Bakke v. Regents of University of California: Potential Implications For Income Tax Exemptions and Affirmative Action In Private Educational Organizations

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This article explores the effects that the United States Supreme Court decision in Bakke *may have on the tax exempt status of private, non-profit educational organizations which have implemented affirmative action programs. It outlines the current IRS position with respect to racial discrimination by such organizations and proceeds to synthesize that position with various possible holdings in* Bakke.

INTRODUCTION

This article reviews generally the position of the Internal Revenue Service (IRS), under the applicable law and the regulations and interpretive rulings of the IRS, on the issue of racial discrimination and federal income tax exemptions for private schools and certain other charitable educational organizations. It will address the very current issue of what effect the operation of "minority-sensitive" programs favoring a particular racial minority in the distribution of benefits, such as admission to professional school, should have on the tax exempt status of such organizations. The article concludes with an

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analysis of the potential impact of the upcoming *Bakke* decision on this issue. This analysis will examine some of the possible alternative holdings in the case, based on existing law, to demonstrate how the Supreme Court's determination may affect far more than just admissions to professional schools in public institutions.

I. POSITION OF THE IRS

The current position of the IRS on racial discrimination in private education, stated in Revenue Ruling 71-447,[1] is that section 501(c)(3) of the Internal Revenue Code,[2] exempts from federal income taxation organizations (including corporations, foundations, community chests, etc.) organized and operated exclusively for any of a number of separate "charitable" purposes, including the advancement of education. Revenue Ruling 71-447 indicates that the term "charity," as conceived at common law, encompasses all three of the major categories identified separately under section 501(c)(3) as religous, educational, and charitable:

> Thus, a school (or other organization) asserting a right to the benefits provided in section 501(c)(3) of the Code as being organized and operated exclusively for educational purposes must be a common law charity in order to be exempt under that section.[3]

This ruling then notes that under common law, a charitable trust may not be formed for a purpose which is illegal or contrary to public policy.[4] Turning to the question of racial discrimination, the ruling, citing *Brown v. Board of Education*[5] and the Civil Rights Act of 1964,[6] finds a well established national policy to "discourage racial discrimination in education, whether public or private." Revenue Ruling 71-447 applies specifically to private schools, even though the cases on racial discrimination generally require a showing of state action before a constitutional violation may be found.[7] The justification for this rule is that, for purposes of the common law of charities, a national public policy condemning both public and private discrimination in education exists. Therefore, private schools practicing racial segregation, whether or not such practice is actually unconstitutional, are not "charitable" in the common law sense.[8] The ruling thus concludes

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1. Rev. Rul. 71-447, 1971-2 C.B. 230.
2. I.R.C. § 501(c)(3), as amended.
3. Rev. Rul. 71-447, 1971-2 C.B. 230.
4. *See* RESTATEMENT (SECOND) OF TRUSTS § 377 (1959).
5. 347 U.S. 483 (1954).
6. 42 U.S.C. §§ 2000c - 2000d-4 (1970).
7. But note that no state action is required under the 1866 Civil Rights Act, which implements the thirteenth amendment. *See* discussion in text accompanying note 49 *infra*.
8. This concept of noncharitability of illegal trusts encompasses more than merely statutory violations. *See* IV SCOTT ON TRUSTS § 377 (3d ed. 1967), which discusses examples of public policies the violation of which may result in a trust failing

that a school that does not have a racially nondiscriminatory policy as to students is acting contrary to this national public policy, and is not charitable in the requisite common law sense. Therefore, such schools are not exempt under section 501(c)(3), and contributions thereto are not deductible as charitable contributions.[9]

It is, of course, extremely difficult to ascribe motivations to the particular actions or inactions of administrative agencies. Nonetheless, as a factual matter, the IRS did not adopt its public position prohibiting racial discrimination by exempt private schools until it was faced with the possibility that the courts might force this rule (or perhaps even a stronger one) on it. The prior IRS policy[10] of issuing determinations of exempt status to schools expressly refusing to admit black students on the basis of race was challenged in *Green v. Connally*.[11] It was not until midway into the litigation in *Green* (after the district court had issued a preliminary injunction)[12] that the IRS shifted gears and adopted its current position, which was eventually published as Revenue Ruling 71-447.

Before it issued this ruling, the position of the IRS can be stated essentially as follows: (1) the term "charitable" in the exemption and charitable contribution sections of the Internal Revenue Code is used in its generally accepted legal sense and is derived from the traditional principles of the common law of charitable trusts;[13] (2) the common law of charities traditionally considered certain purposes, including the advancement of education, to benefit the community as a whole even though the class of eligible beneficiaries did not include all the members of the community, but only a relatively small group. Thus, it is commonly accepted under the general law of charity that advancement of education may constitute a valid charitable purpose even though beneficiaries are limited to a particular class (*e.g.*, religion,

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for illegality even though no statutory infraction has occurred, for example, where a particular act violates a policy stated in a statute without violating the statute itself.

9. Procedures implementing the substantive requirements of Rev. Rul. 71-447 may be found in Rev. Pro. 75-50, 1975-2 C.B. 587, *superseding* Rev. Pro. 72-54, 1972-2 C.B. 834. These procedures (a number of which are derived from the procedures required of Mississippi schools by the court in the *Green* case, *infra*) include extensive record keeping and publication requirements designed to ensure that all exempt schools have racially nondiscriminatory policies and that such policies are effectively made known to the general public. To meet the publication requirement, a school must make its racially nondiscriminatory policy known to all racial segments of the general community served by the school; schools must also maintain records on the racial composition of the student body, faculty and administrative staff. Additional requirements are further developed in Rev. Pro. 75-50.

10. *See* reference in text following note 15 *infra*, regarding the August 2, 1967 press release by the Commissioner of Internal Revenue.

11. 330 F.Supp. 1150 (3-judge court, D.D.C. 1971), *aff'd per curiam sub nom.* Coit v. Green, 404 U.S. 997 (1971).

12. Green v. Kennedy, 309 F. Supp. 1127 (3-judge court, D.D.C. 1970).

13. Treasury Regulations § 1.501(c)(3)-1(d)(2). [1978] 1 U.S. CODE CONG. & ADMIN. NEWS 1652.

sex, geographical location, and *race*);[14] (3) a charitable trust cannot be created for a purpose which is illegal or the accomplishment of which would tend to frustrate a well-defined public policy. But it is the uses to which property is put and not the motive for devotion of property to such uses that determines charitable qualification.[15] Applying the above principles, the IRS had concluded that it had no authority to deny exemption or qualification for deductible contributions to an otherwise qualified private school solely by virtue of the fact that it excluded blacks as students.[16]

In fairness to the IRS, it should be noted that the legal issues involved in this area were (and still are) far from crystal-clear, and had been the subject of much study and review. Thus, in a press release issued on October 15, 1965, the IRS had announced that applications was in effect from that data until August 2, 1967, while the Commissioner reviewed the legal issues. On August 2, 1967, the freeze ended with a press release stating that strictly private schools, not having any substantial involvement with the state or any political subdivision, were to be recognized as exempt and granted advance assurances of deductibility of contributions, if such schools were otherwise qualified under section 501(c)(3). Denial of exemption would occur only where there was sufficient involvement with a state or political subdivision so as to make the segregated operation of the school unconstitutional or a violation of the laws of the United States. This announcement also made exemptions granted on this basis subject to further judicial or statutory developments on the legality of private segregated schools. This position was apparently based on the IRS view at the time that the courts had not yet definitively ruled discrimination in private schools unlawful. Since no standards were ever published by the Service implementing this position, it may be questioned whether it in fact denied many exemptions under this "state action" rule. Dissatisfied with the application of this rule, plaintiffs brought suit in *Green*.

The IRS initially resisted plaintiff's attempts to enjoin the granting of exemptions by the Service to segregated private schools. On July 10, 1970, the IRS issued its new position in a press release stating that private schools not operating on a racially nondiscriminatory basis as

14. *See* IV SCOTT ON TRUSTS § 370.6 (2d & 3d ed. 1956, 1967); BOGERT, TRUSTS § 375 (2d ed. 1964); RESTATEMENT (SECOND) OF TRUSTS § 370, comment j.

15. *See* RESTATEMENT (SECOND) OF TRUSTS § 368(a) & (d); IV SCOTT ON TRUSTS § 348-68; BOGERT, TRUSTS § 364.

16. The Commissioner's position was actually stated in neutral terms and did not specifically refer to which race was excluded. However, it was clear that the issue was the exclusion of black students from white schools, as in the *Green* case. Historically, and as a practical matter, there were no white students seeking admission to and being denied access to black schools, and in fact, the entire rationale for school desegregation was that segregation denied to blacks equality of education, and that desegregation was necessary to achieve this equality.

to students, do not qualify for the benefits of deductibility of contributions and exemption under section 501(c)(3). Notwithstanding this change of position, however, the district court very carefully considered plaintiff's prayer for declaratory and equitable relief in *Green*. Recognizing that there was some merit in the Service's new position, the court nonetheless went even further.

The *Green* court, analyzing the general law of charitable trusts, noted that, under traditional concepts of the term charity, the benefits of charitable status were precluded to trusts advancing or promoting racial segregation.[17] Although in the past the common law had recognized some racially restricted trusts as charitable, the court concluded that the requisite community benefit was no longer found in otherwise charitable trusts which by their segregated nature stigmatized members of a particular race.[18] Without this community benefit,[19] the court found, private segregated schools do not qualify as charitable under emerging authority in the common law of charities.

Even granting this trend in charity law, however, the court chose not to rely exclusively on this authority in making its decision. In construing the application of federal tax statutes regarding exemption and deductibility, the court relied instead on a finding that federal policy did not permit the challenged tax treatment.

The court in *Green* found that racially discriminatory schools fail to come within the scope of section 501(c)(3) on the basis of a general public policy doctrine of federal tax law. This doctrine was construed as precluding the allowance of special tax benefits where such allowance would be inconsistent with or tend to frustrate a well-defined federal public policy. The general public policy doctrine (which is discussed more fully below) relied on by the court is commonly associated with a line of Supreme Court cases involving business expense deductions.[20] The specific federal policy relied on in *Green* is the policy against government support for racial segregation of schools, which the court found in the school desegregation cases, the

17. Under state law, these benefits include, for example, suspension of the Rule Against Perpetuities, modification of the trust to meet the testator's intent under changed circumstances (the Doctrine of Cy Pres), and so on.

18. 330 F. Supp. at 1157-61; *see also* BOGERT, TRUSTS § 375.

19. The IRS has previously recognized that the entire community did not benefit from an organization providing recreational facilities restricted on the basis of race, Rev. Rul. 67-325, 1967-2 C.B. 113, 116. Unlike the case with the advancement of religion or education, or the relief of poverty, however, the providing of community recreational facilities is not within that class of purposes recognized as charitable even where the benefits are not generally available to the entire community. In *Green*, the issue was whether the common law of charity continued to recognize racial restrictions as being included in that narrow class of purposes within which such restrictions are allowed.

20. These cases include Commissioner v. Sullivan, 356 U.S. 27 (1958) and Tank Truck Rentals, Inc. v. Commissioner, 356 U.S. 30 (1958).

1964 Civil Rights Act, and the fifth, thirteenth and fourteenth amendments to the United States Constitution.[21]

In addition to the issuance of a declaratory judgement broader in its scope than the IRS position, the decree of injunction issued by the court also went further than the IRS approach to the segregated schools issue. In its July 10, 1970 press release, the IRS indicated that it "anticipated that in most instances evidence of nondiscriminatory policy can be supplied by reference to published statements of policy or to the racial constituency of the student body." Based on prior school desegregation litigation following the *Brown* decision and the history of events in Mississippi,[22] the court required an extensive affirmative showing of nondiscrimination as a prerequisite to the allowance of a "charitable" tax status to private schools. The court further notes that, as to Mississippi schools, there was a "badge of doubt," and "a mere declaration of the proper construction of the Internal Revenue Code" would have been insufficient to secure plaintiffs' rights; plaintiffs were also entitled to effective directives and procedures to ensure that schools receiving tax benefits are not part of any system of private schools operated on a racially segregated basis.[23]

The court in *Green* specifically left two issues undecided: (1) the constitutional question of whether the allowance of federal tax benefits to private schools engaging in racial discrimination was unconstitutional "state action" in violation of the fifth amendment to the United States Constitution;[24] and (2) whether the tax benefits in question constitute "federal financial assistance," for purposes of the

21. Notwithstanding the fact that some of the same authority was cited in Rev. Rul. 71-447, the *Green* court's reliance on a federal policy doctrine makes it broader in its application than the IRS rationale in Ruling 71-447. The IRS position, in concluding that discrimination engaged in by a school merely renders the school non-charitable (and therefore nonexempt), thereby avoids the question of whether the allowance of tax exemptions and deductibility of contributions to segregated schools could be held to violate federal law; neither Title VI of the Civil Rights Act nor the Constitution would apply under the IRS analysis. Ruling 71-447 also avoids characterizing tax exemptions and deductions as benefits or governmental "support," which also would raise both constitutional and Title VI questions. *See* the discussion in text accompanying notes 84-96 *infra*.

22. Coffey v. State Educ. Fin. Comm'n, 296 F. Supp. 1389 (3-judge court, S.D. Miss. 1969), established that certain of the schools that later were the subject of the *Green* litigation were part of a concerted system of private segregated schools which was specifically set up in an attempt to circumvent federal desegregation orders. In other words, the schools represented an attempt to perpetuate the former, state-sanctioned dual system, and were thus found to violate the fourteenth amendment. *Coffey* cited a number of other cases in which findings of discrimination against blacks were made.

23. Green v. Connally, 330 F. Supp. at 1171.

24. Under Bolling v. Sharpe, 347 U.S. 497 (1954), the same standards as are applicable to the states under the Equal Protection Caluse of the fourteenth amendment are applicable to the federal government under the fifth amendment's Due Process Clauses.

prohibition under Title VI of the 1964 Civil Rights Act[25] against racial discrimination by programs or activities receiving such federal assistance. The IRS position in Revenue Ruling 71-447 would avoid both issues, since it turns not on any concept of federal benefits inherent in charity status, but on a definition of that status itself under common law. The constitutional issues, although left undecided in *Green*, were, as the court put it, more than a mere "scenic backdrop" to the decision in that case.[26] These issues were raised in the court's preliminary order,[27] and their presence is suggested in the phrasing of the court's final decision, which cites a federal policy against "support for racially segregated education." In the court's view, support through tax benefits is different only in degree from support through direct subsidies, which clearly would constitute unlawful state action if made to private segregated schools.[28] It is a matter of speculation whether the indirectness of the benefit involved would exempt it from constitutional infirmity, as one of those neutral benefits (such as electricity, water, fire protection, etc.) which the state may provide to everyone.[29] In any event, the *Green* court apparently felt that there was some likelihood that the continuation of tax benefits to segregated schools would prove unconstitutional.[30]

The classification of tax exemptions and charitable deductions as "support" provided by the federal government also raises the Title VI issue of "federal financial assistance."[31] While not deciding the issue, the court in *Green* also suggested that Title VI may prohibit the granting of tax exemptions to segregated schools.

There is some question as to the continuing (if not the intial) validity of the *Green* court's broad general view that tax deduction and exemption provisions which otherwise apply to a particular organization should not be construed as applicable thereto if such organization regularly engages in activities which are either illegal or contrary to public policy. In this regard, each of the judicial precedents cited in *Green* as establishing such a sweeping principle involved the disallowance of business expense deductions for expenditures relating to

25. 42 U.S.C. § 2000d (1970).

26. 330 F. Supp. at 1171.

27. 309 F. Supp. 1127, 1133-37.

28. *Id.* at 1134-36. *See also* Norwood v. Harrison, 413 U.S. 455, 463-68 (1973) (provision of free textbooks to segregated schools an impermissible aid to racial discrimination).

29. Moose Lodge v. Irvis, 407 U.S. 163, 173 (1972); *see* discussion in text accompanying notes 97-99 *infra*.

30. The court states:

> If the Internal Revenue Service had not adopted its July, 1970 interpretation [that segregated schools were not "charitable"] . . . we would in all likelihood have been required by the Constitution to enter a decree ordering the Service to cease violating plaintiffs' constitutional rights.

330 F. Supp. 1150, 1171.

31. *See* discussion on *McGlotten* case in text accompanying notes 84-96 *infra*.

illegal activities.[32] Moreover, these precedents were decided before the enactment of the Tax Reform Act of 1969[33] and the Revenue Act of 1971,[34] in which Congress undertook to deal with this problem in a comprehensive way. The intervening passage of this legislation is important because the legislative history seems to suggest that Congress effectively set outer limits on the extent to which public policy considerations could thereafter be held to require the disallowance of any item otherwise qualifying for a tax deduction. Thus, the Senate Finance Committee report on the 1969 Act stated: "The provision for denial of deduction of payments . . . deemed to violate public policy is intended to be all-inclusive. Public policy, in other circumstances, generally is not sufficiently clearly defined to justify disallowance of deductions."[35] Similarly, the corresponding report on the 1971 Act included a general explanation reading in part: "The Committee continues to believe that the determination of when a deduction should be denied should remain under control of Congress. However, the Committee has concluded that the area in which deductions are denied should be expanded somewhat beyond the limits set in 1969."[36]

There are thus many more open questions on the issue of federal tax exemptions and deductibility of contributions to segregated schools than are raised or answered by the Service's position in Revenue Ruling 71-447. One current question is what effect the Supreme Court's impending decision in *Bakke v. Regents of University of California*[37] will have on the current position of the IRS. This analysis will focus primarily on the effects of *Bakke* on the treatment of affected educational organizations under existing IRS guidelines on discrimination. A broad constitutional decision against minority-sensitive, or "affirmative action," programs in *Bakke* could potentially identify remedial action of this nature with the kind of racial discrimination prohibited under Ruling 71-447. Such a characterization could lead to loss of both exempt status of and deductibility of contributions to schools or other charitable educational organizations implementing such affirmative action programs. The fear of potential adverse tax consequences could thus have a chilling effect on voluntary efforts to compensate for past discrimination, and on attempts to remedy the exclusion of minorities that has resulted from policies which fail to recognize the importance of race as a factor. The remainder of this

32. *See generally* cases cited note 20 *supra*.
33. Tax Reform Act of 1969, Pub. L. 91-172, 83 Stat. 487 (1969).
34. Revenue Act of 1971, Pub. L. 92-178, 85 Stat. 497 (1971).
35. S. REP. NO. 91-552, 91st Cong., 1st Sess. 274, *reprinted in* [1969] U.S. CODE CONG. & AD. NEWS 2027.
36. S. REP. NO. 92-437, 92d Cong., 1st Sess. 72-74, *reprinted in* [1971] U.S. CODE CONG. & AD. NEWS 1918.
37. 18 C.3d 34, 132 Cal. Rptr. 680, 553 P.2d 1152, (1976), *cert. granted*, 429 U.S. 1090 (1977).

article seeks to explore the arguments in favor of and against such an extension of the current IRS position regarding discrimination by charitable educational organizations to also apply to the operation by such institutions of remedial-type programs designed to benefit disadvantaged racial minorities.

II. BAKKE

In *Bakke v. Regents of University of California*[38], an unsuccessful white applicant for admission to medical school at the University of California at Davis (Davis, or University) brought an action challenging the legality and constitutionality of the University's special admission program for disadvantaged minority students. Both the trial court and the Supreme Court of California held that the "task force" program (as it was known at Davis) discriminated against plaintiff Bakke because of his race in violation of the Equal Protection Clause of the fourteenth amendment.

The University, stipulating that it could not prove that Bakke would not have been admitted in the absence of the task force program, argued that, despite its adverse effect on Bakke, the program is saved from illegality and constitutional infirmity by its benign[39] purpose. This program, like many similar programs, was set up voluntarily by faculty vote, in the exercise of the school's discretion, in an attempt to deal with the serious problem of minority under-representation in the University and in the medical profession. While maintaining that the medical school itself had never discriminated,[40] the University argued that the problem of discrimination is a society-wide problem, and that the overwhelming exclusion of minorities under traditional admissions standards at the medical school was a result of the lingering effects of this societal discrimination. The decision of the faculty to establish the task force program was an attempt to provide a voluntary and affirmative solution to what they saw as the compelling goal of increasing representation of minorities.[41] This decision was made in light of the

38. *Id.*

39. The terms "benign" discrimination and "reverse" discrimination are, in their popular usage, rather inexact and somewhat misleading. For example, the term "reverse" discrimination when used to describe discrimination against whites seems to imply that there is a "regular" discrimination which is properly exercised when nonwhites are the victims. Likewise, to the extent a particular white individual is disadvantaged thereby, "benign" discrimination is certainly not benign as to that individual. The use of these terms by the author is not intended to imply any endorsement of the many connotations arising from the use of these terms in their popular sense; but is merely a convenient way of labeling the topics of discussion in this article.

40. It seems evident that this assertion of the University's nondiscrimination against minorities by both Bakke and the University shows some lack of spirited adverseness between the parties, and could conceivably mean that the issues were not argued as forcefully as they could have been. Since the Supreme Court has chosen to grant *certiorari*, however, speculation on this point appears moot.

41. The particular minorities receiving special consideration under the task force program were Blacks, Native Americans, Hispanics (Chicanos, Puerto Ricans and

fact that the so-called objective criteria for admission into professional school (*e.g.*, grades and standardized test scores) are effective predictors only at a certain threshold level. They establish a statistical probability that a particular applicant will or will not be capable of successfully completing the academic program, entering the profession and being competent in practice. Beyond that, reputable institutions use such "objective" criteria as an exclusionary tool, to reduce the vast overapplication[42] for admission slots to manageable numbers. The University asserted that all admittees to the University, including the sixteen minorities admitted under the task force program, were fully qualified at the relevant threshhold level described above.

The United States Supreme Court granted *certiorari* in light of the extreme controversy surrounding the issue of minority preferences and because of numerous conflicting decisions in the courts on the constitutionality and legality of such special treatment. It is important to examine some of the relevant cases and other authorities which could form the basis on which the Court determines the result in *Bakke*.

A. "Benign" vs. "Invidious"

The unconstitutionality of invidious discrimination by a state is now well established. Before *Brown v. Board of Education*,[43] only the most blatant forms of discrimination were invalidated.[44] After *Brown*'s disapproval of the "separate but equal" doctrine endorsed in *Plessy v. Ferguson*,[45] the courts regularly found state suport of racial segregation of blacks and other minorities in an educational context to be invidious and in violation of the Constitution.[46] Most of the cases

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Cubans) and Asians. The concept of "minority" has been adequately defined in numerous decisions, beginning with Justice Stone's famous footnote in United States v. Carolene Prod. Co., 304 U.S. 144, 152-53, n.4 (1938), in which the Supreme Court recognized that "more searching judicial inquiry" may be needed to prevent prejudice against minorities. Whether the same standards apply in the case of racial classifications to benefit such minorities is not clear; *see* Justice Tobriner's dissent, *Bakke*, 18 Cal. 3d 34, 79-80, 132 Cal. Rptr. 680, 711, 553 P.2d 1152, 1183 suggesting a negative response to that query. *See also* discussion in text accompanying notes 64-67 *infra*.

42. In 1973, the first year Respondent Bakke applied to Davis, there were almost 37 applications for each of 100 available seats; in 1974, the second time Bakke applied, there was a ratio of over 37 to 1. 18 Cal.3d at 38, 132 Cal. Rptr. at 683, 553 P.2d at 1155.

The figure for other professional schools are comparable: vast overapplication for a limited number of places, from which qualified minorities are overwhelmingly excluded by high selection criteria established not so much as a measure of ability to succeed, but as an exclusionary tool. *See* Brief on Petition for Certiorari for Deans of School of Law at Boalt Hall, Davis, UCLA and Hastings as *Amicus Curiae*.

43. 347 U.S. 483 (1954).

44. *See* Nixon v. Herndon, 273 U.S. 536 (1927) (law denying blacks right to vote); Yick Wo v. Hopkins, 118 U.S. 356 (1886) (unequal application of law discrimination against Chinese); Strauder v. West Va., 100 U.S. 303 (1879) (law denying blacks the right to serve as jurors).

45. 163 U.S. 537 (1896).

46. *See* Runyon v. McCrary, 427 U.S. 160 (1976); Norwood v. Harrison, 413 U.S. 455 (1973); Swann v. Charlotte-Mecklenburg Bd. of Educ., 402 U.S. 1 (1971); North

dealt with state-sanctioned dual public school systems and the courts held these unconstitutional under the fourteenth amendment. *Norwood v. Harrison*[47] indicated that even indirect state aid, in the form of state textbook grants to private schools, could violate the fourteenth amendment when the grantee schools excluded black children. *Runyon v. McCrary*[48] cut the unbilical cord of necessity to prove state action by invalidating private school segregation under the thirteenth amendment and the "equal right to contract" provision of section 1 of the 1866 Civil Rights Act.[49]

With regard to school desegregation, affirmative, race-conscious remedies may be ordered when a constitutional violation has occurred, even remedies going beyond merely ordering the cessation of unlawful activity.[50] The federal courts have disagreed, however, on the essential issue in *Bakke*: whether a school may take race into account in an effort to benefit minorities by integrating them into the institution, when an indirect result of such affirmative action is some detriment to the members of the majority. There are numerous decisions going both ways on this issue, not just in the school area, but in the analogous area of employment discrimination as well. The California Supreme Court considered some of these cases and, over a strong dissent by Justice Tobriner, concluded that the weight of authority leaned more heavily towards a finding that the affirmative action program at Davis was constitutionally infirm.[51] The dissenting opinion

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Carolina State Bd. of Educ. v. Swann, 402 U.S. 43 (1971); Griffin v. County School Bd., 377 U.S. 218 (1964).

47. 413 U.S. 455 (1973).

48. 427 U.S. 160 (1976).

49. *Id.* at 177-79. Section 1 of 1866 Civil Rights Act is now codified at 42 U.S.C. § 1981 (1870).

50. Keyes v. School Dist. No. 1, 413 U.S. 189, 207-13 (1973) (operation of dual school system gave school board affirmative duty to make transition to racially nondiscriminatory school system). In some situations, a failure to take race into account may itself be unconstitutional. North Carolina State Bd. v. Swann, 402 U.S. 43, 45-46 (state anti-busing law requiring "color-blind" student assignment unconstitutional in light of prior *de jure* segregation); Swann v. Charlotte-Mecklenburg Bd. of Educ., 402 U.S. at 22-25 (order imposing racial balance ratios for students and faculty within power of federal court, where mathematical ratios were a mere "starting point" in process of shaping an equitable remedy for a constitutional violation); Green v. County School Bd., 391 U.S. 430, 437-42 (1968) ("freedom of choice" plan for desegregating dual school system held unacceptable where segretation in fact continued and more effective alternatives existed).

51. 18 C.2d at 57-58, 132 Cal. Rptr. at 696-97, 553 P.2d at 1168-69. *See* Chance v. Board of Exam. 534 F.2d 993 (2d Cir. 1976) (bona-fide seniority system upheld; preferential treatment in forms of racial quotas, in absence of prior discrimination, characterized as "reverse" discrimination). *See also* Weber v. Kaiser Alum. & Chem. Corp., 415 F. Supp. 761 (E.D. La. 1976) (minority preference held inappropriate where individual minorities preferred were not shown to have been previously subjected to unlawful discrimintion), and Anderson v. San Francisco Unif. School Dist., 357 F. Supp. 248 (N.D. Cal. 1972) (percentage hiring goals for minority school administrators unrelated to any showing of past discrimination enjoined by court); Watkins v. United Steelw'rkr's of Am., 516 F.2d 41 (5th Cir. 1975) ("last-hired, first-fired" seniority system that affected minorities in greater numbers than white did not violate Title VII);

in *Bakke*, however, cited contrary authority, for the proposition that minority preferences are permissible in some circumstances.[52]

The dissent cited a number of "Executive Order" cases[53] upholding the principle of affirmative action espoused by Executive Order 11246,[54] promulgated by President Lyndon Baines Johnson. The Order requires federal contractors to implement affirmative hiring of minorities; no showing of prior discrimination by affected contractors was required by the courts in these cases. The dissent in *Bakke* thus argued that no color blindness is required by the Constitution. As stated by the court in Germann v. Kipp:[55]

> Viewed in a constitutional context, it may be said that utilization of an affirmative preference for women and minorities is ameliorative, rather than invidious, and that it therefore may be permissible to be temporarily color-conscious in order to become color-blind.[56]

Recent decisions by the Supreme Court in other contexts dealing with the subject of minority preferences seem to lend further support to the view that "ameliorative" programs to benefit minorities are permissible. It is not clear, however, to what extent affirmative remedies are dependent on a finding of prior discrimination. For example, in *United Jewish Organizations, Inc. v. Carey*,[57] a redistricting plan

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Kirkland v. N.Y. State Dept. of Corr'l Serv., 520 F.2d 420 (2d Cir. 1975) (minority quota in hiring of supervisors for correctional institution struck down).

52. 18 C.3d at 67-80, 132 Cal. Rptr. at 702-11; 553 P.2d at 1174-83 *citing* Carter v. Gallagher, 452 F.2d 315 (8th Cir. 1971), *cert. denied*, 406 U.S. 950 (1972) (temporary minority hiring goal in fire department hiring ordered by court as remedy for prior discrimination); Porcelli v. Titus, 431 F.2d 1254 (3d Cir. 1970), *cert. denied*, 402 U.S. 944 (1971) (school board abolished promotional list based on use of examination, implemented new standards to move towards racial balance in proportions of blacks at all levels of seniority in faculty and administration); Offermann v. Nitkowski, 378 F.2d 22 (2d Cir. 1967) (school board's pupil placement plan placing students by race to eliminate *de facto* segregation upheld); *see also* Germann v. Kipp, 429 F. Supp. 1323 (W.D. Mo., 1977) (white fire department employees passed over for promotion by minorities under affirmative action plan were not unconstitutionally discriminated against; remedial plan consistent with spirit of Title VII, Executive Order 11246).

53. *See, e.g.*, Contractors Ass'n of Eastern Pa. v. Secretary of Labor, 442 F.2d 159 (3d Cir. 1971), *cert. denied*, 404 U.S. 854, in which the Department of Labor's Philadelphia Plan imposing affirmative action minority hiring goals on certain federal contractors was upheld pursuant to Exec. Order 11246. The court found that the minority utilization goals were not inconsistent with Titles VI and VII of the 1964 Civil Rights Act, or with the fifth amendment. *Id.* at 173-74. The court also found that the goals were within the power of the Executive Branch to impose on federal contractors, even where the contractors themselves had not discriminated (findings of prior discrimination by the union supplying manpower were made, but no such findings were made against the construction contractors). *Id.* at 1975. *See also* Associated Gen. Contractors of Mass., Inc. v. Altshuler, 490 F.2d 9 (1st Cir. 1973) *cert denied*, 416 U.S. 957 (1974); Southern Ill. Builders Ass'n v. Ogilvie, 471 F.2d 680 (7th Cir. 1972); Joyce v. McCrane, 320 F. Supp. 1283 (D.C.N.J. 1970).

54. 30 C.F.R. 12319 (*as amended by* Exec. Order 11375, 23 Fed. Reg. 14303).

55. 429 F. Supp. 1323 (W.D. Mo. 1977).

56. *Id.* at 1332.

57. 430 U.S. 144 (1977).

made under section 5 of the Voting Rights Act of 1965[58] to protect minority voting strength in certain state legislature districts in Kings County, New York, was challenged by the local Hasidic Jewish community which was split in half by the plan. The Court upheld the redistricting plan under the fourteenth and fifteenth amendments, despite its adverse effect on the Hasidic community, holding that such redistricting under the Act was "not confined to eliminating the effects of past discriminatory districting or apportionment."[59] Since the entire thrust of the Voting Rights Act itself is to eliminate the effects of discrimination, the burden of proof is placed on governmental subdivisions, and actual proof of prior discrimination is not required when the Act applied.

A number of cases allowing retroactive seniority for minority workers, thereby advancing them over otherwise senior white workers, also show some acceptance of the principle of minority preferences. In *Franks v. Bowman Transportation Co.*[60] and *International Brotherhood of Teamsters v. United States*,[61] a pattern of racial discrimination violating Title VII of the Civil Rights Act of 1964 was found, and the Court allowed retroactive seniority to the date of the Act (or the date of hiring). Because a pattern of discrimination was found, the Court in *Teamsters* rejected the contention that each individual minority worker who was a member of the class which had suffered discrimination should be required to prove that he personally had unsuccessfully applied for a position from which the class had been excluded. The Court found the detriment to white workers who would otherwise enjoy seniority to be permissible under the Act. Based on these cases, it appears that some deviations from the theory that remedies must be tied to specific prior acts of discrimination have already been established.

A final footnote in the controversy on the issue of minority preferences is the degree of judicial scrutiny to which such preferences should be subject. The majority in *Bakke* applied the traditional standard generally applied in cases of *invidious* racial discrimination:[62] strict scrutiny, with the burden placed on the discriminator to prove the absence of a constitutional violation.[63] The University stipulated that it was unable to meet this burden; a compelling interest was shown to be present, but the California Supreme Court held that the University had not shown that alternatives less detrimental than the affirmative action program did not exist. The dissent, citing Justice

58. 42 U.S.C. § 1973c (1970).
59. 430 U.S. at 161.
60. 424 U.S. 747 (1976).
61. 431 U.S. 324 (1977).
62. Loving v. Virginia, 388 U.S. 1 (1967); McLaughlin v. Florida, 379 U.S. 184 (1964); *see also* cases cited in notes 44-46 *supra*.
63. 18 C.3d 49, 50, 132 Cal. Rptr. 690, 91, 553 P.2d 1162, 1163.

Stone's famous footnote[64] in *United States v. Carolene Products Co.*,[65] on which the strict scrutiny test is based, argued that a less stringent standard of review is appropriate in the case of remedial racial classifications to benefit certain minorities.[66] Justice Brennan's concurring opinion in *United Jewish Organizations* lists a number of good reasons why even so-called benign racial classifications must be given some scrutiny, although short of the demanding "strict scrutiny" standard. Among these reasons is the fact that a purportedly preferential classification may in fact disguise a policy that perpetuates disadvantageous treatment of the minority groups supposedly benefited by the policy. Justice Tobriner's dissent in *Bakke* also recognized this danger, noting that programs of minority preferences must be examined to see if they are a rational means of accomplishing their purported purpose and effectively operate as such.

B. Implications of DeFunis

The judicial controversy over this issue reached the Supreme Court of the United States in an earlier case, in the same context of preferential minority admissions to a professional school. In *DeFunis v. Odegaard*,[67] a white student challenged the admissions procedures of the University of Washington Law School, which separated applications of minority students and gave consideration to their race, along with other more "objective" factors, in determining whether or not to admit them. The case was declared moot on the ground that the plaintiff, after being admitted into the student body pursuant to an interim court order, had already begun the last semester of his senior year by the time the Supreme Court heard oral argument on the case. Justice Douglas wrote a long dissent stating that the case should be tried on the merits. While indicating that the school was correct in separating minority applications for separate consideration, "lest race be a subtle force in eliminating minority members because of cultural differences," he felt that consideration of race as a factor for admission was unwarranted. Douglas put it thus: "The key to the problem is the consideration of each application *in a racially neutral way*."[68] He went on to state that, "There is no constitutional right for any race to

64. Justice Stone recognized that the general presumption of the constitutionality of governmental action is not entirely appropriate in certain cases:

> Prejudice *against* discrete and insular minorities may be a special condition which tends seriously to curtail the operation of those political processes ordinarily to be relied upon to protect minorities, and which may call for a correspondingly more searching judicial inquiry.

United States v. Carolene Prod., 304 U.S. at 152-53, n.4. (emphasis added).

65. 304 U.S. 144 (1938).

66. *See, e.g.*, Morton v. Mancari, 417 U.S. 535 (1974) (Indian hiring preference in Bureau of Indian Affairs upheld).

67. 416 U.S. 312 (1974).

68. *Id.* at 334 (emphasis in the original).

be preferred." Although his opinion also disparaged the creation of population equivalency requirements and other such quotas, it is nonetheless evident that an acceptance of the Douglas philosophy here would not require "color-blindness" nor otherwise preclude an admissions committee from considering the extent to which the prior achievements of any given applicant may have been adversely influenced by prior discrimination of a racial nature. As a matter of fact, the Douglas opinion concluded that the initial trial court record provided no basis for a judgment that the specific law school admission procedure there under challenge was in violation of the Equal Protection Clause.

The manner in which the Court avoided the issue in the *DeFunis* case obviously leaves room for considerable uncertainty. The question remains as to how much of the corrective approach that is reflected in the line of cases approving some kind of affirmative action will ultimately be endorsed by the Supreme Court. Under the Douglas theory, some kind of individualized consideration of the effects of race seems permissible. But the Court has recognized in other contexts the difficulty of individualizing such determinations. Thus, in *International Brotherhood of Teamsters*, it was not necessary for each individual minority claimant who was a member of the affected class to prove that he specifically was refused employment in violation of Title VII, once a pattern of discrimination had been shown.[69] As stated earlier, there are inherent dangers in using group preferences, but it is clear that they may be utilized under certain circumstances for specific purposes.

III. Tax Exemptions: Effect of Bakke Affirmance

Revenue Ruling 71-447 applies its ban to "discrimination" on the basis of race. An affirmance of the California Supreme Court's decision that the minority admissions program in *Bakke* is unconstitutional discrimination could result in the restrictions in this ruling being applied to ban affirmative action programs as well as invidious racial discrimination. The exempt status of private schools would certainly be in question in this event; but other organizations performing educational and charitable functions could be affected as well.[70] An affected organization's noncompliance with a Supreme Court decision declar-

69. *See also* Califano v. Webster, 430 U.S. 313 (1977) (classification under Social Security Act favoring women not unconstitutional, since it served permissible purpose of redressing prior societal discrimination against women as a group); Milliken v. Bradley, 433 U.S. 267 (1977) (*Milliken II*), (pupil assignments and remedial programs ordered to compensate for public schools segregation); Morton v. Mancari, 417 U.S. 535 (1974) (Indian hiring preference for Bureau of Indian Affairs upheld); Gaston County v. United States, 395 U.S. 285 (1969) (voting literacy test adversely affecting minorities invalidated under Voting Rights Act of 1965).

70. *See* discussion accompanying text preceding note 79 *infra*.

ing the minority admissions program at Davis invalid could mean the loss of its exempt status and deductibility of contributions under the ruling, if the term "discrimination" within the meaning of that ruling were expanded to include minority preferences notwithstanding their remedial purpose.

While remedial and invidious discrimination may be equated under Revenue Ruling 71-447 in the event of a *Bakke* affirmance, the author believes that it is unlikely that the IRS will administer the ruling in the same fashion for ameliorative preferences. Thus, with respect to invidious discrimination against minorities, present IRS requirements are generally satisfied if there is no demonstrable exclusion of minorities; actual integration is not required, even for those institutions which were shown to have discriminated in the past, if the Service's nondiscrimination guidelines are followed.[71] Under IRS procedures,[72] a documentary submission by the school that it does not discriminate (along with submissions providing the other information and records required) is usually sufficient for a school to get a favorable ruling from the Service, even in an all-white private school set up on the heels of a local public school desegregation order, and even if no minority enrollment is anticipated.[73] Affirmative action to correct a racial imbalance is not required under current IRS procedure, merely the absence of overt discriminatory acts.

On the other hand, the granting of minority preferences under an affirmative action program is much easier to show. The existence of a policy to grant preferences to minorities in the admissions process would be a red flag, drawing attention to itself as an overt discriminatory act. It would lead to the application of Revenue Ruling 71-447 more quickly than in the case of invidious discrimination, which is

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71. It is questionable, at best, whether the granting of exemptions on this basis to allegedly discriminatory schools in another *Green*-type action could be successfully challenged. In Simon v. Eastern Ky. Welfare Rights Org., 426 U.S. 26 (1976), Justice Stewart noted in his brief concurring opinion:

> I cannot now imagine a case, at least outside the First Amendment area, where a person whose own tax liability was not affected ever could have standing to litigate the federal tax liability of someone else.

Id. at 46. Thus, it is very possible that such an action would be unsuccessful on the grounds of lack of standing. Note, however, that the *Green* case has been refiled, and still another challenge to IRS practice in granting tax exemptions has been initiated. Green v. Blumenthal, Civ. No. 1355-69 (D.D.C., refiled July 23, 1976), and Wright v. Blumenthal, Civ. No. 76-1426 (D.D.C., filed July 30, 1976). The outcome of these cases remains to be seen.

72. Rev. Pro. 75-50, 1975-2 C.B. 587, and its predecessor, Rev. Pro. 72-54, 1972-2 C.B. 834.

73. For schools already recognized as exempt, facts and circumstances such as these, in addition to the general perception of the school in the community, may be considered under the Service's private school audit program, in which 10% of all exempt private schools are examined annually with respect to their racial policies, and suspension of advance assurances of deductibility or actual revocation is recommended if it appears that racially discriminatory policies are in fact being followed. Internal Revenue Manual G-10 (Rev. 1).

generally covert. As a practical matter, it is likely that this possibility would have a "chilling effect" on such affirmative action policies, possibly even where an institution's situation is distinguishable from a *Bakke*-type program, if the points of distinction are not relatively clear or obvious.

A *Bakke* affirmance might also result in some amendment of current IRS pronouncements that indicate that minority-sensitive programs are not within the pale of Revenue Ruling 71-447's ban on discrimination.[74] The Treasury Regulation 1.501(c)(3) states that "charitable" purposes as used in section 501(c)(3) include the elimination of prejudice and discrimination. Remedial programs to encourage more representative minority participation are generally geared to do just that. The above-cited Treasury Regulation, however, does not specifically mention the use of minority preferences as a means of eliminating prejudice, and a Supreme Court judgment that the use of such preferences in the absence of prior discrimination is unconstitutional would, of course, be controlling.

The effects of a broad constitutional decision affirming *Bakke* could be far reaching, not only in the tax exemption area but in other areas as well. Thus, it is important to consider possible points of distinction between *Bakke* and those section 501(c)(3) organizations whose exemptions may be affected under Ruling 71-447. In the next few pages, this article explores some of these distinguishing factors

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74. *See, e.g.*, Rev. Pro. 75-50, § 302, 1975-2 C.B. 587, which states:

> A policy of a school that favors racial minority groups with respect to admissions, facilities and programs, and financial assistance will not constitute discrimination on the basis of race when the purpose and effect is to promote the establishment and maintenance of that school's racially nondiscriminatory policy as to students.

A similar provision as to scholarship and loans programs appears in § 4.05 of Rev. Pro. 75-50. *See also* Rev. Rul. 88-272, 1977-32 I.R.B. 11, in which exemption as a school was recognized for a union job-training program that trained solely American Indians.

Service pronouncements are not the only federal statements accepting the principle of affirmative minority preferences. A list of these is included in the Government's Brief as *Amicus Curiae* in *Bakke*, in Appendix A, and on pages 33-36 of the brief. We have already cited Exec. Order 11246, 30 Fed. Reg. 12319 (*as amended by* by Exec. Order 11375, 32 Fed. Reg. 14303) which requires federal contractors to establish and follow minority utilization goals. The H.E.W. regulations on Title VI (which apply to schools receiving federal funds) allow the use of affirmative action to counteract conditions limiting minority participation, even in the absence of prior discrimination. 45 C.F.R. Part 80 (1976). The Equal Employment Opportunity coordinating Council (a joint body including the Dept. of Justice, Dept. of Labor, Equal Employment Opportunity Commission, Civil Rights Commission and the Civil Service Commission) has issued a statement encouraging state and local governments to adopt affirmative action programs. Other agencies sanctioning or administering some type of affirmative action include the Dept. of Commerce (Minority Business Enterprise Program), the Small Business Administration (Minority Business Development), the Bureau of Indian Affairs, and others. The federal government is thus committed to the concept of ameliorative preference with the purpose of increasing minority participation in society.

and considers how the IRS may apply them in considering the implications of a *Bakke* affirmance.

A. Private Schools:

1. State Action

The constitutional issue in *Bakke* involves the application of the Equal Protection Clause of the fourteenth amendment. The state action requirement for the application of this amendment is so well-established that it does not bear repeating. Thus, with respect to the fourteenth amendment, a truly private institution involving no state action would not fall within the scope of a Supreme Court affirmance of *Bakke* on constitutional grounds.[75] The IRS position pre-*Green* reflected this distinction. It denied exemption and made contributions non-deductible if the operation of the school was segregated *and* involvement with the state or a political subdivision was such as to make the operation unconstitutional or a violation of the laws of the United States. The IRS may follow the same policy after a *Bakke* affirmance, substituting the operation of an affirmative action program for operation on a segregated basis.[76]

2. Prior Discrimination

Another distinguishing factor could be a showing of prior discrimination by an institution against minorities; in such a case, affirmative action would be not only permissible, but required. But the parameters of this factor are not entirely clear. The most narrow coverage would be solely *de jure* segregation, prior intentionally discriminatory acts by school officials. But the discretion of school officials to fashion affirmative remedies goes further than a federal court's power to order such remedies.[77] Thus, in the analogous case of public schools, a finding of prior *de facto* segregation in a state's educational system could be used to justify voluntary corrective action in the form of minority preferences. It might also be argued that, since the medical school at Davis is national in character, as are many professional schools today, it may take into account discrimination in various parts of the country, must of which can be documented as *de jure*. Similarly, a private school might argue that such things as qualifying exami-

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75. *But see* Runyon v. McCrary, 427 U.S. 160 (1976), which held private school segregation to be unlawful under 42 U.S.C. § 1981, enacted in part under the authority of the thirteenth amendment, which requires no state action. In *Runyon*, however, the school there had done extensive solicitation for students, and each solicitation was directed towards the general public; the Court expressly noted this fact, and withheld its opinion on whether § 1981 could be applied to reach truly private discrimination, when no public solicitation has been engaged in.

76. Note that the grant of a tax exemption in itself is probably not "state action" of the kind sufficient to invoke the fifth and fourteenth amendments; *see generally* discussion of *McGlotten*, accompanying notes 87-102 *infra*.

77. Swann v. Charlotte-Mecklenburg Bd. of Educ., 402 U.S. 1, 16 (1971).

nations with disproportionate impact on minorities, or prior discrimination elsewhere, have a continuing adverse effect on minorities, and that its affirmative action program is therefore remedial. This argument, however, may be foreclosed if the Court chooses to deal with it in its opinion.[78]

Administratively, it does appear that a *de jure* rule could be relatively simple for the IRS to follow: where a judicial determination of unlawful segregation is on the record, the implementation of remedial programs by affected institutions would not be in violation of a Supreme Court decision in favor of Bakke, and thus would not run afoul of Revenue Ruling 71-447. In the author's opinion, a *de facto* rule, assuming such would be acceptable under a decision affirming *Bakke*, need not be significantly more complex; a presumption of legality could be made, if a section 501(c)(3) organization asserts that its voluntary affirmative action plan combats *de facto* segregation. This is no different in principle from presuming that a formerly discriminatory school's assertion of nondiscrimination is made in good faith. Perhaps it is even more reasonable, given the pervasiveness of discrimination and its effects in our society. Given the facts and issues under consideration by the Court in *Bakke*, however, it is questionable whether a decision affirming the unconstitutionality of the minority admissions program in that case could be circumvented by simply admitting prior *de facto* segregation. This is in effect what the University has already done.

B. Private Educational Foundations

The analysis of Revenue Ruling 71-447, based on public policy against school segregation in both public and private schools, may not apply to private educational organizations, such as a scholarship foundation implementing minority preferences. As discussed above, an affirmance in *Bakke* might be distinguishable on the basis of the lack of state action in the case of private organizations. On the other hand, if such a distinction does not hold up, the national policy referred to in the ruling, a policy against discrimination in education, may arguably extend beyond schools, to include other educationally oriented organizations. But, in opposition to this argument, it seems evident that a minority preference exercised by a private scholarship trust does not generally foster discrimination;[79] on the contrary, it fosters integra-

78. In part, this is already at issue in *Bakke*: there have been findings of discrimination (*de jure* and *de facto*) in various parts of the California school system. Gomperts v. Chase, 404 U.S. 1237 (1971); Johnson v. San Francisco United School Dist., 339 F. Supp. 1315 (N.D. Cal. 1971), *vacated*, 500 F.2d 349 (9th Cir. 1974); Spangler v. Pasadena City Bd. of Educ., 311 F. Supp. 501 (C.D. Cal. 1970). Therefore, the Court will, to a certain extent, delineate in its opinion some of the limitations on the applicability of this factor.

79. The converse may be more difficult to argue, *i.e.*, that a private scholarship trust operating on a preferential basis for whites is consistent with exempt status under

tion, by facilitating minority enrollment where otherwise there would be little, and should not be classified as discriminatory. Because such foundations lessen prejudice and discrimination, this classification is also consistent with the "community benefit" argument in the Treasury Regulations on section 501(c)(3).

A private trust restricting its charitable beneficiaries to the members of one racial group must be considered in the light of relevant authority under the common law of charities.[80] These authorities show that trusts for certain favored purposes, including at least the relief of poverty, the advancement of religion and the advancement of education, have traditionally been regarded as having sufficient community benefit to be termed charitable notwithstanding the fact that restriction on the class of eligible beneficiaries excludes some members of the community. In the past, such permissible restrictions were commonly held to include racial restrictions, such as "for whites only." The growing trend in American law, however, has been away from the acceptance of invidious racial classifications in trusts purporting to be charitable.[81] At the very least, there is sufficient doubt cast on such racially restricted trusts that such trusts seeking tax exemptions should answer the question of whether the overall effect of the application of such restrictions is to promote fuller participation of all segments of the community in some desired good (such as higher education), or to further exclude one segment of the community to the detriment of its members. In the case of special trusts or foundations primarily or exclusively for minorities, as long as it can be shown that such restrictions are designed to promote a truly nondiscriminatory allocation of community resources to all races, the requisite community benefit would appear to be served. This conclusion should not be changed (for such trusts which are not state supported schools) even should an affirmance in Bakke result in an extension of Revenue

I.R.C. § 501(c)(3). In the most common situation, it has been minorities, not whites, who have been excluded from American institutions of higher education by prejudice, overt or covert restrictions, and economics. Unlike similar programs for minorities, which have the effect of bringing minority representation up to par, a scholarship trust or other educational program for whites only would seem to have some segregative effect with respect to minority groups. This may be the case even if the scholarship or program in question is totally independent of any educational institution, and the institution has scholarships available for minorities and for all students, and an open enrollment policy. A whites-only program that has the effect of exacerbating an existing situation of minority underrepresentation at a particular institution (especially when there has been prior discrimination by such institution) would not seem to have the community benefit typical of charitable endeavors, and would not seem to be "charitable" in the sense of an I.R.C. § 501(c)(3) exempt organzation.

80. *See* RESTATEMENT (SECOND) OF TRUSTS, § 368, comment b & §§ 369-372 (1959); BOGERT, THE LAW OF TRUSTS AND TRUSTEES § 375 (2d revised ed. 1977); IV SCOTT ON TRUSTS §§ 368, 370.6 & 399.4 (3d ed. 1967 & 1977 Cum. Supp.).

81. BOGERT, *supra* note 80 at § 375, IV SCOTT, *supra* note 80 at § 399.4; *see* the Girard College litigation, culminating with Commonwealth of Penn. v. Brown, 270 F. Supp. 782 (1967), *aff'd*, 392 F.2d 120 (3d Cir. 1968), *cert. denied*, 391 U.S. 921 (1968).

Ruling 71-447 to include affirmative action in its coverage. As indicated in our discussion above, however, private schools may not be able to distinguish the facts of their situation from those in the *Bakke* case. This could be the case with many schools receiving substantial amounts of state or federal financial assistance. In the event that the Court characterizes the minority preference in *Bakke* as unconstitutional discrimination, such a private school may be subject to a loss of its exemption under Revenue Ruling 71-447 if it operates a similar affirmative action program.

IV. Effect of Reversal By Supreme Court in Bakke

We have already discussed the possibility that the Court may find the limited minority preference at issue in *Bakke* to be permissible as a voluntary remedial device to alleviate the effects of general societal discrimination, and therefore not in violation of the fourteenth amendment. The Court may base its rationale on the line of cases permitting school authorities broad leeway in the voluntary exercise of their discretion (as opposed to the narrower limits of a court's power to order a remedy). The Court may also rely on the ameliorative (as opposed to invidious, or segregative) nature of the University's special admissions program. Such a decision could be made in the context of some degree of increased judicial scrutiny because of the racial nature of the classifications involved, either "strict scrutiny" (with the program being found to have both a "compelling purpose" and no less drastic alternative) or some lesser degree of scrutiny. Under this increased judicial scrutiny, guidelines could be developed by the Court to determine whether a particular affirmative action program was rationally designed and effectively operated to achieve its corrective purpose of ensuring more equal access to higher education for all races. Failing to meet these guidelines could disqualify a particular program if it were not designed to accomplish this purpose.

Under a decision reversing *Bakke* and upholding the University's affirmative action program within prescribed limits' Revenue Ruling 71-447 could be applied to deny charitable status to programs outside of those limits. In the author's opinion, this would not have to entail serious administrative burden for the IRS; it could employ a presumption of charitability if a school represents that its affirmative admissions program is intended for a remedial purpose, to better ensure equality of access to the school's resources. No modification of IRS procedures would be necessary; there would be no inconsistency under these circumstances.[82] In keeping with a narrow constitutional decision, however, the IRS should investigate factors indicating that a school's minority admissions policy is, in fact, not beneficial to the

82. *See* note 74 *supra*.

minority groups involved. If the program is a disguised form of segregation, or if it otherwise violates constitutional restrictions, the presumption of charitability should be overridden.

The IRS ten percent audit guidelines[83] for private schools with respect to school segregation are probably inappropriate for minority preferences. The history of such preferences is not comparable to that of school segregation, which until very recently had widespread official sanction. Due to the dangers of using racial classifications, however, the IRS would probably have to develop some examination guidelines to help protect against abuses.

V. Effect Of Non-Constitutional Decision: The Civil Rights Act

The trial court decision in *Bakke* was partially based on Title VI of the Civil Rights Act of 1964,[84] which prohibits discrimination based on race in any program receiving federal financial assistance. A decision based on Title VI would limit the extension of Revenue Ruling 71-447 to such schools or other educational organizations receiving federal funds.

The classification of tax exemptions and charitable deductions as benefits or "support" provided by the federal government raises the question of whether such favorable tax treatment constitutes federal financial assistance under Title VI. Although tax deductions are not, strictly speaking, "matching grants" or direct payments, the concept of tax "expenditures" has become so pervasive that the analogy is widely accepted.[85] The court in *Green v. Connally*, while expressly declining to decide the issue, strongly suggests that deductions and exemptions granted to racially segregated private schools may violate Title VI. As evidenced by its position in the *McGlotten* litigation, however, the IRS has apparently never accepted the characterization of tax advantages as "support," either as federal financial assistance in the Title VI sense, or "state action"[86] in the constitutional sense.

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83. *See* note 73 *supra*.

84. 42 U.S.C. § 2000d (1970) (note that further briefing by the parties on this issue was ordered by the Supreme Court after oral argument).

85. *See* Surrey, *Tax Incentives As a Device for Implementing Government Policy: A Comparison with Direct Government Expenditures*, 83 Harv. L. Rev. 705 (1970); Surrey, *Federal Income Tax Reforms: The Varied Approaches Necessary to Replace Tax Expenditures With Direct Government Assistance*, 84 Harv. L. Rev. 352 (1970); Stone, *Federal Tax Support of Charities and Other Exempt Organizations: The Need for a National Policy*, 20 S. Cal. Tax. Inst. 27 (1968).

86. The characterization of tax advantages as "state action" raises issues similar to those raised by a characterization as federal financial assistance; consequently, we will also consider the state action question in this section.

For another case concluding the tax exemptions granted to racially discriminatory organizations constituted "state action" violating the fourteenth amendment, *see* Pitts v. Department of Rev., 333 F. Supp. 662 (E.D. Wis. 1971); *but cf.* Chicago Joint Bd. Amal. Clothing Workers v. Chicago Trib. Co., 435 F.2d 470 (7th Cir. 1970), *cert.*

The government's strong opposition to this characterization was displayed in its defense in *McGlotten v. Connally*.[87] *McGlotten*, like *Green*, involved another action to enjoin Treasury officials, this time from according a tax exempt status under section 501(c)(8) to a fraternal order, the Elks Lodge, that was allegedly discriminating against blacks in its membership policies. The complaint also sought an injunction against IRS recognition of the somewhat similar exempt status section 501(c)(7) provides for social clubs, when such a club engages in racially discriminatory practices. The court concluded that the allowance of tax exemptions for fraternal orders amounts to the provision of a matching grant by the federal government, and must be deemed to be unconstitutional government entanglement in racial discrimination.[88] The court also found that allowing tax deductions for contributions to fraternal orders discriminating against non-whites would violate the federal policy that the "beneficiaries of federal largesse should not discriminate," and that such allowance would represent "federal financial assistance" to a discriminatory organization within the meaning of Title VI.[89]

It does not appear, under the rationale of the *McGlotten* court, that all exemptions, deductions or favorable tax treatment for particular qualifying organizations would unqualifiedly constitute federal governmental "support." *McGlotten* used a "weighing and balancing" test derived from a leading state action case,[90] to measure the amount of governmental involvement caused by the particular code section in question. The court noted that certain deductions are derived merely from the Congressional policy of taxing net rather than gross income.[91] Some code sections advantageous to qualifying taxpayers

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denied, 402 U.S. 973 (1971) (state use tax exemption for newspapers held not significant state action).

87. 338 F. Supp. 448 (D.D.C. 1972).

88. On the other hand, the *McGlotten* court further concluded that there was neither state sanction of discrimination nor any grant of federal financial assistance under Title VI in granting exemptions under I.R.C. § 501(c)(7) to nonprofit social clubs in view of the fact that such organizations, in the court's view, derive only insubstantial benefits from their tax exempt status under I.R.C. § 501(c)(7). The legislative history of the predecessor of § 501(c)(7) indicates that Congress included social clubs in the category of exempt corporations, fraternal benefit orders and other organizations exempt from tax because administratively it was not worth it to tax them:

> The experience of the Treasury Department has been that the securing of returns from them has been a source of expense and annoyance and has resulted in the collection of either no tax or an amount which is practically negligible.

H.R. REP. NO. 922, 64th Cong., 1st Sess. 4 (1916).

One additional fact to be noted about § 501(c)(7) social clubs is that they will now fail to qualify for exemption if the governing instrument contains a provision discriminating on the basis of race, color or religion. This is embodied in I.R.C. § 501(h), passed in the Tax Reform Act of 1976, presumably in response to the *McGlotten* case.

89. 338 F. Supp. at 462.

90. Burton v. Wilmington Parking Auth., 365 U.S. 715 (1961).

91. *E.g.*, I.R.C. §§ 162 & 212, the expense deduction sections.

represent incentives to achieve specific objectives, but are generalized as to the type of taxpayer involved.[92] The *McGlotten* court found a government *imprimatur* only where a specific type of *organization* was singled out as serving some policy endorsed by the federal government.[93]

The concept of tax advantages constituting federal "support" may be somewhat moderated in its scope by subsequent judicial interpretation. *McCoy v. Schultz*[94] lends support to this proposition. In a challenge to the granting of tax exemptions to organizations practicing sex discrimination, the court, in dismissing plaintiff's action, stated that section 501(c)(3) is broad and generalized and does not imply any federal "seal of approval" on any particular kind of (discriminatory) organization claiming exemption under that section.

The above-mentioned conclusions in *McGlotten* were announced in support of the court's denial of a general defense motion to dismiss and have not yet been used as the basis for any final decree. As the decree was only an interlocutory order, the government probably decided not to appeal, at least until after the order became merged into a final judgment. The fraternal organization involved in the case subsequently changed its racially exclusive policy, and appears to be currently admitting black members. It is thus doubtful that *McGlotten* will ever be the vehicle for a final judgment on the basic issues initially raised in that case.[95]

In any event, it is clear that the IRS' position as argued in the *McGlotten* case is contrary to the court's general characterization of tax exemptions and deductions as "federal financial assistance." The current ruling position of the IRS, because it relies on a definition of the concept of charitability rather than directly relying on Title VI or the fourteenth amendment, rests on a foundation that is substantially different from that on which the above-described conclusions of the *Green* and *McGlotten* courts are bottomed.[96]

With regard to the government support issue, there are also some indications from certain Supreme Court cases that tax benefits may be below the threshold level at which government benefits begin to make out a case for "state action" or any other kind of support. In *Walz v. Tax Commissioner*,[97] a case dealing with the allowability of tax exemptions to religious organizations under the first amendment's Anti-Establishment Clause, the Supreme Court declined to characterize

92. *E.g.*, deduction of mortgage interest under I.R.C. § 163.
93. 338 F. Supp. at 456.
94. Civ. No. 1580-72 (D.D.C. 1973), 73-1 U.S. TAX CASES 80,423 (decided in the same district as *McGlotten*, but by a different judge).
95. A memorandum suggesting mootness has been on file with the court since October 15, 1977.
96. *See* discussion in text accompanying notes 30-34 *supra*.
97. 397 U.S. 664 (1970).

state tax exemptions as state action. The Court conceded that granting tax exemptions to churches necessarily operates to afford an indirect economic benefit, but called it a "minimal and remote involvement," albeit under the first and not the fourteenth amendment.[98] As the Court indicated in *Moose Lodge v. Irvis*,[99] not every benefit from the state constitutes support. The Court held the benefit in that case to be an insufficient basis for characterizing the racially discriminatory operation of the fraternal order there in question as a violation of the Equal Protection Clause by the state. Although the state liquor license there in question was undoubtedly of substantial value to the discriminatory licensee, the Court was unwilling to held that the utilization of such a license made the fraternal order's exclusion of blacks as members or guests the equivalent of such exclusion by the state.

If tax benefits themselves are not held to be federal financial assistance under Title VI, an affirmance in *Bakke* based on the Civil Rights Act would apply only to schools receiving federal aid. This result, while not applying to institutions fully independent of such aid, would apply without regard to whether a school is public or private. Because of the extensive role that federal aid plays in contemporary higher education,[100] a decision based on Title VI would be particularly far-reaching. Under such a decision, the IRS would face probable extension of Revenue Ruling 71-447 to encompass those educational institutions receiving federal funds[101] and claiming exempt status under section 501(c)(3).

Conclusions

There are many alternatives open to the Court to avoid a broad constitutional decision in *Bakke*. It is this author's opinion, however, that avoidance of the constitutional issues would only breed further confusion and lead to more litigation. *Bakke* is *DeFunis* the second time around; with the wide split in authority on affirmative action, there will be a third time, and, without guidance, the decisions in the interim will be haphazard. A holding based solely on the Civil Rights Act would not resolve the basic issues, because it would only beg the question of the treatment of remedial programs when federal funds are not at stake. This is illustrated particularly well by the issue we have considered in this article: if the Supreme Court holds for Respondent Bakke on the Title VI ground alone, does this constitute a sufficient change in the national public policy to demonstrate that affirmative action is in violation of such policy across the board (even where there

98. *Id.* at 675-76.
99. 407 U.S. 163 (1972).
100. *E.g.*, federal student loans, federal work study programs, etc.
101. But this result might also apply to nonfederally-funded institutions; *see* Conclusions section, below.

is no federal financial assistance), or only where Title VI literally applies? The answer to this query is problematical, and it appears certain that a nonconstitutional decision would leave this and many other questions unanswered.

Whatever the decision in *Bakke*, the IRS policy will be affected. The Service's current position appears to allow some remedial minority preferences,[102] and generally has not classified such preferences as discrimination. But *Bakke* will be a new statement of national policy on the question of discrimination in education. If the California Supreme Court is affirmed in its holding that Davis' special minority admissions program is impermissible reverse discrimination, the IRS will have to reconsider its position to take account of this change in national policy. We noted earlier that the potential repercussions of such a change could affect institutions other than schools, such as private foundations administering minority scholarships. The latter possess certain distinguishing features, however, which could possibly insulate them from the full effects of adverse consequences of a *Bakke* affirmance.

This author believes that any extension of Ruling 71-447 to accomodate a new declaration of national policy under a *Bakke* decision should be implemented by the IRS with a general view towards disturbing the tax exempt status of institutions with affirmative programs as little as possible within the limits of the Supreme Court's holding. Thus, unless an organization were clearly shown[103] to be within the scope of a *Bakke* affirmance,[104] a presumption that an ameliorative, minority-sensitive program operated by such an organization is nondiscriminatory should prevail. Such a policy recommends itself, because voluntary action to achieve integration, to effect more equal access of all races to desired benefits in society, serves a community benefit and can thus be considered charitable in the common law sense. Another justification for such an IRS policy is that the Service's adminstration of its anti-discrimination policy to revoke charitable exemptions should not be more stringent in the case of remedial action seeking integration than in the case of segregationist actions.[105]

Any decision in *Bakke* will be an important and a difficult one. It is hoped that, because of the extensive ramifications of such a decision, both the Court and those affected by the Court's holding will consider

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102. On the other hand, the IRS requires no such preferences of all-white schools in order to demonstrate their nondiscriminatory policies.

103. Thus, if some distinguishing feature existed to differentiate an institution or its affirmative action program from those in the *Bakke* case, a holding in *Bakke* against "reverse discrimination" should not apply, and the exempt status of such institution should remain unrevoked.

104. *See* the distinguishing factors discussed in text accompanying notes 75-82 *supra*.

105. *See* discussion on IRS enforcement procedures, in text accompanying notes 71-73 *supra*.

all of the equities and make the wisest choice. But whatever the decision it is this author's sincere hope that the possibility of voluntary social change designed to help rectify prior social injustice will not be foreclosed. True integration, in terms of real access and opportunities, is indeed a compelling national purpose, one that will not and cannot wait.