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**In Retrospect of 40 Years, Another Look at Andrews’
Personal Deductions Argument:
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and Child-Care Expenses**

*Limor Riza**

INTRODUCTION

In this Article, I would like to compare two major types of expenses – charitable contributions and child or dependent care expenses – to determine whether they should be deducted from gross income. Although these two expenses have common ground, they are also fundamentally dissimilar. Both expenses are not strictly “private” since they have a normative aspect. Moreover, as suggested by William Andrews in his classical article, *Person Deductions in an Ideal Income Tax*, we should not ignore the use side of the economic equation, which is also relevant to both.¹ Nevertheless, in this Article, I claim that similar treatment of both expenses ignores the income production process, leaving us with a flawed and incoherent tax system.

Andrews discusses some personal expenses that should be excluded from taxable income. He examines the ideal personal income tax with regard to the taxation of personal deductions, and finds the conventional tax expenditure analysis lacking² in that it disregards the *uses* of income as opposed to its *sources*.³ His main argument is that taxable income should be defined by the former, rather than the latter, to prevent the distortion of pretax equality and that the examination of uses facilitates an ideal discussion of personal income tax.⁴ A fair distribution of tax burden is one that takes both consumption and accumulation into account.⁵ The significance of Haig-Simon’s⁶ formula, according to money cash definition, lies not so much in the taxpayer’s

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1. William D. Andrews, *Personal Deductions in an Ideal Income Tax*, 86 HARV. L. REV. 309, 313 (1972); *see infra* Chapter II (elaborating on this discussion).

2. *Id.* at 312.

3. *See id.* at 313, 317, 320 (emphasis added).

4. *See id.* at 316, 328.

5. *See id.* at 316.

6. *See infra* Chapter II.

“participation in the production sector”⁷ but rather in the “distribution sector”⁸ whereas the tax system has a distributive goal.⁹ Although the argument may be somewhat tautological,¹⁰ “deduction should be allowed whenever money is expended for *anything other than personal consumption or accumulation*. And that, arguably, is the intrinsic role of personal deductions.”¹¹ He believes that the justification of deductions “is intrinsic to the elaboration of an ideal personal tax base.”¹²

Andrews illustrates his argument with medical expense and charitable contribution deductions. He rationalizes the deductions of those expenses differently,¹³ despite the fact that the starting point of both is focused on the use side. His main argument for allowing medical expense deductions and excluding them from the tax base is largely distributional.¹⁴ Contribution to charity, on the other hand, is not consumption and thus should be deductible since it is dedicated to third parties and not to the private use of the donor-taxpayer.

Andrews’ position is interesting in several respects. First, its baseline is that the tax system should have some intrinsic objectives.¹⁵ As discussed below, I believe we should strive for a coherent and consistent system though Andrews’ work does not provide us with a one.¹⁶ The second, and more important and appealing, aspect of his work is the focus on the use side of the economic equation. This focus draws various “normative” expenses into the tax system, thus apparently introducing extraneous principles, such as redistribution. Indeed, the following analysis argues that taxation serves two purposes beyond raising revenue: regulatory and redistributive. I do not object to tax incentives for these two purposes; but, by focusing on the use side and somewhat neglecting the income production side, Andrews fails to

7. Andrews, *supra* note 1, at 324.

8. *Id.* Andrews continues, “[a]nd when we say income is to be taxed in whatever form received, it is the latter relation, not the former, that we should seek to refine.” *Id.* For an elaboration see *id.* at 327.

9. *Id.* at 326.

10. Andrews starts his claim by saying that “either that thought is circular since it effectively defines consumption in terms of income or it represents reversion to other senses of income — income as cash receipts or income as compensation. If we take literally Simons’ specification that income is to be defined in terms of consumption and accumulation, then a deduction should be allowed whenever money is expended for anything other than personal consumption or accumulation. And that, arguably, is the intrinsic role of personal deductions.” *Id.* at 325.

11. *Id.*

12. *Id.* at 315.

13. Andrews, *supra* note 1, at 375.

14. *Id.* at 337.

15. *Id.* at 312.

16. See *infra* Chapter V.

provide us with a coherent and consistent doctrine. In order to maintain a comprehensive tax base, we should allow deductions that do not ex ante disregard¹⁷ the income production side of the economic equation. Since Income equals Consumption plus Savings, Andrews shifts the focus to Consumption, which by a simple arithmetic equals Income minus Savings.¹⁸ Prioritizing income over consumption and savings has no relevance in Andrews' work. To achieve a more coherent tax system, I would limit Andrews' determination that "deduction should be allowed whenever money is expended for anything other than *personal* consumption or accumulation"¹⁹ by adding "and anything related ex ante to income production."

The methodology of this Article is to examine whether those expenses that have a normative aspect of altruism, such as dependent care expenses or charitable contributions, fall in line with the three goals of taxation: revenue raising, regulatory, and redistributive goals. Only expenses that serve all three purposes help maintain a coherent tax system. A comparison of the two types of expenses shows that by virtue of an expense's normative aspect, both expenses promote redistribution and regulatory objectives. The discussion hitherto is analogous to Andrews' argument. But the difference occurs when we refer to the first objective that requires us to tackle the deduction issue from both sides of the equation – use and source. A *mixed expense* comprising an altruistic normative component, such as child or dependent care, is one that connects the revenue side to its uses and weighs the use and source sides equally. Conversely, other normative expenses that are not prerequisites for income production should not be deductible. The ex ante and ex post discussion is a fundamental difference between these two normative expenses, which disregards Andrews' view. This link between the income and its uses promotes the three goals of taxation concurrently, making for a more coherent tax system.

The Article is comprised of seven chapters. Chapter I introduces the practical law concerning the allowable deductions and the definitions of mixed business and personal expenses. In Chapter II, I briefly examine the meaning of income. Chapter III focuses on the law applicable to the two expenses at stake: charitable contributions and child-care expenses. Chapter IV briefly reviews the literature on both ex-

17. Andrews does not completely disregard sources, but since he considers sources equal to uses he focuses on the latter. See Andrews, *supra* note 1, at 375; see generally Edward J. McCaffery, *Tax's Empire*, 85 GEO. L.J. 71, 79 (1996).

18. McCaffery, *supra* note 17, at 80.

19. Andrews, *supra* note 1, at 325 (emphasis added).

penses. In Chapter V, I elaborate on the three goals of taxation and the need for a coherent tax system. Chapter VI characterizes the expenses at stake: their common altruistic aspects and the important distinctions between them. Finally, Chapter VII analyses those expenses according to the tax goals while keeping their distinctive aspects in mind. I end this Article with some conclusions.

I. ALLOWABLE DEDUCTION AND THE PROBLEM OF MIXED BUSINESS AND PERSONAL EXPENSES

A. *Allowable Deductions: Definition*

Every business has to pay taxes on its net income, i.e., that remaining after deducting allowable expenses from its revenue. In many instances, it is clear which expenses should be deducted. For example, if the business at stake is a shoe workshop, it is clear under I.R.C. § 162 that raw materials, electricity bills, and salaries are deductible since they are “ordinary and necessary expenses paid or incurred during the taxable year in carrying on”²⁰ the shoe business. This is based on the essential principle that deductible expenses are related to the taxable activity.²¹ Thus, the expense should be characterized as both “ordinary and necessary.” Treasury Regulation 1.212-1(d) defines “ordinary and necessary” expenses as “reasonable in amount and [bearing] a reasonable and proximate relation to the production or collection of taxable income.”²² Courts have developed a more accurate definition than the statutory terminology:²³ “An ‘ordinary’ expense is one that is ‘normal, usual or customary . . .’”²⁴ whereas necessary is interpreted by courts as “appropriate and helpful.”²⁵

B. *Mixed Business and Personal Expenses*

When the expense is considered private it is not deductible. Section 262(a) specifically disallows deductions for “personal, living, or family expenses.”²⁶ A purely private expense which does not contribute to

20. I.R.C. § 162(a) (Westlaw through Pub. L. No. 114-254) (effective Dec. 19, 2014).

21. For a comparative analysis see, for example, HUGH J. AULT & BRIAN J. ARNOLD, *COMPARATIVE INCOME TAXATION: A STRUCTURAL ANALYSIS* 249 (2010) and Joseph A. Pechman & Gary V. Engelhardt, *The Income Tax Treatment of the Family: An International Perspective*, 43 NAT'L TAX J. 1 (1990).

22. Treas. Reg. § 1.212-1(d) (as amended in 1975).

23. See, e.g., Melinda L. Reynolds, *Redlark v. Commissioner: A “Bird in the Hand” for Non-Corporate Taxpayers?*, 47 CASE W. RES. L. REV. 751, 755 (1997).

24. *Curcio v. Comm’r*, 689 F.3d 217, 223 (2d Cir. 2012) (citing *Deputy v. Du Pont*, 308 U.S. 488, 488 (1940)).

25. *Welch v. Helvering*, 290 U.S. 111, 113 (1933).

26. I.R.C. § 262(a) (Westlaw through Pub. L. No. 114-254).

income production and its deduction is prohibited would be, for example, a dentist, who works outside his home, buys flowers to decorate his private living room. The rationale is that it does not promote the progressivity of tax, erodes the tax base, and is inequitable.²⁷

Sometimes expenses have a mixed character, partly personal and partly income-producing. To put it somewhat differently, they carry both an “income-product[ing] and a consumption dimension[s].”²⁸ The distinction between personal and business expenses is not always clear, of course. A common example is travelling expenses as travel may be significantly work-related and at the same time also produces some self-benefits. Another example is a loan where 70% is used for one’s business and 30% is spent on a family vacation.²⁹ In this case, the taxpayer may deduct 70% of the interest paid for his business but the remaining 30% may not be deducted. Further, a dentist who buys the National Geographic journal for his personal use and subsequently places it in his clinic’s waiting room, is another example of a mixed expense.³⁰

Each country has developed different rules in this matter.³¹ In Germany, for example, mixed business expenses are not deductible unless explicitly considered deductible by law.³² The rationale underlying this prohibition is based on tax equity principles.³³ Some special private expenses (Sonderausgaben)³⁴ such as alimony payments and church tax payments or some specific extraordinary expenses (außergewöhnliche Belastungen)³⁵ are allowed.³⁶ Note, the extraordinary expenses are private expenses that the taxpayer is either legally, factually, or morally unable to avoid.³⁷

The separation between business and private expenses is based on the obsolete “separate spheres theory” developed in the nineteenth

27. Jeffrey H. Kahn, *Personal Deductions - A Tax “Ideal” or Just Another “Deal”?*, 2002 L. REV. MICH. ST. U. DET. C.L. 1, 3-4.

28. See AULT & ARNOLD, *supra* note 21, at 250.

29. IRS, DEPT. TREASURY, PUBLICATION 535 BUSINESS EXPENSES (2017), <https://www.irs.gov/pub/irs-pdf/p535.pdf>.

30. See Boris I. Bittker, *A “Comprehensive Tax Base” as a Goal of Income Tax Reform*, 80 HARV. L. REV. 925, 952 (1976).

31. AULT & ARNOLD, *supra* note 21, at 250.

32. *Id.*

33. *Id.*

34. Einkommensteuergesetz [EStG] [Income Tax Law], Oct. 8, 2009, BGBl. I at 3366, § 10-10i (Ger.).

35. *Id.* § 33, 33a.

36. AULT & ARNOLD, *supra* note 21, at 74.

37. EStG [Income Tax Law], § 33(2).

century.³⁸ This theory distinguishes between two separate spheres: male and female. The idea behind this separation is that men belong to the market, or public sphere, and women belong to the family-private sphere.³⁹ As opposed to the family sphere, the market is considered productive.⁴⁰ The related dichotomy between business and private expenses is thus obsolete and inconclusive, and it must, therefore, be reviewed and reformed.

However, what if the expense is not merely economic, but involves a normative aspect or has some private component that is not merely “personal consumption,” as in Andrews’ terminology, but has normative value? Imagine that the shoe workshop employs disabled persons and pays them a salary that is not commensurate with their actual productivity out of charity. Or assume a somewhat different example, where a self-employed person employs a nurse to care for a sick relative in order to be able to go on working and producing higher income. Sometimes a normative expense takes a different form, as argued below, where for example, the self-employed businessman donates some money to charity.

This Article focuses on two normative expenses: child-care, and also similarly dependent care, and charitable contributions.

II. WHAT IS INCOME?

Following Andrews,⁴¹ prior to discussing allowable deductions one must first understand the economic definition of income. The traditional Schanz-Haig-Simons formulation states that Income equals the sum of Consumption and Change of Savings in a certain period, usually, a calendar year. This formulation applies a comprehensive tax base since it measures the growth in individual wealth within the calendar year. It implies that expenses incurred to produce income can be deducted to obtain the net income. Taxation is levied on net income and not on gross income. Thus, revenue-raising income taxation taxes the net income by including all gross income and “deducting all the expenditures associated with the production of that income.”⁴²

38. Assaf Likhovski, *Chasing Ghosts: On Writing Cultural Histories of Tax Law*, 1 U.C. IRVINE L. REV. 843, 847 (2011).

39. For example, the private sphere would include child raising and domestic activities. See e.g., Frances Olsen, *The Family and the Market: A Study of Ideology and Legal Reform*, 96 HARV. L. REV. 1497, 1498-99 (1983).

40. *Id.* at 1498, 1500-01.

41. See e.g., Andrews, *supra* note 1, at 328.

42. Stanley S. Surrey & Paul R. McDaniel, *The Tax Expenditure Concept and the Budget Reform Act of 1974*, 17 B.C.L. REV. 679, 683-84 (1976).

Income may have other definitions. It can be a recurring cash receipt from a certain source, compensation for use of capital or net accretion from whatever source.⁴³ Although it serves as an anchor in many tax laws, even if not adopted per se, the economic definition involves some practical and perhaps theoretical quandaries. For instance, some scholars criticize it for its ambiguous terminology and for ignoring distributive goals.⁴⁴

III. APPLICABLE LAW: TAXATION OF CHARITABLE CONTRIBUTIONS AND DEPENDENT CARE IN US

Charitable contribution and dependent care are private expenses which, according to I.R.C. § 262(a), are not deductible. Though, American tax law treats those payments differently. Under § 170, any corporation or individual may deduct donations to qualified charities, subject to some restrictions. For example, the allowed deduction amount is restricted,⁴⁵ in addition to some restrictions concerning the type of charity and property donated.

As early as 1939, in *Smith v. Commissioner*,⁴⁶ child-care payment was considered by courts as a private expense.⁴⁷ In this case, the taxpayers, working parents, requested a deduction for employing a nursemaid to care for their child while they were working. The court did not accept the “but for” test⁴⁸ and held that daycare payments are not deductible since they are mainly “personal in their nature.”⁴⁹ This old verdict was reinforced also with regard to dependent care expenses in

43. See Andrews, *supra* note 1, at 318-20.

44. See e.g., Dodge, Joseph M., *Deconstructing the Haig-Simons Income Tax and Reconstructing It as Objective Ability-to-Pay ‘Cash Income’ Tax 1* (Fla St. Pub. Law & Legal Theory, Research Paper Series, Paper No. 633, 2013), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2245818## (Click on “Download This Paper” icon for access to the working paper).

45. In general, any individual is allowed to deduct 50% of his adjusted gross income. See I.R.C. § 170(b)(1)(A) (2012). But sometimes the amount of deduction is lower. See e.g., I.R.C. § 170(b)(1)(B)-(D). A corporation, however, may deduct no more than 10% of its taxable income. See I.R.C. § 170(b)(2)(A).

46. *Smith v. Comm’r*, 40 B.T.A. 1038, 1039-40 (1939).

47. For historical legislation developments on childcare tax treatment see Wendy Gerzog Shaller, *Limit Deductions for Mixed Personal/Business Expenses: Curb Current Abuses and Restore Some Progressivity into the Tax Code*, 41 *CATH. U. L. REV.* 581, 606-12 (1992).

48. The taxpayer in *Smith* case claimed that “but for” the nanny the wife could not go to work and produce income: “Petitioners would have us apply the ‘but for’ test. They propose that but for the nurses the wife could not leave her child; but for the freedom so secured she could not pursue her gainful labors; and but for them there would be no income and no tax.” *Smith*, 40 B.T.A. at 1038.

49. *Id.* at 1039. Nevertheless, in Rev. Rul. 73-348 it was ruled that when the corporation pays for a daycare center, these expenses “are directly related to its business and are, accordingly, ordinary and necessary business expenses deductible under section 162 of the Code.” Rev. Rul. 73-348, 1973-2 C.B. 31.

the *Kuntz v. Commissioner*.⁵⁰ In this case, a husband operated a business and hired a person who both worked for the business from home, but also served as a caregiver for his diseased wife who needed “someone to be with her at all times.”⁵¹ Based on *Smith*, the court held that the caregiver expenses were not deductible even though they enabled the husband to work outside the home.

Although courts do not consider child or dependent care as a deductible expense, the law grants a credit for the parent or relative’s working activity.⁵² Section 21 grants a progressive credit for the working individual for his dependent,⁵³ spouse,⁵⁴ or child up to age 13.⁵⁵ This should not be confused with the \$1000 child tax credit, however, which is granted to parents whether they work or not,⁵⁶ for any qualifying child under age 17.⁵⁷

IV. THE PERSONAL DEDUCTIONS DEBATE

Because of the accumulated tax reduction caused by personal expenses, such as child or dependent care and charity contributions, scholars have long disputed the deductibility of those expenses.⁵⁸ The starting point of this discussion is the comprehensive tax base referred to above.⁵⁹ In what follows, I introduce some important works on the personal deductions dilemma. Stanley S. Surrey, who first conceived the tax expenditure notion, treats personal deductions as a deviation from the tax base. He thus considers personal deductions tax benefits equivalent to direct expenditures.⁶⁰

50. *Kuntz v. Comm’r*, T.C. 2011-52.

51. *Id.*

52. *Id.*

53. *Id.* I.R.C. § 21(b)(1)(B) (2012).

54. *Id.* § 21(b)(1)(C).

55. *Id.* § 21(b)(1)(A). Some scholars criticize this tax credit since it is not a full credit but still incentivizes married women to stay at home rather than advance their professional career. See e.g., Grace Blumberg, *Sexism in the Code: A Comparative Study of Income Taxation of Working Wives and Mothers*, 21 *BUFF. L. REV.* 49 (1971–1972).

56. I.R.C. § 24(a). This credit is also a refundable one to help not just middle-class but low-income families. See I.R.C. § 24(d); see also DANIEL Q. POSIN & DONALD B. TOBIN, *PRINCIPLES OF FEDERAL INCOME TAXATION* 641 (2005).

57. See I.R.C. § 24(c). There is also an adoption credit, see *id.* § 23, to parents who have finalized the adoption process, designed to refund adoption costs, including fees and legal costs. *Id.* §23(d)(1).

58. Thomas D. Griffith, *Theories of Personal Deductions in the Income Tax*, 40 *HASTINGS L.J.* 343, 343 (1989).

59. *Supra* Chapter II.

60. See Stanley S. Surrey, *Tax Incentives as a Device for Implementing Government Policy: A Comparison with Direct Government Expenditures*, 83 *HARV. L. REV.* 705 (1970); Stanley S. Surrey, *Tax Incentives – Conceptual Criteria for Identification and Comparison with Direct Government Expenditures*, in *TAX INCENTIVES – SYMPOSIUM CONDUCTED BY TAX INSTITUTE OF*

Andrews⁶¹ takes a somewhat different approach and recognizes the existence of an ideal tax base. He examines the ideal personal income tax with regard to the taxation of personal deductions. His starting point is that income should be defined by its uses and not by its sources: “an ideal personal income tax is one in which tax burdens are accurately apportioned to a taxpayer’s aggregate personal consumption and accumulation of real goods and services and claims thereto — the uses to which income is typically put rather than the sources from which it is derived.”⁶² Thus, taxpayers who use their funds as contributions to charity should be regarded as if they did not own that money. However, he rationalizes the deduction of medical expenses and charitable contributions differently. For example, his main justification for allowing medical expense deductions and excluding them from the tax base is largely distributional.⁶³

Mark G. Kelman⁶⁴ challenges Andrews’ use-oriented deduction concept and bases his theory on net income as the ideal tax base. If the ideal tax base should be measured by relative earnings capacity and if individuals choose not to realize their potential earnings capacity,⁶⁵ it is, in principle, inequitable to allow the deduction of medical and charitable expenses. Kelman and Stanley A. Koppelman⁶⁶ share a similar view. Koppelman argues that since income means the power to consume most personal expenses, which are not related to income production, should not be deductible.⁶⁷ Johnny Rex Buckles, similar

AMERICA, NOVEMBER 20-21, 1969 (1971); STANLEY S. SURREY, *PATHWAYS TO TAX REFORM – THE CONCEPT OF TAX EXPENDITURES* (1973); STANLEY S. SURREY & PAUL R. MCDANIEL, *TAX EXPENDITURES* (1985).

61. Andrews, *supra* note 1.

62. *Id.* at 313.

63. Andrews’ distributional justification is as follows:

What is important about money income for tax purposes, Simons’ formulation indicates, is not so much that it reflects one’s participation in the production sector, but that it determines his participation in the distribution sector. And when we say income is to be taxed in whatever form received, it is the latter relation, not the former, that we should seek to refine. If a taxpayer’s contributions in the production sector are more or less than what he is paid, it really does not matter; he should be taxed on what he is paid anyway. But if a person’s money income fails to give a fair general measure of his participation in the distribution of real goods and services, then we must consider how great the disparity is and whether there are practical ways to adjust for it. Hard policy problems do not have simple answers.

Andrews, *supra* note 1, at 324-25.

64. See Mark G. Kelman, *Personal Deductions Revisited: Why They Fit Poorly in an “Ideal” Income Tax and Why They Fit Worse in a Far From Ideal World*, 31 *STAN. L. REV.* 831 (1979).

65. *Id.* at 832-33.

66. See Stanley A. Koppelman, *Personal Deductions Under an Ideal Income Tax*, 43 *TAX L. REV.* 679 (1988).

67. *Id.*

to other tax-base scholars, justifies the charitable contribution deductions since he regards it as “community income” rather than an “individual income.”⁶⁸ With regard to personal deductions, Boris I. Bittker⁶⁹ criticizes the supporters of the all-inclusive tax base as inconsistent. Some of these scholars agree to exclude some personal expenditure from gross income and to deviate from the Haig-Simons formula. Bittker believes that their reasoning is similar to the rationale given in support of all other “exceptions,” or “preferences,” in the law and that each provision should be examined separately.

In a similar vein, Thomas D. Griffith⁷⁰ criticizes Surrey’s, Andrews’ and Kelman’s models, since they lack “a coherent normative principle.”⁷¹ He addresses personal deductions by examining two distinct distributive justice principles: a utilitarian one and a variant of Rawlsian maximin principles.⁷² He concludes that under some simplifications, either medical deduction or credit, can increase social welfare both under utilitarian and leximin theories.

Jeffrey H. Kahn⁷³ examines four personal nonbusiness deductions officially – and in his opinion, wrongly – classified as tax expenditures: medical expenses, theft and casualty losses, charitable contributions, and the interest deduction for mortgages on a personal residence. He reviews both Andrews’ and Kelman’s papers on personal deductions and supports the former’s conclusion with a different rationalization by concluding that since those deductions fall in line with progressive taxation, they should not be characterized as tax expenditures.⁷⁴

Since two specific “normative” personal deductions are examined here, it will be useful to review the particular attitudes towards those expenses in the literature and not just as part of “personal expenses.” Charitable deductions have received broad support since their enactment in 1917.⁷⁵ The main three justifications are the measurement,

68. Johnny Rex Buckles, *The Community Income Theory of the Charitable Contributions Deduction*, 80 IND. L.J. 947, 971-72 (2005).

69. See Bittker, *supra* note 30, at 950-54.

70. See Griffith, *supra* note 58, at 343-45.

71. *Id.*

72. *Id.* at 345.

73. Kahn, *supra* note 27, at 2.

74. *Id.* at 6-7. For mixed business and private expenses see also Shaller, *supra* note 47. The author analyzes the legal treatment of the following personal expenses: home office deduction, the deduction allowed for certain travel between home and work, the moving expense deduction, the exclusion for certain fringe benefits, the deductions for business meals and entertainment, and childcare credit. The author suggests some specific amendments in each personal expense to accomplish equality in taxation.

75. See e.g., Mark P. Gergen, *The Case for a Charitable Contributions Deduction*, 74 VA. L. REV. 1393 (1988). Gergen differentiates between various kinds of charitable contributions and examines them on both efficiency and equity grounds. Not all donations can be justified as pro-

subsidy, and choice theories.⁷⁶ Andrews' measurement theory⁷⁷ focuses on the donor and his tax burden, emphasizing that he does not obtain any material benefit. The second – subsidy theory – treats charitable aid as public goods,⁷⁸ as it is seen to include the two main attributes of public goods: non-rivalry and non-excludability.⁷⁹ The basic idea is that charities offer free public goods to the donees.⁸⁰ However, while some charities, such as scientific research organizations, are almost pure public goods, others – such as museums where visitors can directly pay for their benefit – are less so.⁸¹ Be that as it may, if governments tax those public goods, this will cause underfunding.⁸² The third main justification for deducting charitable contributions is based on choice theory. Choice theory considers the choice granted to donors as valuable in itself.⁸³ Therefore, the charitable deduction is valuable, not just because of its public good merits, but also because it enables donors to decide which charity they wish to support.⁸⁴ The public choice mechanism facilitates the democratic process and treats taxpayers as voters and taxes as ballots.⁸⁵ In that respect “[t]he [charitable] tax deduction essentially casts the government as a financing partner, with taxpayer-donors serving as intermediaries or agents who choose the providers of, or indeed the very existence of, certain services.”⁸⁶ In this Article, I follow Andrews' measurement theory.

moting both efficiency and equity principles. For a more comprehensive discussion on this issue, see MATTHEW HARDING ET AL., *TAXING CHARITY – A LITERATURE REVIEW* (2011), <http://law.unimelb.edu.au/centres/cclsr/research/major-research-projects/defining-taxing-and-regulating-the-not-for-profit-sector-in-australia-law-and-policy-for-the-21st-century/nfp-publications>.

76. See Grace Soyon Lee, *Mitigating the Effects of an Economic Downturn on Charitable Contributions: Facing the Problem and Contemplating Solutions*, 22 *CORNELL J.L. & PUB. POL'Y* 589, 601 (2013).

77. See Andrews, *supra* note 1.

78. See e.g., Gergen, *supra* note 75, at 1394 (aiming to answer the following important questions: why should charitable contribution be deducted and exactly what payments and to which organizations?). For the recognition of contribution deductions Gergen supports both the subsidiary and the equity theories. *Id.* Gergen believes that “[m]uch of Andrew’s argument for allowing deductions for contributions to charity shares a premise with the argument for a deduction as a subsidy: the fact that charities provide collective goods.” *Id.* at 1421.

79. *Id.* at 1397.

80. *Id.*

81. *Id.* at 1397-98.

82. *Id.* at 1398.

83. See Boris I. Bittker, *Charitable Contributions: Tax Deductions or Matching Grants?*, 28 *TAX L. REV.* 37, 61 (1972) who claims “that the deduction can be viewed as a mechanism for permitting the taxpayer to direct, within modest limits, the social functions to be supported by his tax payments.” See also Lee, *supra* note 76, at 606.

84. Saul Levmore, *Taxes as Ballots*, 65 *U. CHI. L. REV.* 387, 388 (1998).

85. *Id.*

86. *Id.*

The debate around child-care deductions is also long lasting.⁸⁷ The main criticism against the legal treatment of childcare is that it discourages mainly married women with children from working.⁸⁸ When housewives stay at home to raise their kids, a non-pecuniary income is produced, which is untaxed. This untaxed imputed income induces many women to stay at home rather than be productive in the traditional sense by working outside the home.⁸⁹

V. TAX GOALS AND TAX SYSTEM HARMONIZATION

The question whether to deduct a certain amount is central to the discussion of “ideal income tax.” This discussion clarifies that taxation is not merely “revenue raising.”⁹⁰ As early as 1934, Robert E. Cushman alleged that the federal income tax achieves both social and economic goals⁹¹ and that “taxation need not be for revenue only.”⁹² More recently, Reuven S. Avi-Yonah claimed that tax goals are threefold: the first, and obvious, goal is raising revenue to finance public goods, but there are two more controversial⁹³ goals: redistributive and regulatory.⁹⁴ The threefold tax goals will be the premise of the following discussion.⁹⁵

The three objectives of taxation are not necessarily compatible. For instance, “revenue-raising” is not correlated with “revenue-affecting.”⁹⁶ For instance, in order to properly tax income, the law allows deducting “ordinary and necessary expenses,”⁹⁷ such as raw materials

87. On its legislative history see, Shaller, *supra* note 47, at 606–12.

88. See Blumberg, *supra* note 55.

89. See Richard A. Posner, *Taxation by Regulation*, 2 BELL J. ECON. & MGMT. SCI. 22, 42 (1971).

90. See Levmore’s classification between “revenue-raising” and “revenue-affecting.” Levmore, *supra* note 84, at 387 n.1.

91. Robert E. Cushman, *Social and Economic Control through Federal Taxation*, 18 MINN. L. REV. 759, 762 (1934).

92. *Id.* at 764. For the purposes of tax goals see also 2 ROYAL COMMISSION ON TAXATION, REPORT OF THE ROYAL COMMISSION ON TAXATION: The Use of the Tax System to Achieve Economic and Social Objectives 1-2 (1996).

93. See LIAM MURPHY & THOMAS NAGEL, THE MYTH OF OWNERSHIP 76–77 (2002). Murphy & Nagel believe that taxation has mainly two goals – revenue raising and redistribution.

94. Reuven S. Avi-Yonah, *The Three Goals of Taxation*, 60 TAX L. REV. 1, 3 (2006).

95. Posner claims:

Taxation in common parlance refers to the use of the powers of the state to extract money from its subjects in order (1) to defray the cost of services that the politically dominant elements of the state wish to provide and that the market would not provide in the desired quantity and at the desired price, or (2) to transfer money from one group to another, or (3), often, to do both.

Posner, *supra* note 89, at 28-29.

96. See Levmore, *supra* note 84, at 387 n.1.

97. I.R.C. § 162(a) (2012); see *supra* Chapter I.A.

in the shoe business example above.⁹⁸ This deduction has nothing to do with the regulatory goal of taxation. Nevertheless, in this Article, I claim that there are few expenses that promote the triple goals of taxation, and that we should support tax deductions that meet all three.⁹⁹ Those deductions support an ideal coherent and comprehensive tax system. When some deductions support just one, which is not revenue raising, or two goals, however, our tax system is incoherent and disharmonic.

This discussion bears some similarities to the theory of interpretation.¹⁰⁰ Although, a harmonic system is not a primary goal of a jurisdiction, both legislators and judges endeavor to attain such a system.¹⁰¹ Interpretation theory treats the statute as “a living organism,”¹⁰² meaning that legislative interpretation should strive for harmony between a particular statute and the entire legal system. Similarly, even a particular legal provision is “a living organism” in a dynamic environment, and its adjacent surroundings is the law itself. Before striving to achieve both harmony and consistency at the macro level, the entire jurisdiction should strive for harmony at the micro level between the various provisions of the law itself and specifically its underlying rationales. If there is no harmony at the micro level, it cannot be reached at the macro level (a bottom-up argument). If the law is designed to promote the fundamental principles of the law system, then its components, the statutory provisions, also have to be harmonized. In particular, laws must not contradict each other, let alone various provisions in the same law, or else normative harmony would remain unattainable.¹⁰³

Since the federal tax code contains thousands of legal provisions, many of them are inconsistent and do not fully serve the three tax goals. If one aims at attaining legislative harmony, the interpreter should endeavor to settle legal disagreements in a way that falls in line

98. See *supra* Chapter I.A.

99. See also Limor Riza, ‘I Have Nourished and Brought Up a Child, and the State Has Rebelled Against Me’ – Recognition of Child Care Expenses as a Mixed Personal/Business Deduction Unifying Tax Goals 245, in *ESSAYS IN TAX LAW IN HONOR OF ARIE LAPIDOT* (David Gliksberg ed., 2015) (Hebrew).

100. Here, I base my discussion mainly on the extensive research of Prof. Aharon Barak. Another justification can be found in the coherence theory. See Robert Alexy & Aleksander Peczenik, *The Concept of Coherence and Its Significance for Discursive Rationality*, 3 *RATIO JURIS* 130 (1990).

101. For the discussion on harmony see, for example, Aharon Barak, *A Judge on Judging: The Role of a Supreme Court in a Democracy*, 116 *HARV. L.REV.* 19, 76-77, 91, 144 (2002). See also McCaffery, *supra* note 17 (supporting a coherent tax interpretation).

102. See Barak, *id.* at 28.

103. See *id.* at 35.

with all three tax goals. This interpretation may also contribute to answering the fundamental question: what is income, i.e., whether the Haig-Simons formula is indeed its proper measure.

VI. CLASSIFYING PERSONAL EXPENSES

A. *Altruism*

After understanding that tax provisions should fall in line with the three goals of taxation, it is necessary to classify the private expenses at stake. This examination is required to determine whether those expenses fall in line with the three tax goals or whether their deduction maintains a coherent system.

It should be noted that not every private expense is a normative one with an altruistic component, as seen in the dentist-flower example above.¹⁰⁴ The common denominator of both types of expenses discussed here is altruism – helping a person other than the taxpayer.

There are different kinds of altruism, and the term evades a unified definition. One distinction that may be directly relevant to the discussion on donations is made by Amartya K. Sen. Sen distinguishes between donation or behavior motivated by commitment and those motivated by sympathy.¹⁰⁵ But as Mark P. Gergen comments, “[w]e cannot say with confidence, for example, whether a parent aids a child for reasons of pleasure or duty.”¹⁰⁶

Some scholars focus on the sacrifice and help aspects of altruism.¹⁰⁷ Others concentrate on its goal: the altruist is a person who wishes to increase the other’s welfare.¹⁰⁸ Still others rely on economic theories that focus on the rationality of the action and the utility derived from it.¹⁰⁹

104. See *supra* Chapter I.B.

105. Amartya K. Sen, *Rational Fools: A Critique of the Behavioral Foundations of Economic Theory*, 6 PHIL. & PUB. AFF. 317, 326-29 (1977). Sen stated,

It can be argued that behavior based on sympathy is in an important sense egoistic, for one is oneself pleased at others’ pleasure and pained at others’ pain, and the pursuit of one’s own utility may thus be helped by sympathetic action. It is action based on commitment rather than sympathy which would be non-egoistic in this sense.

Id. at 326.

106. Gergen, *supra* note 75, at 1433.

107. See e.g., Jacqueline S. Mattis et al., *The Social Production of Altruism: Motivations for Caring Action in a Low-Income Urban Community*, 43 AM. J. COMMUNITY PSYCHOL. 71, 72 (2009) (citing Samuel P. Oliner, *Extraordinary Acts of Ordinary People: Faces of Heroism and Altruism*, in ALTRUISM AND ALTRUISTIC LOVE: SCIENCE, PHILOSOPHY, AND RELIGION IN DIALOGUE 123 (Stephen G. Post et al. eds., 2002)).

108. See *id.* (citing C. Daniel Batson, *Why Act for the Public Good? Four Answers*, 20 PERSONALITY & SOC. PSYCHOL. BULL. 603 (1994)).

109. See ROBERT M. AXELROD, *THE EVOLUTION OF CORPORATION* 3-24 (1984).

The literature on the motives for helping others is irrelevant, and it is only the consequences that matter: did the taxpayer's action actually benefit the other? Helping the other can increase one's utility. However, since this utility is impractical to measure,¹¹⁰ the focus of this section will be on the outcome itself. Clearly, the two types of expenses in question are altruistic in the sense that they meet the two requirements of this definition. First, the altruistic act increases the other's welfare, regardless of its motive. Second, it is considered a valuable act. This definition is important to exclude immoral or illegal acts.

This definition implies that the "other" is any person besides the taxpayer. If one donates money to a third party, this is clearly an altruistic act. A question may arise about the consequences of such a donation if the beneficiary is a relative. Donations to a relative may be treated as dependent care. Under § 170(g)(3),¹¹¹ a relative is defined as "an individual who, with respect to the taxpayer, bears any of the relationships described in subparagraphs (A) through (G) of section 152(d)(2)" – namely a child, a sibling or a parent. But as stated above, the "other" is anyone, also a relative, other than the taxpayer. Accordingly, while some scholars who restrict altruism to almsgiving exclude children from the "other,"¹¹² other theories consider the act of helping the child as altruistic.¹¹³ As stated above, the motive for the "contribution" is irrelevant – only the outcome is relevant to the analysis.

In sum, the main characteristic of the "private" expenses in question is that they contain a normative aspect of altruism. The requirement is that the expense was carried out to increase the other's welfare whereas the "other" is any person except for the taxpayer, the income-producer.

110. See, e.g., Gergen, *supra* note 75, at 1423-28 (discussing donor's satisfaction). And see the claim that "[a]lthough it once had some currency, few scholars today think that we should be concerned with subjective satisfaction in measuring income." *Id.* at 1427 (internal citations omitted).

111. With regard to "amounts paid to maintain certain students as members of taxpayer's household." I.R.C. § 170(g) (Westlaw through Pub. L. No. 114-254) (effective Dec. 18, 2015).

112. Elias L. Khalil, *Adam Smith and Three Theories of Altruism*, 67 LOUVAIN ECON. REV. 421 (2001).

113. This perspective relies on evolutionary biology and rational economy theories. Evolutionary biology considers altruism as gene perpetuation thus a child is naturally the "other." Rational economy may identify one's utility with the other's, but still the other is separate from the altruist. For evolutionary biology theory see, for example, RICHARD DAWKINS, *THE SELFISH GENE* (1976); for rational economy see, for example, Gary S. Becker, *A Theory of Social Interactions*, 82 J. POL. ECON. 1063 (1974) and Gary S. Becker & Robert J. Barro, *Altruism and the Economic Theory of Fertility*, 12 POPULATION & DEV. REV. 69 (1986).

B. *Altruistic Act towards Related or Unrelated Party*

The various altruistic expenses can be differentiated by the distance of the relation with the “other.” This distinction is related to two linked sub-distinctions: whether this expense is forced or optional, i.e., the choice characteristic, and whether the expense is “ordinary and necessary,” i.e., the mixed business characteristic.¹¹⁴ When a taxpayer transfers money, not in an arm’s length transaction, in order to nurse her child and to be able to continue to work, the expense is a coerced one. The working mother has no other alternative other than to pay this expense, even if the choice to go to work is voluntary. This is not true with regard to charity donation. The donor is not coerced to make the altruistic act to the unrelated party. In the former case, the altruistic act is directly related to the income production and thus carries a mixed business characteristic, while the latter has nothing to do with it. These distinctions will prove vitally important in examining the differences between the two types of expenses in question in Chapter VII.

VII. THE NORMATIVE ASPECTS OF TAX GOALS

A. *The Regulatory Aspect*

The normative aspects of tax goals are embodied in the redistributive and regulatory aspects of taxation. Taxation can enhance desirable behavior by promoting an economic, social or national goal by virtue of its regulatory mechanism. Surrey,¹¹⁵ for example, demonstrates how tax policy is used as a tool to regulate and favor certain activities or groups. According to Surrey and Paul R. McDaniel, all deviations from “normal income tax” can be considered as tax expenditures or “special preferences found in every income tax. . . . often called tax incentives or tax subsidies, [which] are departures from the normal tax structure and are designed to favor a particular industry, activity, or class of persons.”¹¹⁶ They may be structured in different forms, such as deductions, credit, and exemptions,¹¹⁷ but their common denominator is that they form a “‘normative’ income tax structure.”¹¹⁸

A common example of using tax as a means to regulate an activity is the Pigovian tax, which deals with negative externalities and aims at

114. See also Riza, *supra* note 99, at 261-266.

115. See generally Surrey *supra* note 60.

116. Surrey & McDaniel, *supra* note 42, at 680.

117. *Id.*

118. *Id.*

inducing tortfeasors to internalize the negative private costs, in order to produce efficiently. Naturally, there is disagreement among scholars regarding whether taxation should serve as a regulatory mechanism¹¹⁹ and whether the legislator should use tax expenditure rather than direct spending.¹²⁰

Both types of expenses in question here can be justified on regulatory grounds – both from social and economic perspectives. The first type of expenses is donations to charities. These donations are the bread and butter of charities – an umbrella term, used here, to apply to what is variously called the non-profit sector, social economy, or the third sector. All these terms define different aspects: the “non-profit sector” emphasizes mainly the lack of profit redistribution; the term “social economy” highlights its socioeconomic aspect; whereas the “third sector” refers to its position between the market and the government.¹²¹ Non-profit organizations (NPOs) are not a new phenomenon but their numbers and global impact have significantly increased in the last decades.¹²² If one accepts the importance of NPOs and acknowledges their contribution both to “social cohesion”¹²³ and market efficiency,¹²⁴ then, naturally, a tax relief for donations should be supported on regulatory grounds.

The same applies to the other type of expense, again relying on both economic and social grounds. In many societies, mothers are the parents who stay at home to raise the children and consequently delay their career progress for several years. Now, if women do not get a tax relief for this non-pecuniary work, the family unit usually makes a cost-benefit analysis, calculating the costs of hiring a nanny versus the mother’s income. In many cases deciding that the mother should stay at home and raise the children is made simply because it is more economical, at least in the short run.¹²⁵ This is partly a result of not tax-

119. *Id.*

120. Other scholars believe that in order to examine whether a certain government policy should be implemented through taxation or not, we should shift from tax to institutional discourse. See David A. Weisbach & Jacob Nussim, *The Integration of Tax and Spending Programs*, 113 *YALE L.J.* 955 (2004).

121. *ORG. FOR ECON. COOPERATION AND DEV. (OECD), THE NON-PROFIT SECTOR IN A CHANGING ECONOMY* 10, 12 (2003), http://www.keepeek.com/Digital-Asset-Management/oced/urban-rural-and-regional-development/the-non-profit-sector-in-a-changing-economy_9789264199545-en#page1.

122. For the reasons of their popularity and significance see *id.* at 10-14.

123. *Id.* at 47.

124. See the European experience supporting the social and efficiency grounds of NPOs. *Id.* at 47-51.

125. See *Baby Blues; A Juggler’s Guide to Having It All*, *ECONOMIST* (Nov. 26, 2011), <http://www.economist.com/node/21539925>. The article states,

ing an imputed income. Richard A. Posner nicely illustrates the economic problem of exempting the imputed income of such mothers:

[T]he exemption from income taxation of the real but not pecuniary income generated by housewives must cause a significant misallocation of resources by inducing many women to stay at home who would be more productive in other employments. The administrative costs of implementing a broader income concept would be so great, however, that this exemption is probably a permanent feature of income taxation.¹²⁶

If those women wish to return to work, they are at a certain disadvantage due to the delay in their career progress and are often required to compromise on a less desirable workplace. Moreover, by staying at home, they deny other people an employment opportunity, leaving potential nannies unemployed. In that respect, inducing women to continue working after giving birth is stimulation for the entire economy.¹²⁷

It is therefore quite straightforward that tax relief for daycare expenses is economically justified. In addition, there are perfectly good societal reasons for supporting it. From the parents' perspective, the benefits are clear-cut and relate mainly to the economic aspect and women autonomy to decide whether they prefer staying at home and raising their children or not. The law should provide women with the free choice to decide if they wish to work and should not interfere with such a private, autonomous decision. It is the child's perspective that requires elaboration here. The duty to support children is both moral and legal, based on the UN Convention on the Rights of the Child. Many nations have ratified this Convention and are bound by its content.¹²⁸ For our discussion, Article 18 is particularly relevant:

The OECD reckons that across its member countries the net average cost of child care after allowing for fees, cash benefits and tax concessions is 18% of the average wage, which makes children seem a bit of a luxury. Child-care arrangements are often a complicated patchwork quilt of paid help, family, friends and neighbours. In some countries . . . the combined effect of the cost of child care and the lack of tax concessions and benefits makes it unattractive for mothers of young children to work unless they are very well paid.

126. Posner, *supra* note 89, at 42.

127. This claim is relevant *mutatis mutandis* to dependent care expenses as well. Nevertheless, one possible claim against the recognition of dependent care deductions is that the dependents (i.e., people who became dependent during their adult life, that is not born with handicaps) could have saved for a rainy day so as not to become financially dependent on others. Recognizing dependent care deductions discourages people from saving for the future. This argument is inapplicable to the child care expense.

128. The US has signed but not yet ratified the Convention. See Status of United Nations Treaties UNITED NATIONS TREATY COLLECTION, https://treaties.un.org/Pages/Home.aspx?clang=_en (click on the "Depository" tab and select "Status of Treaties" from the drop down menu; then click on the "Title Search" tab; enter "Convention on the Rights of the Child in the search

[B]oth parents have common responsibilities for the upbringing and development of the child. Parents . . . have the primary responsibility for the upbringing and development of the child. The best interests of the child will be their basic concern. [Governments] shall render appropriate assistance to parents and legal guardians in the performance of their child-rearing responsibilities and shall ensure the development of institutions, facilities and services for the care of children.¹²⁹

In the United States, parents have the duty to support and take care of their children, but the scope of this duty varies between states.¹³⁰ Although this is not a social science paper, one can find support in social studies to examine whether it is better from a child's perspective to be raised by a nanny rather than by his mother. Naturally, there are various studies on the matter. One study carried out by the National Institute of Child Health and Human Development (NICHD) emphasizes that there is not any developmental difference between children who were exclusively cared for by their mothers and those who were cared for by others.¹³¹ Thus, the child-care expense can be justified mainly through the mothers' lens also on social grounds.

B. *The Redistributive Aspect*

The relationship between regulation and redistribution is explained by Posner, who argues, "[O]ne of the functions of regulation is to perform distributive and allocative chores usually associated with the taxing or financial branch of government."¹³² Although there are diverse perspectives on distributive justice (egalitarian, utilitarian, etc.), the discussion here will be limited to a somewhat circular argument and to Andrews' view.

It is indeed not consensual that taxation or other legal rules are suitable for achieving distributional goals.¹³³ Whatever position

field; the first result of the search will be a hyperlink to the convention status; then click on the first link; once on the page, scroll down to see entry "United States" in the table).

129. United Nations Convention on the Rights of the Child art. 18, June 26, 1945, 1577 U.N.T.S. 3.

130. For example, in NY the parents' duty ends when the child is 18 years old. *See* N.Y. DOM. REL. LAW art. 1, § 2 (McKinney 2016).

131. *See* NAT'L INST. OF CHILD HEALTH AND HUMAN DEV., U.S. DEP'T OF HEALTH AND HUMAN SERVS., THE NICHD STUDY OF EARLY CHILD CARE AND YOUTH DEVELOPMENT: FINDINGS FOR CHILDREN UP TO AGE 4½ YEARS (2006), http://www.nichd.nih.gov/publications/pubs/documents/secycd_06.pdf.

132. Posner, *supra* note 89, at 23.

133. *See, e.g.*, Jacob Nussim, *Redistribution Mechanisms*, 3 REV. L. & ECON. 323 (2007); *see also* Louis Kaplow & Steven Shavell, *Why the Legal System is Less Efficient than the Income Tax in Redistributing Income*, 23 J. LEGAL STUD. 667 (1994); Louis Kaplow & Steven Shavell, *Should Legal Rules Favor the Poor? Clarifying the Role of Legal Rules and the Income Tax in Redistrib-*

taken, for our purpose it is sufficient to accept that taxation has the power to serve as a distributive mechanism. The question of whether this is the best alternative for redistribution is beyond the scope of this paper.

A very simple definition of redistribution is the transfer of wealth from high net worth persons to others. The taxpayer or transferor gives part of his income to the transferee. Altruism, expressed in “almsgiving” terms, as discussed above, is a clear example of such redistribution. Child-care deduction naturally meets this simple definition of redistribution. Bear in mind, though, in that simple sense, charitable contributions do not always involve transfer from economically better off persons to worse off persons.¹³⁴ Only donations to people in need promote this simple idea of redistribution.

These two kinds of personal expenses are also in line with Andrews’ position that taxation should not focus to such an extent on the income and on the taxpayer’s “participation in the production sector,”¹³⁵ but rather on the “distribution sector,”¹³⁶ given that the tax system has a distributive goal.¹³⁷ Thus, the normative aspect of expenses, which are not for self-use, justifies their tax relief since they also promote distribution goals.

C. Revenue Raising for Public Goods

There is no doubt that the first goal of taxation is revenue-raising to finance public goods and services.¹³⁸ However, since Adam Smith, it is not unconditional. Over two hundred years ago, Adam Smith suggested four principles necessary for applying a good tax system. Those principles – still referred to as the canons of taxation – require that tax should be equal, certain, and efficient, and also take the tax-

uting Income, 29 J. LEGAL STUD. 821 (2000); A. MITCHELL POLINSKY, AN INTRODUCTION TO LAW AND ECONOMICS 119-127 (2nd ed. 1989).

134. See, e.g., Gergen, *supra* note 75, at 1398.

135. Andrews, *supra* note 1, at 324.

136. *Id.* Andrews continues: “[a]nd when we say income is to be taxed in whatever form received, it is the latter relation, not the former, that we should seek to refine.” *Id.* For an elaboration see *id.* at 327.

137. *Id.* at 326.

138. The neoclassical economic approach is that government intervention is needed in case of market failure. The classical public goods have two characteristics: non-rivalry and non-excludability. See, e.g., ROBERT S. PINDYCK & DANIEL RUBINFELD, MICROECONOMICS 644-49 (5th ed. 2001).

payers' convenience into account.¹³⁹ They are commonly accepted today and have since been developed further.¹⁴⁰

Equity, in particular, is a widely accepted principle although different scholars have conceptualized it differently.¹⁴¹ Two fundamental principles have been developed to evaluate equity: the benefit principle and the ability to pay principle.¹⁴² The benefit principle treats taxation as a price – taxpayers should pay taxes only on the benefits they derive from using public goods.¹⁴³ Ability to pay is the most established principle, both in theory and practice.¹⁴⁴ According to this principle, taxes should be levied in accordance with taxpayers' wellbeing. As a rule, a well-off taxpayer with a higher ability to pay should pay more taxes.

Ability to Pay and Expense Deductibility

By applying the ability-to-pay principle of equity, both taxpayers – the one that contributes to charity and the one who pays for childcare – are less able to pay than other taxpayers who are not required to spend these amounts, following Andrews' line of thinking.¹⁴⁵ If we accept the Haig-Simons formula, how should those expenses be treated? Should this payment be treated as a private expense – and thus as consumption – or rather as part of income production, or a business expense? The normative personal expenses in question indeed reduce taxpayers' resources. In other words, they reduce their economic ability to choose how much to consume and how much to save. This is true for both types of expenses.

Nevertheless, there is still dissimilarity if Andrews' view is disregarded. Andrews, to some extent, detaches the use side from the income production side. The ability to pay is indeed lowered in both cases – whether a taxpayer paid for charity¹⁴⁶ or for childcare – but not for self-consumption. This is a sufficient condition for Andrews. If someone transfers some of his income to charity or to childcare, then indeed he immediately reduces his disposable income for future

139. 2 ADAM SMITH, AN INQUIRY INTO THE NATURE AND CAUSES OF THE WEALTH OF NATIONS 825-28 (R.H. Campbell et al. eds., 1979).

140. RICHARD A. MUSGRAVE & PEGGY B. MUSGRAVE, PUBLIC FINANCE IN THEORY AND PRACTICE 235 (3rd ed. 1980).

141. See, e.g., MURPHY & NAGEL, *supra* note 93, at 12.

142. See, e.g., JOEL SLEMROD & JON BAKIJA, TAXING OURSELVES 61-66 (4th ed. 2008).

143. See, e.g., Joseph M. Dodge, *Theories of Tax Justice: Ruminations on the Benefit, Partnership, and Ability-to-Pay Principles*, 58 TAX L. REV. 399, 401-03 (2005).

144. See, e.g., MURPHY & NAGEL, *supra* note 93, at 20.

145. For ways to measure the ability to pay see Andrews, *supra* note 1, at 327.

146. See, e.g., Gergen, *supra* note 75, at 1426.

saving or consumption. But there is an important distinction between those expenses which are directly related to the income production side of the equation and the “alternative” the taxpayer has, which Andrews did not consider important.¹⁴⁷

Ex Ante/Post Expense and Un/Related Party

Both payments – to charity and to childcare – reduce one’s ability to pay. Nevertheless, one expense is directly related to income producing and is similar to an *ex ante* expense. If the parent, usually the mother,¹⁴⁸ does not pay the nanny for taking care of the child, then she cannot go to work and produce her income. And when she does work, when daycare expenses are not deductible, and she continues to work the same number of hours, she is left with a lower income. This result is absurd. Not only does she have to pay the child-care expenses to be able to work, but she has to support another person with a lower real income.

On the other hand, the contribution to charity expense is not a prerequisite for income production. The expense to charity is *ex post* – after the income has been produced. This *ex-ante/post* discussion is related to the remoteness of the other person, the transferee, in the altruistic act. The payment for child or dependent care benefits a related party, as opposed to contribution to charity,¹⁴⁹ and is thus motivated by a much more powerful need. If the parent will not provide for his child – who will? But if the person will not donate to the charity – others may still donate. Moreover, the parents’ payment to childcare is directly related to income production.

The *ex ante/post* distinction is fundamental for differentiating between these two normative expenses,¹⁵⁰ despite Andrews’ view. Naturally, both expenses are relevant for the use side of the equation, but only the child-care expense is related also to the income production side. It is a normative expense that can be normatively discussed from both the source and use sides of the equation. It is a personal expense but at the same time, a business-oriented one, and thus should be regarded as “ordinary and necessary.”¹⁵¹

147. For the importance of the income production side see, for example, Koppelman, *supra* note 66.

148. See *supra* Chapter VII.

149. This paper disregards donations to related parties.

150. The *ex ante* expense is also relevant to many other basic expenses (such as food, accommodation etc.) though those expenses lack a normative aspect.

151. See *supra* Chapter I.A.

Andrews stresses an expense that is not for personal use should be deductible since it promotes other distributive goals.¹⁵² Clearly, both expenses in question are normative ones that promote both regulatory and redistributive goals, but the main difference is that one expense is detached from income production and the other is not.¹⁵³ This difference is related to the traditional definition of mixed business and personal expense and the comprehensive tax base discussion. Donation to charity is a personal expense, but a child-care expense required by the parent to produce income is a mixed business and personal expense.

Keeping in mind the dissimilarity of the expenses, should both kinds be treated the same way? Child-care expenses are mixed business and personal expense and should be treated accordingly,¹⁵⁴ but charity donations, which only promote regulatory and distributive goals, may be treated differently since they are irrelevant to income production. A certain tax incentive may be appropriate, but perhaps in the form of credit.

Economically, there is a key difference between a credit and a deduction: A credit reduces the tax liability itself, whereas a deduction is subtracted from the income itself.¹⁵⁵ Credits directly reduce the total tax rate and deductions reduce the taxable income. If we adopt Surrey's hypothesis, then a credit is a tax incentive that is "a departure from normal tax structure,"¹⁵⁶ usually granted to help low-income families avoid eroding their real income¹⁵⁷ and to save a certain minimum amount of money for equitable reasons.¹⁵⁸ This can be mainly achieved by refundable credits.¹⁵⁹ According to the Haig-Simons formula, there is no room for credits, but only for business deductions since they help assess the net income, the change in individual wealth. A credit may promote other tax goals, such as regulatory and redis-

152. But see Andrews' argument for deducting childcare expenses: "[T]he reason for allowing the [childcare] deduction has to do with the working mother's loss of time to devote to household tasks as compared with the nonworking mother, which is precisely the kind of household difference that ought to be taken into account in allocating personal tax burdens." Andrews, *supra* note 1, at 382.

153. See the above discussion on the Ability to Pay and Expense Deductibility under this Chapter.

154. This conclusion is relevant to any mixed expenses with an altruistic aspect, such as dependent expenses, and extra payment to a disabled employee, as discussed *supra* Chapter I.B.

155. See, e.g., POSIN & TOBIN, *supra* note 56, at 3, 633.

156. Surrey & McDaniel, *supra* note 42, at 680.

157. See, for example, ROYAL COMMISSION ON TAXATION, *supra* note 92, at 46-47.

158. 3 ROYAL COMMISSION ON TAXATION, REPORT OF THE ROYAL COMMISSION ON TAXATION: THE USE OF THE TAX SYSTEM TO ACHIEVE ECONOMIC AND SOCIAL OBJECTIVES 21 (1966).

159. *Id.*

tributive ones, but it does not accurately measure wealth production. Over the years, policymakers deviated from the Haig-Simons formula for economic or social goals¹⁶⁰ that can be justified on regulatory or redistributive grounds. If we adopt a more economic, but still normative, approach to income, we may say that a child-care expense should be deductible precisely because it is also business related and thus promotes all tax goals. This deduction does not contradict the ideal income tax even according to the tax expenditure analysis.¹⁶¹ On the other hand, since charity contribution expenses are tax incentives that only support the redistributive and regulatory goals but are unrelated to income production, they should be incentivized by way of credit, but not deduction. This recommendation is diametrically opposed to the applicable law. As shown above, charity donations are deductible, whereas child-care expenses are given a credit.

CONCLUSIONS

In this Article, I tried to find a coherent justification for certain expenses that have a normative aspect of altruism, such as charitable contributions and child-care expenses. An essential characteristic of those so-called “private” expenses is the taxpayer’s altruistic behavior. In other words, the expense was made to benefit another person. The methodology was to examine whether those expenses fall in line with the three goals of taxation: revenue raising, regulatory, and redistributive goals. Only expenses that serve all three purposes help maintain a coherent tax system by synchronizing the comprehensive tax base theory with its opponents.

One of the criticisms raised against Andrews’ work was that it is chaotic and lacking in a “coherent normative principle.”¹⁶² Our comparison of the two types of expenses has shown that by virtue of an expense’s normative aspect, both expenses meet and promote redistribution and regulatory objectives. The discussion hitherto is analogous to Andrews’ argument. But the difference occurs when we refer to the first objective, which requires us to tackle the deduction issue from both sides of the equation – use and source. I believe that by focusing on the use side, at the expense of the income production side, Andrews has missed an important distinction. Charitable contributions can be made after the income has been produced, while child-care expenses are linked to the production of income itself. This is

160. See the discussion on income *supra* Chapter II.

161. See *supra* Chapter IV.

162. See, for example, the discussion surrounding *supra* Chapter IV.

because child-care expenses are mixed expenses that carry both business and private elements. Moreover, this direct link between the use and source is vital to income production since childcare is a *coercive ex ante expense*. Conversely, other normative expenses, which are not prerequisites for income production, should not necessarily be deductible and may receive other tax reliefs. The *ex ante* and *ex post* discussion is a fundamental difference between these two normative expenses, which disregards Andrews' view. Thus, child and dependent care expense can be normatively discussed both from the income production and use side of the equation, as it represents a mixed personal and business expense, which should thus be regarded as "ordinary and necessary."¹⁶³

A mixed expense comprising an altruistic normative component is an expense that connects the revenue side to its uses and weighs both the use and source side equally. This link between the source of income and its uses enables a coherent tax policy to promote the three goals of taxation at the same time. Following this analysis, my recommendation is to treat child-care expenses as deductions and charitable contributions as credits – the exact opposite of applicable law in the United States.

163. See the discussion in *supra* Chapter I.A.

