000 gave 18.8 percent of their income in
gifts; and those with incomes from $100,000 to $500,000 gave 10 per-
cent of their income in gifts.75 No discernible subgroup of the class of
taxpayers with annual incomes between $10,000 and $50,000 gave
more than 3.3 percent of their income in gifts.76 Second, the charac-
ter of gifts from high-income givers is inevitably reciprocal in a way
not necessarily true for the low-income donor. The average annual
contribution of those earning over $1 million a year is $287,651, com-
pared with between $90 and $478 for those with incomes below
$50,000.77 Gifts of that size presumably draw some individual atten-
tion from recipients, charitable conduits, or the donor’s community.

The fact that there is troublesome reciprocity throughout the
charitable area is even clearer when one notes that the bulk of giving
done by low-income donors is to churches. Political expediency
alone dictates that the government not reduce a parishioner’s deduct-
ible contribution by the apportionable cost of the church services the

74. See Feldstein, supra note 4, at 87.
75. Id.
76. Id.
77. Id.
parishioner receives.\textsuperscript{78} Admittedly, there is no noncharitable market for church services, but it remains true that the churchgoer receives a service that costs something to provide.\textsuperscript{79}

In 1962, 61 percent of all charitable donations went to churches. Those who do not make "significant donations" give almost entirely to churches: Those earning less than $15,000 a year give average donations to hospitals and educational institutions of $6 or less.\textsuperscript{80} While only 1.1 percent of religious contributions came from those

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78. Professor Andrews simply asserts that the value of church services ought not to be taxed: "There is no satisfactory way of measuring the benefit conferred on any particular [church] member. Even if we took the church budget as setting a prima facie value or price on the total of benefits produced for its members, there is no adequate method of determining distribution of those benefits among church members for individual income tax purposes. And even if we could put values on such things, I doubt if we would want to include them in taxable income. Whatever considerations lead most churches not to charge admission may make it undesirable as well as impractical for the state to define taxable consumption in such a way as to impose a secondary admission charge in the form of a tax burden." Andrews, supra note 1, at 358-59.

I would argue that the charitable deduction ought to be disallowed because there is no principle which logically distinguishes charitable spending from other forms of spending. Even if "pure" charitable spending should be deductible, the appropriate size of a charitable deduction could never be ascertained once the donor appropriates some goods or services, since we do not generally assume that spenders get deductions for purchases where price is above cost. If we want to include only the "cost" of services in the consumption tax base, we certainly should include at least that cost rather than assume the expenditure is sufficiently explained by the charitable roots and thereby justify deduction of the whole expense.

79. Where the taxpayer transfers money to a qualifying charitable organization which directly provides him with services, the § 170 deduction must be reduced by the market value of the services. Thus, if $X$ gives $100 to the symphony, and is entitled to attend a concert which would otherwise cost $20 to attend, the charitable donation deduction will be reduced to $80. \textit{See} DeJong v. Commissioner, 309 F.2d 373 (9th Cir. 1962) (deduction of "contribution" by parents to private schools their children attended allowed only to extent such "contributions" exceeded market value of tuition). There is some question whether one can characterize a transfer of funds as a qualifying donation wherever substantial benefits are received as a quid pro quo for the transfer. Thus, it is possible that denial of the deduction, rather than apportionment, is appropriate if the taxpayer receives concrete benefits. \textit{See}, \textit{e.g.}, Singer Co. v. United States. 449 F.2d 413 (Ct. Cl. 1971) (no deduction when benefits received by purported donor are substantial enough to provide quid pro quo for transfer). Essentially, the argument the courts use for disallowing deductions under § 170, when the donor has received reciprocal benefits, is that one must transfer funds with the same "disinterested generosity" required of donors in the ordinary gift context to ensure exclusion of the "gift" from the donee's income under § 102. \textit{See} Commissioner v. Duberstein, 363 U.S. 278 (1960). The courts may then regard the existence of substantial benefits as evidence of the lack of requisite disinterestedness. \textit{See}, \textit{e.g.}, Allen v. United States, 541 F.2d 786 (9th Cir. 1976); Stubbs v. United States, 428 F.2d 885 (9th Cir. 1970). This "subjective test" of disinterested giving has been criticized by some courts, \textit{e.g.}, Oppewal v. Commissioner, 468 F.2d 1000 (1st Cir. 1972), particularly when the donor is corporate and the concept of disinterested generosity is more inscrutable, \textit{see}, \textit{e.g.}, United States v. Transamerica Corp., 392 F.2d 522 (9th Cir. 1968).

earning more than $50,000 a year, 33.1 percent of donations to educational institutions came from those taxpayers.81

The charitable world, then, seems to be made up largely of two types of gifts. First, there are small gifts by lower income donors to churches. These may be relatively insignificant for tax policy purposes, but they certainly involve a rather direct quid pro quo. Second, there are large gifts by the rich to educational institutions and hospitals, which divert resources to institutions that the rich choose, which often (particularly in the case of educational donations) benefit the class the rich want to be benefiting, and which involve a great deal of reciprocity, at least in the form of attention and deference. This second class of donations seriously undermines vertical tax equity because large amounts (and percentages) of income are at stake. Thus, real world complexity undercuts even further an already questionable defense of the charitable deduction.

III. THE MEDICAL CARE DEDUCTION

Section 213 of the Internal Revenue Code allows itemizing taxpayers to deduct medical care and medical insurance payments which exceed certain percentage limits of their adjusted gross income.82 The exact mechanics of the section do not matter here.83 I will simply assume that if taxpayer A's net receipts total $50,000 and B's $60,000, but B incurs medical bills of $10,000, B's medical care deduction ensures that A and B pay the same tax.

81. Id.
82. Taxpayers may deduct uncompensated medical care expenditures which exceed 3% of adjusted gross income. I.R.C. § 213(a)(1). Purchases of drugs over 1% of adjusted gross income are included in medical care expenditures. I.R.C. § 213(b). Taxpayers may deduct one-half of their health insurance premiums up to $150. I.R.C. § 213(a)(2). Percentage limits are intended to enhance administrative convenience. If most taxpayers deducted a very small portion of their income for "unextraordinary" medical care spending, the deduction would increase the taxpayer's paperwork without giving any real benefit to taxpayers, since the government could just adjust rates upward to collect the same amount of revenue.
A. Professor Andrews's Arguments for the Medical Deduction: A Presentation and a Capsule Critique

1. Refining the definition of "consumption."

Professor Andrews approves the charitable deduction because the charitable donor does not appropriate scarce economic resources. He concedes that the medical care purchaser does preclusively appropriate resources\(^84\) and gains as much "utility" from the use of the marginal dollar spent on medical care as she would from other purchases. But Professor Andrews nevertheless offers several reasons why medical expenses are not true "consumption": (1) The appropriate consumption base, on which all taxpayers should be taxed, includes the satisfaction derived from good health as well as the satisfaction derived from traditional consumption.\(^85\) (2) A taxpayer obtains no positive increment of well-being when she spends money on medical care, but simply restores the state of good health she enjoyed before her illness or injury.\(^86\) A third argument which Professor Andrews never explicitly makes but which his reasoning leads one to make is: (3) The proper consumption tax base is "total discretionary consumption," consumption spending net of spending on "needs."\(^987\)

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84. Andrews, supra note 1, at 335.
85. "The right basis for making interpersonal welfare comparisons on which to base the distribution of tax burdens is that ultimate object, good health . . . ." Id. at 335–36.
86. See id. at 334 ("the provision of medical services . . . only serves as a remedy for the injury."). Advocates of the medical care deduction use the restoration metaphor to draw on the intuitive appeal of the exclusion of tort judgments from the tax base. As I argued earlier, however, see note 34 supra and accompanying text, a restoration argument does not explain the distinction courts draw between standard § 104(a)(2) exclusion cases where the damages are received after the injury, and inclusion cases where the taxpayer contracted away the rights before the injury. See, e.g., Meyer v. United States, 173 F. Supp. 920 (E.D. Tenn. 1959). This distinction is better understood as a way of protecting a taxpayer's decision not to enter the market. Thus, the restoration metaphor is of limited use even if it were applicable to most medical care expenditures.
87. Professor Chirelstein makes an argument precisely parallel to this third argument. He finds no logical explanation for the exclusion of nonphysical damage judgment awards but he supports the medical care deduction. M. CHIRELSTEIN, FEDERAL INCOME TAXATION 40, 139 (1977). He argues that medical care expenditures are involuntary and unexpected, much like casualty losses deductible under I.R.C. § 165. Id. at 139. This involuntary expenditure puts the taxpayer in the same position as someone who never received money at all, whereas the recipient of a tort judgment for nonphysical injury receives money, losing only psychic benefits generally excluded from taxation. The characterization of medical expenditures as "involuntary spending" by Professors Andrews and Chirelstein is inappropriate. See notes 101–14 infra and accompanying text.

Moreover, the notion that the "casualty loss" deduction is itself justified—even if one could look at medical expenditures as resembling a casualty loss—is not nearly so clear as Professor Chirelstein implies. In the ideal-typical case—where, say, the taxpayer has his paycheck stolen—one can argue either: (1) From my net receipts tax perspective, that the
Good health as a component of the consumption tax base. Professor Andrews asserts that the consumption tax base ought to include the satisfaction derived from good health. But he gives no persuasive reason for the tax base to account for such psychic income derived from good health while ignoring all other psychic income. If taxing authorities wanted to account for the positive worth of health, the government could allow each taxpayer to add to his nominal income a sum of money representing the value of his health, or, on the other hand, allow him a deduction for the onset of disease. Professor Andrews approves a third method—that of section 213: Taxpayers deduct medical care expenditures from their taxable income.

taxpayer has never effectively received or appropriated income; that earnings capacity over a lifetime includes the risk of being unable to appropriate one's earnings and that it is administratively feasible to measure differential risks among taxpayers only when losses actually occur; (2) From Professor Andrews's perspective, that the tax base equals consumption plus savings; that losing a check is not an appropriative act, and therefore not an act of consumption. But the deductions for losses of previously appropriated property are more bothersome; they come more and more to resemble other disappointments with purchased commodities: The person saddled with a "lemon" may well "lose" more vis-à-vis expected return on a consumption expenditure than someone whose product is destroyed by fire, but "excessive" bills from mechanics are clearly not deductible. Whether the array of disappointments with past-purchased items ought to be taken account of at all seems quite open to debate: Once again, I suspect that the sort of one-shot, "incident" casualties which give rise to § 165 deductibility are more likely to be evenly distributed across classes than are "bad buys," which the poor are perhaps more likely to make.

88. Andrews, supra note 1, at 335–36.

89. Such a system might be modeled on a Workmen's Compensation scheme. Generally, of course, compensation in Workmen's Compensation settings is based solely on lost pay. See M. FRANKLIN, INJURIES AND REMEDIES: CASES AND MATERIALS ON TORT LAW AND ALTERNATIVES 531–33 (1st ed. 1971). But in dealing with job-related injuries that cannot be fully compensated simply by providing the worker with some portion of lost pay, administrative agencies have drawn up schedules with varying degrees of flexibility which peg compensation to particular injuries. Id. at 534–36.

Whether a workable medical care deduction scheme that would abstract from taxpayers' spending is administratively workable is a difficult question. One of my aims in this section of the article is to convince people that it might be worth trying to construct an administrable system that abstracts from expenditures.

90. Andrews, supra note 1, at 336. Thus, assume $A$ and $B$ each has $50,000 to spend on traditional consumption items. If $A$ is in perfect health, we could add, say $10,000, to his nominal income while $B$, with say, a broken leg, would only have $7,000 added, the presumed value of being in generally good health except for the broken leg. Alternatively, $A$'s income would remain at $50,000 and $B$ would receive a $3,000 deduction for the onset of a broken leg. The assumption, in each case, is that it is worth $3,000 to be free from a broken leg. Finally, under § 213, $B$ would receive a deduction equal to what he spends to treat the broken leg. The second and third tax treatments are identical only if every taxpayer who has the relevant disease (broken leg) spends the same amount ($3,000) to treat the ailment.

If the medical care deduction is not to undermine the progressivity of the tax system, it must be restricted to spending which is either unaffected by the class position of the spender or engaged in by all members of each relevant income class. If the deduction is not to under-
Professor Andrews's approval of section 213 rests on three unwar-

time horizontal equity (more than it necessarily does by assuming medical spending is "dif-
ferent" from other spending), it must be restricted to spending that is (1) always required for
the treatment of a particular ailment or, (2) for which all taxpayers would always seek
treatment.

Only one scheme is consistent with these vertical and horizontal equity aims: a Work-
men's Compensation-like system which allows uniform deductions for the onset of particular
symptoms while ignoring the actual spending on the alleviation of the symptoms. Such a
system recognizes that the loss of good health destroys as much "real" income for one tax-
payer as another, regardless of class—assuming income includes the psychic income of good
health while still excluding psychic income in general. Section 213, however, cannot be read
in so restrictive a manner. The IRS and the courts recognize such limits on the deduction
only in "extreme" cases. They generally allow deductions for highly elective medical care
"needs" and all spending that purportedly arises from those needs. This expansive rule is
then limited by ad hoc equitable exceptions: Where the idiosyncrasy of a medical expenditure
presses the line on elasticity "too far," or where the expenditures "arising from" the disease
include "too many" traditional nonmedical elements (made nondeductible expressly by
§ 262), deductibility will be denied. As for the source of these limits, first, the Service has long
held that the deductible expenditure must arise from a "defect," "disease," or "medical con-
dition." See I.R.C. § 213(e)(1)(a); Treas. Reg. § 1.213-1(e) (1974). Expenditures which bene-
fit the taxpayer's health in some more general way, which do not arise from a discrete
condition, are clearly nondeductible. Treas. Reg. § 1.213-1(e)(1) (1974). Here the question is
whether the "maladies" underlying the more elastic forms of medical spending constitute
such "medical conditions" or "defects."

Second, the Service holds that the expenditure must serve as "treatment" for the "de-
fect." See Treas. Reg. § 1.213-1(e)(1)(ii) (1974). The question is whether the traditional per-
sonal consumption aspects of a treatment process, which may help relieve, on the whole, the
adverse condition, may be deducted.

The dilemmas of defining defects in a manner consistent with Professor Andrews's view
that there is a baseline of good health included in the consumption tax base are insoluble
under the current statutory scheme. In effect, the Service has ended up accepting the exist-
ence of a "defect" whenever the taxpayer receives "treatment" provided by health care
professionals or the health care professional certifies the existence of a defect when either a
nonprofessional treat, or the professional provides treatment that could reasonably be pro-
vided by a non-health care professional. This definition of defect bears no significant relation

to the one that Professor Andrews implicitly relies upon: a condition that inevitably "wors-
en" a baseline tax-free condition of "good health" and which inexorably calls forth
treatment.

The problem of highly elective surgery illustrates the difficulty. Though there is theore-
tically a 2-part test for deductibility—the taxpayer must have a disease and his spending must
go to treatment for the disease—the first part simply disappears here. The Service, in effect,
"presumes" that operations ("treatments" performed exclusively by medical professionals) indi-
cate health defects. See Rev. Rul. 332, 1976-2 C.B. 81. Only if the medical professional per-
forms a service that a nonmedical person could perform will the courts or the Service look
further in determining the presence of a disease. See, e.g., Wendell v. Commissioner, 12 T.C.
161 (1949) (salary of practical nurse for routine child care nondeductible "absent special cir-
cumstances of illness, accident, or physical or mental defects"). Compare Rev. Rul. 187, 1975-
1 C.B. 92 (fee for psychiatrist treating sexual maladjustment deductible), with Rev. Rul. 319,
1975-2 C.B. 88 (no deduction for marriage counseling cost).

Professor Andrews is indeed bothered by deductions for such things as cosmetic surgery.
Andrews, supra note 1, at 337. But if the Service proceeds to inquire into the elasticity and
variability of decisions to elect surgery and limits deductions to unavoidable operations, it
ranted assumptions (or at least on the belief that the real world departures from these assumptions are small). First, all purchases of "medical care" result from a departure from some baseline state of good health. Thus, if B goes to a psychiatrist and spends $10,000 to cure "neurosis," section 213 presumes the absence of neurosis as part of the baseline of good health. Second, every departure from the baseline of good health results in an expenditure on medical care. Third, the precise expenditure made in response to a departure from good health is determined wholly by the nature of the departure and not at all by general consumption desires irrelevant to medical care.

*Restoration of good health.* To understand Professor Andrews’s argument that the restoration of good health is not taxable consumption,91 assume a taxpayer, B, in perfect health, who earns $50,000 every year, which she spends on traditional consumption. At the end of year 1 she is taxed on the entire $50,000. In year 2 she is injured by a tortfeasor.92 Consider the following three possible financial events:

1. The tortfeasor pays B $10,000 to pay her medical bills. For that $10,000, B's doctor can restore her to the state of perfect health she enjoyed before the injury.
2. The tortfeasor is a doctor himself, who provides B with $10,000 worth of his services at no cost to her, and thereby restores her to her perfect health.
3. The tortfeasor is judgment proof, but B is able to earn $10,000 additional income with which to pay her medical bills.

Professor Andrews argues that in all three cases B is in precisely

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91 See note 86 supra and accompanying text.
92 The analysis will be the same where B suffers an illness rather than an injurious tort. See Andrews, supra note 1, at 334.
the same consumption position in year 2 as she was in year 1,93 that is, she has $50,000 to spend on traditional consumption and she is healthy. Since the appropriate base to measure taxable capacity is this "consumption position," not nominal income, taxing her on the additional $10,000 she receives in year 2 (in money or in kind) would be wrong, regardless of the source of the receipt.94

A similar fact pattern demonstrates the vulnerability of Professor Andrews's restoration argument. In year 1, Z earns $50,000 working regular hours in a comfortable office at an enjoyable job. In year 2 he changes jobs; he now must work erratic, long hours in an ugly office on meaningless projects. But he now earns $60,000 a year. The extra $10,000 may simply "purchase" or "restore" the untaxed psychic benefits of his first job. If all one had was a view that any time a taxpayer is "restored" to a position he would view as equivalent to that he left, deduction of the raise would be appropriate. But Professor Andrews does not suggest exempting the $10,000 raise, either because he believes there is something unique about the psychic benefits of good health95 or because he believes the tax system can measure the value of lost health while it cannot measure other psychic changes.96

The restoration argument poses another problem less clearly suggested by the consumption-base argument—the unreasonable time restriction. Assume once more that B earns $50,000 in year 1 and $60,000 in year 2, when she develops an illness that costs $10,000 to cure. But in year 1 B may have lived a risk-free life, while in year 2 she may have enjoyed such risks as skiing or smoking which gave her substantial untaxed psychic income even though they impaired her health. Should the tax system exclude the $10,000 because it restores untaxed good health, or include the $10,000 medical bill as representing the psychic benefits of risky living that the tax system has not yet otherwise recognized?

"Discretionary consumption". Professor Andrews observes that medical expenditures vary among taxpayers of similar wealth almost exclusively as a result of differing medical "needs" and not as a result of personal taste.97 The "need" argument suggests that the best measure of a taxpayer's ability to pay is discretionary income, the

93. Id.
94. Id.
95. See id. at 335.
96. See id. at 336.
97. Id. at 314.
income he is free to spend after he has taken care of his "needs"\textsuperscript{98} (rather than the sum of "properly defined consumption" and savings). Is a person who receives more income and has more "needs" to absorb that income better able to pay taxes than one with both little income and few needs?

Though Professor Andrews specifically asserts that he does not wish to try to define "ability to pay,"\textsuperscript{99} a focus on "discretionary income," inevitably grounded in precisely such an attempt, better explains the section 213 scheme than do the first two arguments. If the consumption base or the "restored" untaxed benefit is supposed to be good health, it is not at all clear why the tax system does not allow a deduction for the onset of disease regardless of whether treatment is purchased, or explicitly recognize that a taxpayer's taxable income ought to be \textit{less} than income net of health care spending if treatment does not restore him to the state of full health. Measuring discretionary monetary income instead of psychic income avoids these pitfalls: The claim would be that the tax base ought to be designed so that taxpayers share their pocket money with the government, but that that is the \textit{only} money they must so share. But I will show that the discretionary income argument is subject to the same basic problems as the other arguments. Are health-care expenditures responsive to fixed needs, or are they discretionary themselves?

2. \textit{Problems of mixed motive.}

Even if Professor Andrews could establish that medical care spending does not represent taxable consumption, he would still have to \textit{define} medical care spending. A lot of the money spent on "medical care" produces nonmedical benefits (such as privacy in a more expensive hospital room). The government thus should perhaps ap-

\textsuperscript{98} Many commentators have argued that medical care deductions ought to be allowed because ability to pay is best measured by subtracting all "non-discretionary expenses" from net receipts. \textit{See, e.g., 1 REPORT OF THE ROYAL COMM'N ON TAXATION} 22-24 (1966). According to this argument, the medical care deduction resembles a dependency exemption: The taxpayer who "must" support more children, or who "must" spend money on medical care, is less able to pay taxes. \textit{See note 87 supra} and accompanying text. Professor Andrews makes arguments that, while not framed in this way, give support to this viewpoint. \textit{("[A]llowing a deduction for medical expenses does not involve us in the difficulties of trying to put a price on the enjoyment of good health. The deduction will reflect differences in health only as they manifest themselves in financial terms by requiring substantially different levels of expenditures for different medical services. In this respect the deduction treats substantial medical expenses like a loss of earnings... One who incurs unusual medical expenses, though his salary is interrupted, suffers a similar reduction in funds available for other purposes." Andrews, \textit{supra} note 1, at 336.)}

\textsuperscript{99} Andrews, \textit{supra} note 1, at 326-27.
portion "medical" expenditures between nontaxable medical and nonmedical taxable elements. But Professor Andrews does not deal with this problem.

Professor Andrews concedes that some taxpayers spend more on medical care when faced with a particular ailment than others do. Yet section 213 allows the taxpayer to deduct all expenditures whose primary origin is medical. 100 I will construct and criticize an argument implicit in the Andrews piece—that the section 213 scheme does not erode horizontal equity. I will also comment on Professor Andrews's explicit contention that no vertical equity problems arise from the fact that wealthier taxpayers spend more on health care than do poorer taxpayers.

B. A Critique of Professor Andrews's Position

Professor Andrews's justification of section 213 rests on two assumptions: (1) The tax system should allow some deduction for departures from a baseline of good health, in effect including good health in the consumption tax base while excluding other forms of psychic income. (2) The deduction is measured by what the taxpayer actually spends on "medical care."

After examining its empirical and theoretical surroundings, I will argue that the second assumption is unsupportable. And while the first assumption is not entirely without support, I will show that it presents a far closer question than Professor Andrews implies.

1. Empirical problems.

Professor Andrews's justification for the section 213 scheme would be stronger if we could assume the following features of the medical care market: (1) A taxpayer is unambiguously either in "good health" or in a state of illness or injury, the latter status always being involuntary, and changes in health create greater changes in a person's psychic well-being than do other psychic changes that the tax system ignores. (2) All taxpayers automatically spend the same amount of money whenever they "lose" their "good health" to "get it back." Thus, Professor Andrews portrays a world in which medical care expenditures vary only according to susceptibility to illness: Medical care expenses are price- and income-inelastic, unaffected by changes in income and taste. 101 And perhaps a few real-world cases


101. Medical care expenditure responds to rises in income only insofar as it competes with other income-inelastic "needs" like food and basic shelter. According to the Andrews
fit this paradigm—like an emergency-room visit to stop arterial bleeding. But the literature amply shows that such cases are, to say the least, atypical.

Health care economists agree that the *quantity* of medical services consumed (for example, in terms of *number* of doctor visits) is not as sensitive to changes in income as are purchases of many other goods, though it is by no means insensitive.\(^{102}\) But richer taxpayers tend to buy more *expensive* medical care (for instance, the doctors they visit charge more per hour): The income elasticity of medical expenditures is very nearly one.\(^{103}\) Thus, if \(B\)'s income is double \(A\)'s, \(B\) is likely to spend about double the amount spent on medical care.

The high income elasticity of medical expenditures may reflect a number of factors relevant to the debate on the medical deduction. Richer taxpayers may purchase more technically sophisticated medical care from better-trained doctors. The richer taxpayers, assuming such care is more effective,\(^ {104}\) may be more likely to regain good health. Thus, if the level of health is the relevant consumption category, as Professor Andrews suggests, the user of "better" medical care is likely to have more taxable consumption than the less affluent party treated for the same affliction. Richer taxpayers also more frequently consume such discretionary and unusually costly services as psychotherapy.\(^ {105}\) Whether purchasers of such services have departed from an uncontroversial baseline of good health is questionable. Moreover, richer taxpayers are, of course, more likely to buy amenities incidental to medical care, such as private hospital rooms.\(^ {106}\)

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\(^{102}\) Estimates of the income elasticity of the quantity of medical care demanded vary from .04 to .62. (That is, a 100% rise in income results in a rise between 4% and 62% in the quantity of care demanded.) V. Fuchs & M. Kramer, Determinants of Expenditures for Physicians' Services in the United States, 1948–1968, at 33 n.20 (1972).

\(^{103}\) *Id.* at 34.

\(^{104}\) There is considerable debate about the efficacy of increasing medical expenditures. Evidence suggests that an aggregate rise in health care spending beyond a certain minimum does not increase a population's health. V. Fuchs, Economics, Health, and Post-Industrial Society 3 (1978).

\(^{105}\) This naturally helps explain why the quantity of care demanded is somewhat elastic as well.

\(^{106}\) Prices of medical services vary considerably, depending on the cost of "imbedded consumption services" such as decor and privacy. Looking at pricing policies at four neighboring health facilities which had both private and semi-private rooms, I found that costs were as follows:

*Facility 1*: $50/day private  
$41.10/day semi-private
Rises in income also seem to change the composition of health care expenditures, thus reflecting the difficulty of assuming that a taxpayer has lost his "good health" whenever we observe a "medical expenditure." Rich taxpayers, for example, are much more likely than the poor to obtain preventive or reassuring pediatric care for their children. In 1970, children age 0–5 coming from high-income families made 44 percent more visits to the doctor than their low-income peers; the difference was 41 percent for children age 6–17. There is no reason to believe richer children are more vulnerable to illness; if anything, the opposite seems more likely. Yet to add to the difficulty of measuring health by doctor visits, low-income adults seem to visit the doctor more often than high-income adults.

The rich are also much more likely than the poor to seek dental and obstetrical care. In 1970, 67 percent of those with income above $17,500 saw a dentist, compared with 23 percent of those with incomes below $4,000 and 40 percent of those with incomes between $5,000 and $10,000. Eighty-five percent of pregnant women in the highest income group saw a physician in the first trimester of pregnancy, compared with 71 percent of those in the lowest group. Does "good health" include good teeth or prenatal checkups? Does a regular pediatric visit "restore" the tax-free benefit of freedom from anxiety about a child's health? If many people live with toothaches, backaches, or neuroses, a great deal of "medical care" spending may achieve an atypical rather than a "normal" state of health.

Facility 2: $139/day private or semi-private
(private 21% higher)
Facility 3: $40/day private
$34–$37 semi-private
(full range of difference, private 18% higher)
Facility 4: $50–$60 private
$37–$39 semi-private
(full range of difference, private 61% higher)

The price of routine medical services also varies considerably. Planned Parenthood itself charges $70 for insertion of an IUD and $50 for fitting of a diaphragm. The agency also lists four private practitioners and three clinics whose prices for IUD insertion range from $45 to $77; the prices for diaphragm fitting range from $8 to $60. Prices for an abortion at the four offices and the three clinics range from $185 to $370.

108. Id.
109. Id. at 23.
110. Id. at 22.
111. In fact, members of different economic classes have significantly different perceptions of what symptoms require medical attention. An old but illuminating study of an up-
Estimates of the price elasticity of medical care further demonstrate the problem of a tax definition of "good health." Apparently, a 100 percent increase in the price of hospital care will decrease the quantity of care demanded by 50 to 70 percent,112 while a 100 percent rise in doctor's fees will reduce demand by 20 percent.113 (The availability of substitute forms of health care that can replace hospital care partially accounts for the greater elasticity of buying hospital services.)114 This demonstrates the error of Professor Andrews's initial assumption that expenditures are consistent for given diseases: Allowing full deductibility of the cost of a day at the hospital falsely assumes that hospitalization was the only treatment regimen available.

2. Conceptual problems.

The factual record suggests that a deduction tied to actual "medical care" spending is unjustifiable unless there is good reason to allow deductions for all expenditures whose "origins" lie in medical needs.115 But the factual record does not so clearly disprove the validity of some deduction for departures from "good health," since differences among taxpayer decisions whether to obtain medical service remain smaller than differences in what taxpayers will pay once they do seek care.116 Yet even if true departures from good health could be identified and their value measured, ought the tax system reflect such departures? Two things suggest it should not: Many present departures from good health result from past decisions that gave the taxpayer untaxed benefits, and the tax system generally does not tax psychic income.

state New York city divided the population into three economic classes and asked respondents which symptoms on a given list should be called to the attention of a doctor. At least 75% of the respondents in the highest socioeconomic class studied checked all but two of the symptoms listed. Respondents in the lowest socioeconomic class checked 10 items less than 25% of the time and only three symptoms, all related to unexplained bleeding, were checked by more than half of these respondents. E.L. Koos, The Health of Regionville 32–37 (1954).


113. Id. at 405 n.39. Visits are even more price elastic than these figures imply if one accounts for the fact that consumers put a positive value on their use of time—increases in time associated with a doctor visit will lead to a decline in visits. Holtman, Prices, Time, and Technology in the Medical Care Market, 7 J. Human Resources 179 (1973).


116. See notes 102–03 supra and accompanying text.
The time factor. It is plausible that most medical needs really arise from voluntary decisions to pursue potentially unhealthful activity: Professor Andrews and section 213 obscure this problem by avoiding all focus on the taxpayer's health until the moment he becomes "ill." People voluntarily engage in conduct that puts their health at risk. A and B both love to smoke. A quits smoking and averts lung cancer but loses the (untaxed) pleasure he got from smoking. B continues to enjoy the pleasure of smoking, and is allowed to deduct all medical expenses for ailments caused by her smoking. Perhaps Professor Andrews's baseline consumption position should be refined to include ordinary taxable consumption and health and pleasure from her risky activities: A deduction for the loss of health without inclusion of the gains from risky activities will mismeasure how relatively well-off the two taxpayers are.

Even Professor Andrews's paradigm case—the tortiously inflicted loss of health—may involve some voluntary risk. People avoid tortious injury (at some psychic cost) if they closet themselves from most activity. Recognizing that medical spending may involve discretion before illness manifests itself, it is no longer plausible to say that such spending "restores" the taxpayer to a baseline position enjoyed by those without medical care "needs."

Other types of psychic pleasure. Professor Andrews emphasizes, in his defense of the charitable deduction, that consumption does not equal pleasure.117 Why, then, is the pleasure of good health included in the tax base while other psychic pleasures are ignored? Professor Andrews offers no reasons. I will put forth two possible reasons—and refute them.

First, although Professor Andrews claims that the exclusion of pleasure from the tax base rests on principle,118 one could argue that the real reason is administrative—the difficulty of valuation. Perhaps the pleasure of health is included, then, simply because it can be valued. The tax system cannot allow Z, the man who moves from a terrific job to a terrible one for a $10,000 pay increase, to deduct the increase as representing the restoration of the untaxed benefits of the good job, because it has no objective way to tell how much of the $10,000 restored old pleasure and how much increased his well-being. If the minimum value of good health is the amount a taxpayer

117. Andrews, supra note 1, at 355-56.
118. Id. at 356.
But the distinction has both theoretical and practical flaws. The tax system generally does not exclude a benefit from the tax base entirely simply because the benefit is hard to value.\(^{119}\) Moreover, so long as some taxpayers do not purchase all aspects of "good health," the tax system will inevitably mismeasure well-being by incorrectly assuming that all nonpurchasers enjoy good health, even if it correctly measures the value of "health" to those who do purchase its restoration. Finally, because "medical spending" includes nonmedical elements, insoluble practical problems remain: The value of restoration may not equal the cost of the "cure." The taxpayer who spends $5,000 on a sinusitis cure at an Arizona resort may not be willing to spend that much to buy pills that cure the disease.

A second argument for distinguishing health from other psychic pleasure is that taxpayers differ in their health far more than they do in other forms of well-being. But this is not plausible. It seems unlikely that a clearly "medical ailment" like tendonitis causes more suffering than a quasi-medical one that will slip outside section 213 coverage, like untreated clinical depression,\(^{120}\) or more than a bad marriage or boring job. All that is clearly true is that disease is likely to be far more equally distributed among income classes than are other forms of distress,\(^{121}\) so drawing a distinction between health

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119. As Justice Clark noted, "once it is recognized that the transfer was a taxable event, it is more consistent with the general purpose and scheme of the taxing statutes to make a rough approximation of the gain realized thereby than to ignore altogether its tax consequences." United States v. Davis, 370 U.S. 65, 72–73 (1962); see Reginald Turner, 23 T.C.M. (P-H) ¶ 54,142 (1954). Deferral might be appropriate pending the resolution of valuation problems. See Burnet v. Logan, 283 U.S. 404 (1931) (deferral of taxation where valuation of open transaction impossible). But see Ginsburg, Taxing the Sale for Future Payment, 30 TAX L. REV. 469 (1975) (critique of policies permitting ordinary deferral opportunities).

120. Depression is certainly pandemic in America; ignoring its effects in a tax system that attempts, as Professor Andrews does, to measure significant disparities in psychic income distorts the facts. During any given year, 15% of the adult population may suffer significant depressive symptoms. According to the National Institute of Mental Health, 50% of depressed people in the United States are not being treated; relying on medical expenditure deductions to serve as a proxy for deducting the psychic loss of depression is ineffective. Coping with Depression, NEWSWEEK, Jan. 8, 1973, at 51 (providing slightly different estimates of the problem); Depression: Our Common Curse, SATURDAY EVENING POST, Dec. 1975, at 54.

121. Generally, physical health is distributed rather equally by class. V. FUCHS, supra note 104, at 4–5. Confirming evidence can be found in Lefcowitz, Poverty and Health: A Reexamination, in THE HEALTH GAP 40, 44–47 (1976). Other forms of psychic benefits do not seem to be so distributed. For instance, if we decided to add the psychic income derived from "happiness in marriage" to the consumption tax base or allow a deduction for the "onset of divorce," perceived cross-class inequality would probably rise. In 1970, more than 20% of all those with incomes below $5000 had been divorced, and divorce rates decreased as incomes
and other psychic pleasures could allow the rich taxpayer to pay relatively lower taxes.\(^{122}\)

increased until, at incomes of $15,000 or greater, less than 11% had been divorced. 1970 Census of Population, Subject Reports: Marital Status 223 (1972). Moreover, richer people seem to be less depressed. While in Cook County from 1959 to 1963 the suicide rate of managers was 15.8/100,000 and of professionals was 14.8/100,000, laborers had a suicide rate of 50.6/100,000 and service workers had one of 46.4/100,000. R. Maris, Social Forces in Urban Suicide 122 (1969). Thirty-three percent of persons with incomes below $6,000/year experienced symptoms of “intense anxiety” in a 1976 survey, compared to only 13% of those with incomes above $18,000. Radabaugh, Economic Strains and the Coping Functions of Alcohol, 81 Am. J. Soc. 652, 657 (1976).

122. Including a benefit in the tax base that is distributed equally decreases progressivity; deducting an equally distributed burden increases the perceived degree of inequality and thus increases progressivity. Thus, a § 213 deduction scheme would increase progressivity if expenditures on equally distributed disease do not vary by class. A conceptually equivalent scheme which adds the value of equally distributed good health to each healthy taxpayer’s income would lower progressivity.

An algebraic example demonstrates that the § 213 scheme accepted by Professor Andrews would increase progressivity if medical expenditures on fixed diseases did not vary.

\[
X = \text{average income before medical expenses of a “rich” taxpayer.}
\]

\[
cX = \text{average income before medical expenses of a “poor” taxpayer (0<c<1).}
\]

Before medical deductions, the fraction \(X/cX\) represents the degree of inequality between rich and poor. We now introduce medical deductions.

\[
P = \text{probability of a taxpayer, rich or poor, becoming ill (0<P<1).}
\]

\[
D = \text{average deductions resulting from illness.}
\]

\[
PD = \text{expected medical deduction for a taxpayer, rich or poor.}
\]

\[
X - PD = \text{rich taxpayer’s expected taxable income.}
\]

\[
cX - PD = \text{poor taxpayer’s expected taxable income.}
\]

The fraction \(X/PD\) now represents the inequality between the average rich and poor taxpayer. This new fraction is larger than the inequality ratio before the medical deduction,

\[
\frac{X - PD}{cX - PD} = \frac{X}{cX} (1 - \frac{PD}{cX})
\]

\[
= \frac{X}{cX} (1 - \frac{PD}{cX})
\]

\[
= \frac{X}{cX} (1 - \frac{PD}{cX})
\]

\[
= \frac{X - PD}{cX - PD}
\]

\[
= \frac{X - PD}{cX - PD}
\]
C. Problems of Mixed Motive

Professor Andrews concedes that rich taxpayers probably spend more on medical care than poorer taxpayers when afflicted with the

\[
\frac{PD - PD}{cX - PD} = \frac{PD}{cX} \cdot \frac{1 - 1}{cX - PD}
\]

\[
\frac{PD}{cX} \cdot \frac{1}{c} > 0
\]

because \( c \), being less than 1, makes \( 1/c \) greater than 1. If the difference between the inequality ratio after medical deductions and before medical deductions is greater than zero, then the former must be greater than the latter.

A similar equation shows how taxing all healthy people for the benefit of their good health would tend to make the incomes of the rich and poor more equal and thus decrease the progressivity of the tax system. If \( P \) is the probability of being sick, then \((1 - P)\) is the probability of being healthy. The average rich taxpayer would have a taxable income of \( X + (1 - P)D \) (assuming the benefit of being healthy equals the cost of being sick); the average poor taxpayer would have a taxable income of \( cX + (1 - P)D \). Subtracting as before,

\[
\frac{X + (1 - P)D}{cX + (1 - P)D} - \frac{X}{cX} = \frac{X + (1 - P)D}{cX} - \frac{X}{cX} \frac{(1 - P)D}{cX}
\]

\[
\frac{X + (1 - P)D}{cX + (1 - P)D} - \frac{X}{cX} = \frac{X + (1 - P)D}{cX + (1 - P)D} - \frac{X}{cX} \frac{(1 - P)D}{cX}
\]

\[
\frac{(1 - P)D}{cX} - \frac{cX + (1 - P)D}{cX + (1 - P)D} = \frac{(1 - P)D}{cX} - \frac{cX + (1 - P)D}{cX + (1 - P)D}
\]

\[
\frac{(1 - P)D}{cX} - \frac{cX + (1 - P)D}{cX + (1 - P)D} < 0
\]

again because \( c \), being less than 1, makes \( 1/c \) greater than 1. The inequality ratio was greater before the benefit of good health was included in taxable income; the change hindered progressivity, assuming that rates are not altered.
same ailment. He argues, however, that this disparity causes no great problem of vertical equity, because the government can adjust tax rates to account for spending by the rich incidental to the purchase of medical care left outside the tax base because of section 213.

To illustrate this argument, we can assume a 2-class world: Class 1 consists of people with incomes between $50,000 and $60,000 a year, and Class 2 of people earning between $10,000 and $20,000. Taxpayer A makes $50,000 a year and is disease-free; B makes $60,000 and suffers from condition Q. B spends $10,000 to treat the condition. C makes $10,000 and is as healthy as A. D makes $12,000 but also suffers Q, which he spends $2,000 to cure. Professor Andrews claims that the tax system can ignore the disparities between B's medical spending and D's, even if B's extra expense goes to traditional consumption (such as a private room), so long as Class 1 taxpayers generally engage in such incidental luxury "medical" spending. The government can adjust rates to tax the consumption inherent in B's spending. Professor Andrews would argue that the sole concern in defining the tax base should be ensuring horizontal equity between A and B and between C and D.

Unless all members of an income class make the same class-differentiated expenditures, Professor Andrews is wrong to ignore vertical effects. As a matter of empirical reality, taxpayers within a given class do not all face the same medical expenditures. The probability of a taxpayer who earns between $100,000 and $200,000 a year facing a medical expense exceeding the percentage-of-income limit on deductibility is less than 10 percent. Only 62 percent of itemizing taxpayers with incomes over $100,000 take any medical deductions.

124. Id. at 339 ("In general, when considerations of horizontal and vertical equity seem to conflict, decisions about the tax base should rest primarily on horizontal considerations, since vertical considerations can be reflected in the rate structure.").
125. Presumably, then, it does not concern Professor Andrews that the mean tax reduction in 1970 arising from the I.R.C. § 213 deductions for taxpayers with incomes between $100,000 and $200,000 a year was $301 compared with $18 for those with incomes from $7,000 and $8,000 and $1 for those with incomes between $1,000 and $2,000. Mitchell & Vogel, Health and Taxes: An Assessment of the Medical Deduction, 41 S. Econ. J. 660, 667 (1975).
126. But see notes 135–40 infra and accompanying text, where I argue that horizontal equity considerations also dictate eliminating the deduction.
127. Mitchell & Vogel, supra note 125, at 667.
128. Id. at 662.
If the government raises the marginal tax rate for Class 1 taxpayers because they spend more on medical care than Class 2 taxpayers when they are sick, the substantial majority of Class 1 taxpayers without large medical claims can justly feel persecuted. $A$ would face a greater tax bill than would otherwise be proper for a taxpayer who earns $50,000 a year just because $B$, when he is sick, chooses to spend more on health care than do lower-income taxpayers with similar ailments. If the rate-setter assumes that Class 1 taxpayers have $50,000 for traditional consumption and good health (through the mechanism of permitting deductions for spending to rectify departures from good health) and some consumption incidental to health care, the rates will be inequitable to $A$, who simply does not make the third class of expenditure. Congress is likely to ignore some or all of $B$'s consumption to avoid imposing an unwarranted loss on $A$, thus dealing a blow to progressivity.


When $B$ spends $10,000 “curing” a disease, and the “cure package” includes additional consumption items, she seems clearly better off than disease-free $A$, at least to the extent of the consumption component of the “cure.” Professor Andrews argues that $A$ and $B$ are equally well off, though this view implies that $E$, who makes $52,000 a year but spent only $2,000 to cure his $Q$, would be taxed just like $B$, though he seems undeniably worse off. The problem is one of causation. Professor Andrews would have to construct some sort of “origins” test to show that a taxpayer should be allowed a deduction for all his actual spending on a cure, even where some of it seems to go to traditional consumption, so long as the taxpayer would never have made any part of that expenditure had he not become ill.

In cases where some of $B$'s medical expenditure undeniably goes to traditional consumption (like a limousine ride to the hospital),

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129. I will ignore that case in which the taxpayer engages in an activity, like eating, which he engages in inside or outside the medical care setting and for which he pays higher prices than are necessary. I think that Professor Andrews would call this a “hard” case, although ultimately it is conceptually indistinguishable from cases he considers “easy.” For instance, the taxpayer consumes kosher food at the hospital, which increases his food bill there, just as it does when he is not in the hospital. Upon reflection, this “hard case” is not so different from the “easy one.” It is indeed true that a taxpayer does not purchase privacy-in-the-hospital unless he is sick, while he does purchase kosher food whether in the hospital or not. But the taxpayer does purchase privacy-on-the-outside and he does not purchase kosher-food-in-the-hospital unless he is sick. Nonetheless, I suspect that Professor Andrews would
$B$ would have to argue: (1) The limousine ride only serves to reduce the pain of her illness; it does not make her better off than she would have been had she never been ill. (2) Medical misfortune is the “but-for” cause of all the spending; had $B$ not become ill she never would have gone to the hospital at all. And (3) deducting the entire expenditure is consistent with the principle that taxpayers may deduct all ordinary and necessary business expenses, including those that happen to give them more personal pleasure than was strictly necessary for the business purpose (such as dining with clients at fine restaurants rather than cafeterias).  

The argument would be unconvincing. The “pain-relief” test may simply encourage taxpayers to engage in excess consumption whenever they have a reasonable claim of a “medical” origin. Defining a baseline state of satisfaction in terms of the uninjured taxpayer and allowing deductions for all expenditures which do not make him better off than he was before injury gives injured taxpayers broad power to engage in extravagant consumption at less cost than had they avoided injury. Moreover, any act of consumption can be called pain-reductive rather than pleasure-seeking. A taxpayer who buys an air conditioner after moving from Alaska to Florida could say he is simply “restoring” the “normal” atmosphere in which he was previously comfortable. Unless the tax system devised some accurate philosophical or psychological tool for distinguishing reductio of pain from increase in pleasure, this stage of the argument will be hollow.

The “but-for” causation test is unpersuasive because it is arbitrary to automatically attribute the portion of an expenditure above that necessary to cure illness to the first-in-time cause. If $B$ had taken a limousine to the theater when well, she certainly would have been balk at a deduction for a high cost “special diet” which is not “caused” in a “but-for” sense by the hospital visit.

130. For example, businessmen may deduct first-class accommodations on business trips. See Treas. Reg. § 1.62-1 (1977). I believe that this principle is wrongly accepted. See notes 135–40 infra and accompanying text.

131. For example, $B$ eats gourmet food to make up for the fact that she cannot enjoy skiing while her injured knee heals; even if she would have been happier spending money on skiing rather than truffles, it is difficult to call truffles “pain-reductive” and therefore deductible.

132. Each time a person buys something, he might say he would just as soon not have felt the urge to purchase it. He could argue that the tax system should tax ascetics the same as high-spending compulsive materialists like himself because the former enjoy the implicit income of not feeling painful desires to consume, but it is unlikely that the argument would be taken too seriously.
taxed on the cost. While the remote root of the limousine trip to the hospital may be ill health, the decision seems to bear a more immediate nexus to general consumption desires.

A proponent of full deductibility might respond at this point that my attack fails because it points to problems the tax system clearly tolerates in the business expense deduction. But the parallel between the two deductions is misleading. While problems of mixed motive make full deduction inequitable for both medical and business expenses, we are, in a strong sense, saddled with a tougher administrative problem in the business area. First, the tax system must allow on principle some deduction for business expenses, the costs of producing income, in order to establish net income in the first instance. But the medical care deduction, at best an unusual attempt to refine the tax base to account for psychic income, is hardly as integral to the system as sections 162 and 212. Second, to ascertain whether income-producing expenditures are stripped of superfluous consumption elements would often require an administratively nightmarish case-by-case analysis of the long-term least-cost production techniques. In the medical care area, a standard deduction for specific ailments, as in a Workmen’s Compensation scheme, might work fairly simply. It is instructive to note that even in the business area, Congress may disallow deductions for personal consumption aspects of an expenditure when the least-cost means of producing income are identifiable.


A proponent of some form of medical deduction may still insist that the business deduction analogy is instructive—not because the business deduction is fully on point, but because it points to theories about the general problem of joint causation in tax law that may apply to the medical deduction. The tax literature addressing the business expense has posed a number of solutions to the problem of the

133. A’, in absolutely Spartan surroundings, nets $50,000 a year; B’, with Matisse prints lining his wastebaskets, also nets $50,000 but if he avoided such “frills” he would net $60,000. B’ can almost surely deduct such frills as a business expense. One could say that B’ would still rather be at home than at work, and as long as he has not made the office more desirable than leisure, he has simply “minimized the pain” of sacrificing leisure or one could note that the “but-for” cause of the frills was setting up an office to generate income.

134. For instance, the recently enacted I.R.C. § 274(h)(2) limits deductions on foreign convention travel to the price of a tourist class ticket. Naturally, one could explain § 274(h)(2) as a boon to the domestic travel industry, rather than a principled response to the problem of accounting for imbedded consumption.
mixture of consumption and nonconsumption elements in one expenditure: (1) allow the deduction only if the deductible element is the but-for cause of the spending; (2) allow full deductibility only if the deductible element is sufficient to account for the expenditure; (3) allow the deduction only if the deductible interest is dominant in the decision to spend; and (4) not allow the full deduction, but apportion the expense between the consumption and nonconsumption elements. But none of these approaches bears much scrutiny.

But-for tests. As I noted earlier, the but-for causation test simply is too generous. A trivial medical interest can transform a marginally unattractive potential consumption expenditure into a profitable and irresistible one. The taxpayer would spend only $5,000 to cruise the Caribbean; he convinces us that he purchased the $5,100 cruise ticket because it is worth a bit more than $100 to him to get physical therapy on the cruise. Should we allow $5,100 of deduction because he would not have spent the money “but-for” the physical therapy? Obviously, the result of the but-for test depends on arbitrary choice of starting points. Should the tax system allow deductibility whenever the deductible cause is a but-for cause, or disallow deductibility whenever the consumption element is a but-for cause?

Sufficiency and domination tests. A sufficiency test may appear the most sensible and most administrable. But it fails, because the tax system simply cannot determine whether the precise marginal expenditure is accounted for by medical reasons even when the expenditure as a whole is explicable without regard to the personal consumption element. Assume the taxpayer spends $10,000 on a cruise which does, in fact, appear to relieve an illness which it would be rational to spend that much treating. The tax system cannot determine whether

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136. Once an expenditure is sufficiently explained by business motive, no sane taxpayer will admit to personal motives. See Klein, supra note 135, at 1111. The fact that only the sufficiency test is administrable makes “domination” tests a bit chimerical, even if they were conceptually proper. But cf. Henry v. Commissioner, 36 T.C. 879 (1961) (if personal motives dominate business motives, fact that income has been generated will not ensure deductibility).
the medical motive was sufficient to account for the actual spending unless it knows whether $50 of medication would also have fully cured the condition but the cruise was simply more attractive.\textsuperscript{137} A domination test falls prey to the same problem: Do we measure whether the business or medical motive is the dominant motive for the expenditure as a whole or some portion of the expenditure?

Apportionment. At the other extreme, apportionment inevitably fails administratively because no taxpayer will ever admit personal motives when a business motive sufficiently “explains” the expenditure. In addition, adoption of a general apportionment principle will have far-reaching consequences for currently nondeductible expenditures, some portion of which could arguably be deducted.\textsuperscript{138} There are theoretical problems as well. Assume the taxpayer pays $5,000 for a physical therapy cruise that produces adequate curative benefits to justify the decision to go on the cruise. He (coincidentally?) would have purchased cruise tickets for the same price had he had no medical needs. Thus, the deductible and nondeductible motives each “explain” the entire spending decision. An apportionment scheme would allow him to deduct only $2,500, the proportion of the expenditure attributable to deductible roots. This solution seems like an utterly unprincipled compromise between two competing tax policies. Proponents of taxation on all consumption would allow no deductibility while those who believe that the consumption benefits accompanying business or medical spending resemble untaxed consumer surplus would allow full deductibility. Proponents of a tax on all consumption believe that the tax system should use the taxpayer’s command over resources to measure how well off he is. The latter position assumes that as long as the taxpayer is not taxed on consumer surplus he ought not to be taxed on any consumption pleasures that he did not “have to buy.”\textsuperscript{139} The sole appeal of the apportionment solution

\textsuperscript{137} The ability to decide when some portion of a unified spending decision is worthy of separate consideration is important in a variety of contexts, but the rules formulated in such contexts are not well illuminated. For example, it was not difficult to devise rules to distinguish home office expenditures from expenditures on the house as a whole. See I.R.C. §§ 162, 183; Treas. Reg. § 1.262-1(b)(1) to (4) (1972). However, in divorce litigation the courts have been unable to apportion a single bill to a lawyer between personal and business aspects. See, e.g., United States v. Patrick, 372 U.S. 53 (1963).

\textsuperscript{138} A vacation trip to Hawaii (which gives one a tan that might help attract clients) might have to be apportioned, though it is clearly entirely nondeductible now, if we decide to apportion expenditures that are now clearly fully deductible.

\textsuperscript{139} It is possible that “consumer surplus” is more evenly distributed across taxpayers than is the ability to make business expenditures which give personal benefits. Thus, the failure to tax consumer surplus may in part be motivated by a sense that including each
is its recognition that neither of these strains of tax jurisprudence is sufficiently powerful to overcome the other.

In short, any expenditure-oriented scheme will inevitably fail to solve the joint causation problem: As long as medical care expenditures include personal consumption elements, the section 213 scheme will not be rationally defensible. 140

IV. CONCLUSION

Ultimately, I suspect that my support of a net receipts tax and taxpayer's surplus in the rate base would not lead to a different arrangement of taxpayers according to income, but only cause an aggregate proportional rise. See note 82 supra.

140 The courts have moved in the same direction in the medical context as they have in the § 162 and § 212 areas. The same scope of view problems abound here as in the "sufficiency test" for deducting business expenditure: What is the expenditure to look at—the whole bill the taxpayer has paid to the hospital or the itemized accounts? The courts largely ignore this problem and instead try to restrict deductibility in other ways, though these conceptual limits are narrowly interpreted. Ordinarily, if the expenditure would, or even might, have been made in the absence of a defect, where the defect is not a but-for cause of the expenditure, deductibility will be denied; thus, often where there are two sufficient causes of the expenditure, the personal is deemed to govern. See, e.g., Jacobs v. Commissioner, 62 T.C. 813 (1974) (legal expenses of divorce recommended by psychiatrist to ameliorate mental health problems nondeductible for failure to establish illness as but-for cause). But see Starrett v. Commissioner, 41 T.C. 877 (1964) (expenses for psychiatric treatment deductible despite equally motivated purpose of qualifying for admission to institute's training curriculum). The absence of a but-for cause serves as a tripping mechanism for the court to inquire whether the medical context might be a bad faith cover to allow deductibility. But some see this test as one that demands the taxation of consumption: If an expenditure would have been made without a deductible root, it is taxable. This necessarily involves a determination of whether the whole expenditure is explicable without reference to the deductible root. Here the absurdities of the but-for test become manifest.

If there is little reason to believe that the treatment will be effective in ameliorating the defect, deductibility will be denied—presumably on the theory that if it is not going to remedy the disease, it must be satisfying some other consumption urge. See, e.g., Ring v. Commissioner, 23 T.C. 950 (1955) (deduction disallowed for costs of trip to Shrine of Our Lady of Lourdes in France). The logical extension of these rulings—that any patient paying for care that is not ameliorating his condition must be "buying something else"—could wipe out a good deal of medical care deductions, whether for purely hypochondriacal visits or for heroic efforts with terminal patients without realistic chances of recovery. This extension, of course, has not been made: The courts have conferred this limit to cases of "unusual" cure.

In a peculiarly limited class of cases, the courts and the Service will deny deductibility of certain expenses that in some sense substitute for ordinary nonmedical care spending, even when these expenditures are tied up with a treatment plan. Compare Commissioner v. Bilder, 369 U.S. 499 (1962) (expenditures for meals and lodging while visiting Florida for health reasons nondeductible), and Newman v. United States, 68-1 U.S. Tax Cas. ¶ 9,411 (W.D. Ark. 1968) (deduction for costs of special food for diabetic denied, with Randolph v. Commissioner, 67 T.C. 481 (1976) (deduction allowed for additional cost of medically required chemically uncontaminated foods). See note 129 supra for a critique of the idea of limiting "substitution" tests to cases like that of food.
Professor Andrews's support of use-oriented deductions reflect the different ideological lenses through which we view reality.

The economic stratification in our society is extreme. Given citizens of widely divergent talent and background and a hierarchical wage structure in which people respond to wage signals in choosing what work to do, no tax system could eliminate this stratification. But progressive taxation may help to mitigate it.141

A tax system whose goal is redistribution must look to the taxpayers' relative abilities to pay. But I do not advocate a direct tax on ability to earn to achieve this goal, because I both recognize its administrative difficulties and think the tax system's respect for a taxpayer's refusal to treat potentially marketable resources as commodities represents a desirable anticapitalist strain in a market-obsessed culture. But I believe that once people deliberately exercise their earning power in the market, the tax system should measure their relative positions as a prelude to redistribution.

My opposition to the charitable donation is bolstered by my sense that charitable donors are the same as everyone else in an individualist culture: They use their money for their own relative benefit. Even the most sincere altruist buys the scarce resource of looking altruistic.142

My hostility to an expenditure-oriented medical care deduction is sharpened by my feeling that a capitalist system encourages its members to disguise their ability to pay in order to avoid taxes. Government spending benefits everyone, regardless of individual tax payment; but each person's tax payment reduces her ability to make private appropriations. And as long as the taxpayer's sense of "utility" is grounded in private consumption, she will assume an adversarial role with respect to the tax system. The government inevitably exacerbates the problem by putting the tax law in terms of "rules"

141. I doubt that a tax system can radically redistribute income. However, radically different distributions of income might be possible, efficient, and politically acceptable if production could be reorganized so that high earners could not initially receive high income shares. See Kelman, The Ambiguities of Tax Reform, in 6 Working Papers for a New Society 85 (1978).

142. "That which exists for me through the medium of money, that which I can pay for, i.e. which money can buy, that am I, the possessor of the money . . . . Therefore, what I am and what I can do is by no means determined by my individuality. I am ugly, but I can buy the most beautiful woman. Which means to say that I am not ugly, for the effect of ugliness, its repelling power, is destroyed by money. . . . I am a wicked, dishonest, unscrupulous and stupid individual, but money is respected, and so also is its owner." K. Marx, Economic and Philosophical Manuscripts, supra note 38, at 377.
rather than "standards." A taxpayer can manipulate a "rule" ("deduct medical expenditures") by imbedding as much consumption as she can into an imprecise legal definition of a nontaxable transaction. The government can observe only the flow of money—it is largely bound by the taxpayer's initial characterization of her expenditure. While the government could interpret a "standard" ("deduct reasonable medical expenditures") to serve the ultimate purpose of measuring true ability to pay, standards are inevitably nonadministrable and prejudicially enforced.

I certainly can do no more than speculate on Professor Andrews's political principles. I think he believes that a focus on earnings overstates the nominal inequalities in society—that rich donors share, rather selflessly, to mitigate inequalities, and that the rich suffer ailments which make them worse off than they appear. He is apparently not bothered that the circumstances of the rich donor may be better than those of people who cannot donate precisely because the rich are able to donate—because the rich may be better off psychologically in many other ways that the government cannot tax. He is not concerned that the charitable and medical deductions inevitably flatten the tax base. Protecting progressivity is not high on Professor Andrews's agenda.

Most significantly, I suspect that Professor Andrews's concept of use distinctions is based on a misunderstanding of the nature of consumption in a capitalist culture. Abstractly, one could argue that activities (like donating or buying medical care) have intrinsic purposes—that there are, in effect, "right reasons" for engaging in the activity. Sir Bernard Williams, for instance, argues that the "right

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143. For a full discussion of the tension between rules and standards in our legal culture, see Kennedy, Forms and Substance in Private Law Adjudication, 89 Harv. L. Rev. 1685 (1976).

144. For instance, if we exempt some sorts of in-kind income because we usually cannot value the in-kind receipt, see, e.g., I.R.C. § 119 (exempting value of meals and lodging received for convenience of employer on employer's premises), particular taxpayers will be encouraged to take income in-kind. Problems of whether tax-collecting authorities can overturn a tax-motivated transaction simply because it is tax-motivated will inevitably plague the courts. See, e.g., Knetsc v. United States, 364 U.S. 361 (1960); Gregory v. Helvering, 69 F.2d 809 (2d Cir. 1934) (L. Hand, J.), aff'd, 293 U.S. 465 (1935).

145. Conservative theorists focus a great deal on the ways in which nominal income purportedly overstates real inequality. See, e.g., M. Friedman, A Theory of the Consumption Function (1957) (inequality in transitory income, which is what we measure when looking at tax returns, is greater than inequality in lifetime or permanent income because of year-to-year fluctuation); Friedman & Savage, The Utility Analysis of Choices Involving Risk, 56 J. Political Econ. 279 (1948) (nominal inequality may be overstated because some people voluntarily choose to receive less risk of fluctuation so that their utility position is equivalent to that of those with higher nominal incomes).
reason” for supplying, and perhaps, by extension, purchasing, medical care is to cure illness and that a society which distributes medical care according to money claims is acting for an intrinsically inappropriate reason.\textsuperscript{146}

But in a capitalist society, where the aim of all activity is to satisfy individual subjective desire,\textsuperscript{147} claims of intrinsic purposes are inapt.\textsuperscript{148} Professor Andrews’s use distinctions must assume that activity is restricted in purpose—the buyer of medical care only pursues the intrinsically appropriate aim of medical care (curing illness) and the donor seeks only the intrinsically pure aim of donating (the private knowledge that he has helped someone else to consume). But in a market economy, the use of funds usually defies an attempt to identify a single purpose: Money is a medium that cancels all need for explanation. The claimant of medical care need not justify his claim; he need only pay the bills. The charitable donor can attach whatever conditions he wants to his “gifts.” This observation may well provide the basis for an attack on market economies; it ought not to be ignored in designing a tax system within such an economy.

It may be possible to imagine a tax system which can distinguish medical care purchases from other purchases because the society distributes medical services according to need rather than desire. But our ability to hypothesize the pure medical care purchase should not suppress our sense of contradiction as we face the real section 213 scheme—the contradiction between the notion “Getting sick and having to spend money to get well again is just like never getting the money in the first place,” and the notion “Actual spending on sickness is just like actual spending on everything else.”

If the purpose of defining a tax base is to determine relative abilities to pay and if earnings capacity best measures ability to pay and if net receipts best measure earnings capacity (given the desirable side constraint of respecting the decision not to enter the market), an income tax that ignores different uses of received income is presump-


\textsuperscript{147} See R. Unger, \textit{Knowledge & Politics} 76–81 (1975).

\textsuperscript{148} Nozick denigrates the very idea of an intrinsic purpose to an activity. His derision seems appropriate within the capitalist culture. Even if we assumed that “doctoring” had to be allocated according to medical need, there could be a parallel activity where providers gave “medical services” for money and purchasers bought such services for any or no reason. As Nozick says, “let ‘schmctoring’ be an activity just like doctoring except that its goal is to earn money for the practitioner; has Williams presented any reason why schmctoring services should be allocated according to need.” R. Nozick, \textit{supra} note 33, at 235.
tively just. There are a number of arguments for accounting for one sort of use in picking a tax base, exempting funds "used" to save— but one ought to be wary of such focuses on uses, particularly when taxpayers in higher income classes are more prone to use their funds to make exempt purchases. Use distinctions among consumption items should be particularly suspect: Andrews's distinctions between either charitable or medical care spending and other forms of taxed spending are tenuous; ultimately, one would be very unlikely to adopt them unless one's goal were to reduce the progressivity of the tax system or increase its complexity.

149. The central debate in current academic tax literature is whether we should tax savings currently or should defer taxation until the taxpayer consumes. See generally N. Kaldor, supra note 12; U.S. Dep't of Treasury, supra note 12; Andrews, supra note 12; Warren, supra note 12.