

# TAXING CULTURAL ENDOWMENTS

## INTRODUCTION

On February 5, 2019, the Museum of Modern Art (MoMA) in New York announced that it had received the largest donation in its ninety-year history: a \$200 million gift from the estate of David Rockefeller, the grandson of oil magnate John D. Rockefeller.<sup>1</sup> Rockefeller was a tremendous steward of the MoMA not only at death, but also during his life. He served on the museum's Board of Trustees for nearly seventy years<sup>2</sup> and made several landmark gifts of cash and art<sup>3</sup> to the museum, including a \$100 million gift in 2005.<sup>4</sup> During Rockefeller's most active years supporting the MoMA, the museum's endowment<sup>5</sup> grew from \$324 million in 2009 to \$1.2 *billion* in 2019.<sup>6</sup>

The story of Rockefeller's philanthropy and the MoMA's financial growth points to a trend in America's cultural sector: a surge in the value of elite cultural institutions' endowments.<sup>7</sup> The largest cultural institutions in America currently boast endowed funds that exceed \$1 billion.<sup>8</sup> These include the Metropolitan Museum of Art, whose endowment has nearly

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1. See Press Release, Museum of Mod. Art, The Museum of Modern Art Announces More Than \$200 Million Bequest from the Estate of David Rockefeller (Feb. 5, 2019), [https://press.moma.org/wp-content/uploads/2019/02/7\\_MoMA\\_DavidRockefeller\\_February2019PressRelease\\_FINAL.pdf](https://press.moma.org/wp-content/uploads/2019/02/7_MoMA_DavidRockefeller_February2019PressRelease_FINAL.pdf) [<https://perma.cc/5J8M-ZRX5>].

2. See *id.*

3. See *id.*

4. See Press Release, Museum of Mod. Art, David Rockefeller Pledges \$100 Million to the Museum of Modern Art: Largest Monetary Gift in MoMA's History Will Support Endowment (Apr. 13, 2005), [https://press.moma.org/wp-content/press-archives/PRESS\\_RELEASE\\_ARCHIVE/Rockefeller\\_Pledge.pdf](https://press.moma.org/wp-content/press-archives/PRESS_RELEASE_ARCHIVE/Rockefeller_Pledge.pdf) [<https://perma.cc/PZ2G-VSSF>].

5. This Note uses the term "endowment" to refer to the entirety of a charity's passive investments—that is, not only donor-restricted funds and contributions to an existing endowment, but also the revenue and unrestricted donations that a charity chooses to invest. This definition of "endowment" mirrors that used by David M. Schizer in *Charitable Subsidies and Nonprofit Governance: Comparing the Charitable Deduction with the Exemption for Endowment Income*, 71 TAX L. REV. 665, 685 n.49 (2018) ("Operating charities can accumulate investment assets in three ways. First, donors can require the charity to invest their gift, allowing the charity to keep the principal and spend only the income. Second, the charity itself can create the endowment, inviting donors to contribute to it and committing to spend only the income. Third, a charity that earns more than it spends can choose to invest this surplus. Technically, the term 'endowment' refers only to the first and second of these choices, and the third is usually called a 'quasi-endowment.' However, this Article uses the term 'endowment' to describe all three . . .").

6. See Museum of Modern Art, *Full Text of "Form 990, Schedule D" for Fiscal Year Ending June 2019*, PROPUBLICA, <https://projects.propublica.org/nonprofits/organizations/131624100/202041959349303519/IRS990ScheduleD> [<https://perma.cc/4L2T-TW3A>].

7. This Note uses the phrase "elite cultural institutions" to refer to the most well-endowed cultural institutions in America. See *infra* Appendix A for a list of cultural institutions with endowments valued at over \$200 million.

8. See *infra* Appendix A.

doubled in size in the past decade<sup>9</sup> growing to \$4.22 billion in 2023,<sup>10</sup> and the Smithsonian Institution,<sup>11</sup> which in 2022 had a \$2.32 billion endowment,<sup>12</sup> up from \$1 billion in 2012.<sup>13</sup> The largest performing arts and historical preservation organizations, while generally smaller than museums, also have substantial endowments. The Colonial Williamsburg Foundation's endowment, for example, was recently valued at \$712 million.<sup>14</sup>

Scholars have long criticized charitable endowment growth and proposed policies to curb it. In 1999, Professor Evelyn Brody proposed that Congress “adopt a low-level investment tax to offset charities’ incentive to save,” noting that “by existing at the periphery of the tax system, charities quietly have garnered billions of dollars.”<sup>15</sup> Over a decade later, Professor Daniel Halperin echoed Brody’s support for a tax on investment income.<sup>16</sup>

9. The Metropolitan Museum of Art’s endowment was valued at \$2.37 billion in Fiscal Year (FY) 2013. See Metropolitan Museum of Art, *Full Text of “Form 990, Schedule D” for Fiscal Year Ending June 2014*, PROPUBLICA, <https://projects.propublica.org/nonprofits/organizations/131624086/201540409349300819/IRS990ScheduleD> [https://perma.cc/P9VM-DESU].

10. See Metropolitan Museum of Art, *Full Text of “Form 990, Schedule D” for Fiscal Year Ending June 2023*, PROPUBLICA, <https://projects.propublica.org/nonprofits/organizations/131624086/202410469349300531/IRS990ScheduleD> [https://perma.cc/2WHG-LKM3].

11. The Smithsonian Institution has a unique organizational structure, in that it combines elements of a federal institution and a public charity. Most of its funding comes from the federal government. But the Smithsonian also actively solicits and receives private donations, grants, and other forms of private support. Because it is a trust instrumentality of the United States, meaning that it operates independently of the government in its ability to receive and manage private funds, the organization’s endowment is still relevant to this Note. See generally *Legal History*, SMITHSONIAN INST., <https://www.si.edu/ogc/legalhistory> [https://perma.cc/L26U-3Q36].

12. See Smithsonian Institute, *Full Text of “Form 990, Schedule D” for Fiscal Year Ending Sept. 2022*, PROPUBLICA, <https://projects.propublica.org/nonprofits/organizations/530206027/202302269349301205/IRS990ScheduleD> [https://perma.cc/65LF-873F].

13. See Smithsonian Institute, *Form 990 for Period Ending September 2012*, PROPUBLICA, [https://projects.propublica.org/nonprofits/display\\_990/530206027/2013\\_09\\_EO%2F53-0206027\\_990\\_201209](https://projects.propublica.org/nonprofits/display_990/530206027/2013_09_EO%2F53-0206027_990_201209) [https://perma.cc/UF2W-28D2].

14. See Colonial Williamsburg Foundation, *Full Text of “Form 990, Schedule D” for Fiscal Year Ending Dec. 2022*, PROPUBLICA, <https://projects.propublica.org/nonprofits/organizations/540505888/202323179349302897/IRS990ScheduleD> [https://perma.cc/M9RV-PNX8]. See *infra* Appendix A for examples of other sizeable cultural endowments.

15. Evelyn Brody, *Charities in Tax Reform: Threats to Subsidies Overt and Covert*, 66 TENN. L. REV. 687, 693 (1999).

16. See Daniel Halperin, *Tax Policy and Endowments – Is Excessive Accumulation Subsidized?*, TAXNOTES (Jan. 1, 2011), <https://www.taxnotes.com/exempt-organizations/exempt-organizations/tax-policy-and-endowments-excessive-accumulation-subsidized/2011/01/01/lysz?highlight=tax%20policy%20and%20endowments%20halperin> [https://perma.cc/4LF7-ZDK5] (“I believe that an unlimited subsidy for charitable accumulation is not an efficient and equitable use of limited government resources. . . . [T]here appears to be a tendency, or at least a desire, toward increasing the shares of budgets provided from endowments, apparently to increase the competitive advantage of richer institutions, which again does not appear to reflect the public interest.”); see also Daniel Halperin, *Tax Policy and Endowments – Is Excessive Accumulation Subsidized? (Part II)*, TAXNOTES (Feb. 1, 2011) [hereinafter Halperin, *Tax Policy and Endowments (Part II)*], <https://www.taxnotes.com/exempt-organizations/charitable-giving/tax-policy-and-endowments-excessive-accumulation-subsidized-part>

He concluded that endowment growth did not serve the public interest and suggested several options for policy reform, including limiting the deduction available for restricted gifts.<sup>17</sup> Other scholars have suggested more extreme measures. In 2015, Professor Michael Fricke called for the complete eradication of the charitable tax exemption; in defense of this position, he remarked that “the wealthiest nonprofits in this country . . . stock [their] profits away, building endowments seemingly simply for the sake of having a large endowment.”<sup>18</sup>

In recent decades, Congress has echoed these concerns, affording particular attention to university endowments. In 2008, the Senate Finance Committee launched an investigation into university endowment spending policies.<sup>19</sup> The investigation aimed to draw attention to colleges’ growing endowments, particularly as tuition prices rose: “It’s fair to ask whether a college kid should have to wash dishes in the dining hall to pay his tuition when his college has a billion dollars in the bank,” Senator Grassley commented.<sup>20</sup> The debate over university endowments reached an apex in 2017, when Congress enacted a 1.4% excise tax on private universities’ investment income.<sup>21</sup> The tax, now codified as Section 4968 of the Internal Revenue Code (“the Code”), marked the first time in history that Congress had placed an excise tax on a public charity.<sup>22</sup>

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-ii/2011/02/01/lyw9? [https://perma.cc/HQX8-J69Y] (“[T]he issue is whether a bias toward current spending is desirable. I suggest that it is. . . . One possibility is to require a minimum distribution from public charity endowments as is now required from private foundations. Because a mandate could be intrusive and not necessarily very effective, it is not desirable. I suggest, instead, a tailored tax on investment income, perhaps to encourage current spending, but in any event to reduce the tax subsidy for excessive accumulation. For efficiency reasons, it could be preferable if the tax were a percentage of assets rather than income. Also, the limit on the charitable deduction for at least some gifts to endowments should be reduced at least to the level applicable to gifts to private foundations. Finally, the limitations on tax-exempt financing and the taxation of debt-financed income should be reexamined.”).

17. See Halperin, *Tax Policy and Endowments (Part II)*, *supra* note 16.

18. Michael Fricke, *The Case Against Income Tax Exemption for Nonprofits*, 89 ST. JOHN’S L. REV. 1129, 1158 (2015).

19. Press Release, U.S. Senate Comm. on Fin., Baucus, Grassley Write to 136 Colleges, Seek Details of Endowment Pay-Outs, Student Aid (Jan. 24, 2008), <https://www.finance.senate.gov/release/baucus-grassley-write-to-136-colleges-seek-details-of-endowment-pay-outs-student-aid> [https://perma.cc/2ZW9-NDW9].

20. *Id.*

21. Only private universities with at least five hundred tuition-paying students and total assets of at least \$500,000 per student are subject to the investment tax. I.R.C. § 4968 (West). Since 2017, some Republicans have proposed increasing the excise tax from 1.4% to as high as 35%. See Samantha Handler, *Universities Fear Endowment Tax Hike Amid Congressional Heat*, BLOOMBERG TAX (June 20, 2024, 3:45 AM), <https://news.bloombergtax.com/daily-tax-report/universities-fear-endowment-tax-hike-amid-congressional-heat> [https://perma.cc/KDH9-2RDV]. Section 4968 defines “net investment income” as the amount by which the sum of an organization’s gross investment income (i.e., income from interest, dividends, rents, royalties, and similar sources) and capital gain net income exceeds allowable deductions. See 26 C.F.R. § 53.4968-2 (2024).

22. See Jennifer Bird-Pollan, *Taxing the Ivory Tower: Evaluating the Excise Tax on University Endowments*, 48 PEPP. L. REV. 1055, 1057 (2021).

Since 2017, some have called for Section 4968 to encompass *all* endowed charities. Professor Edward Zelinsky, for example, has argued that all sizeable endowments, not just university endowments, should fall under Section 4968's umbrella.<sup>23</sup> Zelinsky's proposal rests on the notion of tax fairness,<sup>24</sup> or the idea that similarly situated entities should receive similar tax treatment. Craig Kennedy, a senior fellow at the *Giving Review* and the former president of the Joyce Foundation, advanced a similar argument in the *Chronicle of Philanthropy* in 2023.<sup>25</sup> Reaching beyond Section 4968, Kennedy argued that Congress should subject all "large, endowed institutions" to the rules governing private foundations,<sup>26</sup> including the minimum distribution requirement<sup>27</sup> and the limited deduction for donors.<sup>28</sup>

These proposals, while implicating *all* endowed charities, focus near-exclusively in their rationale on concerns surrounding endowed universities and hospitals, with little regard given to cultural institutions. They acknowledge potential motivations for taxing university endowments, nonprofit hospitals, and donor advised funds,<sup>29</sup> yet fail to identify the deleterious effects of cultural endowment growth.<sup>30</sup> Should these proposals make headway, someone will need to answer the question: what is the rationale for taxing our cultural sector?

This Note answers that question. More specifically, it contributes to the academic discourse on endowment taxation a detailed examination of cultural endowments, the tax policies that shape them, and the problems that arise from their growth. The Note begins with the laws and regulations that shape cultural organizations and their endowments. While this section focuses on the tax treatment of cultural institutions, it also includes a brief

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23. See Edward A. Zelinsky, *Section 4968 and Taxing All Charitable Endowments: A Critique and a Proposal*, 38 VA. TAX REV. 141, 143 (2018).

24. See LIAM MURPHY & THOMAS NAGEL, *THE MYTH OF OWNERSHIP: TAXES AND JUSTICE* 12 (2002) ("Fairness, in the traditional conception, is thought of specifically as a standard for evaluating differences in the tax treatment of different people: the principle that like-situated persons must be burdened equally and relevantly unlike persons unequally.").

25. See Craig Kennedy, Opinion, *J.D. Vance Had a Point: Let's Rein in All Large Endowed Institutions*, CHRON. PHILANTHROPY (Sept. 14, 2023), <https://www.philanthropy.com/article/j-d-vance-had-a-point-lets-rein-in-all-large-endowed-institutions> [<https://perma.cc/4GEF-UBXA>].

26. *Id.*

27. Private foundations are required to distribute annually at least 5% of the fair market value of their non-charitable use assets for charitable purposes. See I.R.C. § 4942.

28. Donations to private foundations are generally deductible up to 30% of the donor's adjusted gross income (AGI), compared to 50% for public charities. See I.R.C. § 170.

29. See Zelinsky, *supra* note 23, at 142; see also Kennedy, *supra* note 25.

30. Craig Kennedy's article briefly mentions cultural institutions. See Kennedy, *supra* note 25 ("Museums and other cultural institutions have seen a sharp rise in assets as well, according to audited financial statements and annual reports. The Metropolitan Museum of Art had \$2.3 billion in assets in 2010. Today, the institution's investments total \$4.7 billion. The New York Philharmonic's endowment grew from less than \$166 million in 2010 to more than \$241 million in 2021, despite declining attendance and other challenges."). However, this brief discussion fails to offer a justification for altering museum endowment taxation.

discussion of the Uniform Prudential Management of Institutional Funds Act (UPMIFA), an act that offers guidance on investment decisions and endowment expenditures for nonprofit organizations. This legal background is followed by a brief discussion of the rationale of cultural endowments (i.e., why an organization might choose to reinvest, rather than spend, its investment income). Part III of this Note identifies the problems that arise from cultural endowment growth. The Note argues that growth (1) occurs at the expense of charitable spending, (2) shields organizations from public accountability, and (3) produces a concentration of wealth among elite institutions that results in unfair competition over philanthropic dollars and diminishes cultural pluralism. Part IV then briefly evaluates the capacity of select tax policy proposals to mitigate these harms.

In conclusion, the Note argues that cultural endowment growth causes distinct harms that *can* and *should* be mitigated through measured tax reform. To alter the tax treatment of elite cultural institutions, without impacting organizations that are similarly sized but relatively small within their respective subsectors (e.g., smaller universities and smaller nonprofit hospitals), I argue, for the first time in legal literature, that Congress should define the taxable base of future endowment tax reforms on a subsector-by-subsector basis.<sup>31</sup> In other words, the taxable base for an excise tax on or minimum distribution requirement for public charities should differ between the university subsector, the cultural subsector, and so on, due to those subsectors' differently sized economies. Part IV of this Note details this proposal, including which tools might be used to define charitable subsectors. This discussion services the article's broader argument—that Congress should alter the tax treatment of elite cultural institutions—by resolving how taxing cultural endowments, which are generally smaller than university and hospital endowments, can be achieved in an equitable manner.

This Note uses the term “cultural sector” to refer to public charities dedicated to creating, preserving, and promoting cultural and artistic expressions. Examples of such organizations include opera companies, university presses, art and history museums, botanical gardens, theaters, and symphony orchestras. I intentionally exclude both for-profit corporate entities and private non-operating foundations, even though many cultural organizations operate under those forms for tax purposes, because the policy reforms discussed in this Note would not apply to those organizations. In Part IV of this Note, I explicitly define the cultural subsector using the National Taxonomy of Exempt Entities (NTEE) system, which includes a

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31. Taxable base refers to the individuals or institutions that are subject to a specific provision of the Internal Revenue Code. Often this group is defined based on their income or net assets.

category for “Arts, Culture, and Humanities” organizations.<sup>32</sup> Because all exempt organizations are placed within the NTEE classification system upon approval for tax exemption,<sup>33</sup> the system can prove useful for sorting charitable organizations.

Legal scholars, particularly those who research exempt organizations and philanthropy, should attend to America’s cultural sector, for several reasons.<sup>34</sup> First, cultural philanthropy constitutes a noteworthy and sizeable part of America’s charitable economy. In 2022, America’s nonprofit arts and culture industry “generated \$151.7 billion in economic activity,”<sup>35</sup> and donations to arts, culture, and the humanities represented five percent of all charitable giving.<sup>36</sup> To overlook the cultural sector is therefore to neglect a significant facet of America’s charitable economy. Second, from a practical perspective, any policymaker that proposes to alter the tax treatment of *all* public charities, including arts organizations, will need to account for opposition from cultural advocates. Should a proposal affect the tax treatment of arts organizations, cultural administrators and philanthropists will almost certainly ask: why modify the tax benefits long afforded to our nation’s orchestras, theaters, and museums? This Note offers answers to this question. But space remains to respond and to advance further rationales. Finally, unique policy considerations appear at the intersection of culture and exempt organization law. Tastes, individual preferences, and social aspirations motivate giving in distinct ways in the cultural sector, leading certain “highbrow” artistic activities to thrive,<sup>37</sup> while other cultural

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32. See Deondre’ Jones, *National Taxonomy of Exempt Entities (NTEE) Codes*, URB. INST. NAT’L CTR. FOR CHARITABLE STAT. (Apr. 2, 2019), <https://urbaninstitute.github.io/nccs-legacy/ntee/nTEE-history.html> [<https://perma.cc/3R54-BY8U>].

33. See INTERNAL REVENUE SERV., CAT. NO. 17132Z, INSTRUCTIONS FOR FORM 1023 (2020).

34. Endowed cultural institutions have received some attention in tax-focused scholarship. However, scholars have typically treated these institutions as a metonym for institutional “elitism” in America’s charitable sector. Mention of cultural institutions most often arises in a discussion of which activities and organizations the government should or should not subsidize through tax exemptions and charitable deductions, rather than how Congress might modify their tax treatment. See generally John Stanton-Ife, *Must We Pay for the British Museum? Taxation and the Harm Principle*, in PHILOSOPHICAL FOUNDATIONS OF TAX LAW 35 (Monica Bhandari ed., 2017); see generally Miranda Perry Fleischer, *How Is the Opera Like a Soup Kitchen?*, in PHILOSOPHICAL FOUNDATIONS OF TAX LAW, *supra*, at 255.

35. See *What Is Arts & Economic Prosperity 6?*, AMS. FOR ARTS, <https://aep6.americansforthearts.org/> [<https://perma.cc/3L43-XEPV>].

36. See *Giving USA: Total U.S. Charitable Giving Declined in 2022 to \$499.33 Billion Following Two Years of Record Generosity*, IND. UNIV. INDIANAPOLIS LILLY FAM. SCH. OF PHILANTHROPY (June 20, 2023), [https://philanthropy.iupui.edu/news-events/news/\\_news/2023/giving-usa-total-us-charitable-giving-declined-in-2022-to-49933-billion-following-two-years-of-record-generosity.html](https://philanthropy.iupui.edu/news-events/news/_news/2023/giving-usa-total-us-charitable-giving-declined-in-2022-to-49933-billion-following-two-years-of-record-generosity.html) [<https://perma.cc/RM74-TJRP>].

37. I use the term “highbrow” throughout this Note to refer to cultural forms that have historically been seen as more refined, sophisticated, and intellectually demanding and elevated above popular or folk culture (e.g., fine art, classical music, literature). I borrow this definition from Lawrence Levine. See generally LAWRENCE W. LEVINE, *HIGHBROW / LOWBROW: THE EMERGENCE OF CULTURAL HIERARCHY IN AMERICA* (1988).

organizations, often those that serve Black and indigenous communities, carry on under-resourced. Understanding these dynamics, both how they can and historically have played out, allows us to reform the tax treatment of cultural organizations so as to better encourage pluralism of artistic activity.

### I. THE LAW AND RATIONALE OF CULTURAL ENDOWMENTS

Many American museums and performing arts institutions are organized as tax-exempt organizations under Section 501(c)(3) of the Code.<sup>38</sup> This status allows them to receive donations, which the donor may deduct from their taxes,<sup>39</sup> and to invest and grow their endowments without paying federal income tax on either source of revenue.<sup>40</sup> Take, for example, a notorious, fictional benefactor of the arts: Frasier Crane. When Frasier donates \$1 million to the Seattle Opera, the Code permits Frasier to report that charitable contribution as a personal deduction against his adjusted gross income<sup>41</sup> and the Seattle Opera to collect Frasier's gift free of taxation.<sup>42</sup> Furthermore, when the Seattle Opera invests Frasier's \$1 million gift and later collects interest on the gift principal, it does so without incurring taxation.<sup>43</sup>

This Note focuses not on the comprehensive tax treatment of cultural institutions as exempt organizations, but rather on the legal status of their endowments. This Part provides the background necessary to comprehend that legal status. The Part begins by defining the term "endowment." It then

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38. I.R.C. § 501(c)(3).

39. I.R.C. § 170(c)(2)(D).

40. I.R.C. § 501(c)(3). Many cultural institutions are categorized as "public charities." Since the adoption of the Tax Reform Act of 1969, Section 501(c)(3) of the Internal Revenue Code has distinguished between two types of tax-exempt organizations: public charities and private foundations. Tax Reform Act of 1969, Pub. L. No. 91-172, 83 Stat. 487. Public charities are "public" in nature because they are funded by a broad range of donors. See Philip Hackney, *The 1969 Tax Reform Act and Charities: Fifty Years Later*, 17 PITT. TAX REV. 235, 237 (2020). Private foundations, on the other hand, are usually funded by a single source or a small group of individuals, most often a family. *Id.* Public charities generally provide *direct* public benefit through their programs and services, whereas private foundations most often provide *indirect* charitable support by way of grant-making. The distinction between public charities and private foundations appears not only in their institutional character but also the treatment afforded to them by the Code. See generally James J. Fishman, *The Private Foundation Rules at Fifty: How Did We Get Them and Do They Meet Current Needs?*, 17 PITT. TAX REV. 247 (2020). While not the focus of this Note, it is important to acknowledge that some cultural institutions (e.g., the Getty Museum in Los Angeles) exist as private foundations. These organizations are designated as private *operating* foundations, a type of private foundation that receives funds from a limited number of donors but, like public charities, engages in activities that extend beyond grant-making and serve a charitable or educational purpose. See I.R.C. § 170(b)(1); see also Khrista McCarden, *Private Operating Foundation Reform and J. Paul Getty*, 17 PITT. TAX REV. 387, 387 (2020) (explaining the difference between private *non-operating* and private *operating* foundations).

41. I.R.C. § 170(c)(2).

42. I.R.C. § 501(c)(3).

43. I.R.C. § 501(c)(3).

discusses the regulation of cultural endowments and their investment practices, looking particularly to the Uniform Prudent Management of Institutional Funds Act (UPMIFA). While reform of UPMIFA is not a focus of this Note, the Act nonetheless deserves brief attention, as it shapes the legal boundaries of endowment investment and spending. Finally, this Part examines a select few of the established rationales for endowments, or why a cultural organization might choose to invest, rather than spend, its investment income. In doing so, I highlight how the law and industry standards encourage endowment growth and, in the case of UPMIFA, limit the percentage of endowment funds Congress can require charities to distribute on an annual basis.

#### A. Definition of an Endowment

The term “endowment” has assumed both a legal and popular definition. Colloquially, the term is often used to refer to an organization’s portfolio of investments, whether donor-restricted or not.<sup>44</sup> Legally, however, the term “endowment” refers only to a charity’s donor-restricted funds. The Uniform Management of Institutional Funds Act (UMIFA), for example, defines an endowment as “an institutional fund, or any part thereof, not wholly expendable by the institution on a current basis under the terms of the applicable gift instrument.”<sup>45</sup> In other words, Frasier’s \$1 million gift to the Seattle Opera does not contribute to the organization’s endowment by default. The gift only becomes part of the endowment if Frasier explicitly stipulates that Seattle Opera invest the gift and spend only the income earned on it.<sup>46</sup>

The Metropolitan Museum of Art’s 2022–23 Financial Statements provide an illustrative breakdown of a paradigmatic endowment.<sup>47</sup> According to the report, the Met’s portfolio of passive investments was valued at \$4.87 billion in 2023.<sup>48</sup> The majority of these funds, \$4.65 billion, were held in the Met’s long-term portfolio and allocated between a diverse set of investments, including short-term investments, equities, hedge funds, private equity funds, and real asset funds.<sup>49</sup> The remaining assets were held

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44. As a reminder, this Note adopts the broader of these two definitions. *See supra* note 5.

45. UNIF. MGMT. OF INSTITUTIONAL FUNDS ACT § 1(3) (NAT’L CONF. OF COMM’RS ON UNIF. STATE L. 1972).

46. An institution can also choose to treat unrestricted capital gifts as endowment. Practitioners refer to this as a “quasi-endowment.” Self-restricted funds may be spent at any time by an institution.

47. PRICEWATERHOUSECOOPERS LLP, THE METROPOLITAN MUSEUM OF ART: FINANCIAL STATEMENTS FOR THE YEARS ENDED JUNE 30, 2023 AND 2022 (2023), <https://cdn.sanity.io/files/cctd4ker/production/aa954d8cda489bfd5e50572bfbbd81af5180851.pdf> [https://perma.cc/ZE55-6B3G].

48. *Id.* at 12.

49. *Id.*

for capital projects and other miscellaneous purposes.<sup>50</sup> The report further indicates that the Met experienced a \$249 million return on its investments in 2023; of these returns, \$161 million were donor-restricted and \$87 million were not.<sup>51</sup> While the report does not specify whether these funds were passage of time or purpose restricted,<sup>52</sup> it later lists several categories of purposes donors have stipulated the Met put their gifts toward, including art acquisitions and book purchases, education and public programs, and exhibitions and publications.<sup>53</sup>

### *B. Regulation of Endowment Investing*

One notable law that regulates charitable endowments is UPMIFA. Promulgated by the National Conference of Commissioners on Uniform State Laws in 2006, UPMIFA provides guidelines for the management and spending of endowment funds.<sup>54</sup> While UPMIFA is a uniform law and therefore carries no legal authority on its own, forty-nine states have adopted its provisions,<sup>55</sup> so it applies to the majority of nonprofit investment activity in the United States.

UPMIFA only applies to a nonprofit's management of its endowed or donor-restricted funds.<sup>56</sup> As previously discussed, donors can instruct a charity to hold their donated funds "as an endowment" or to spend only the income earned on their gift. In these instances, UPMIFA provides a rule of construction that the donor's written agreement creates an endowment fund, subject to the spending rules of the Act.<sup>57</sup>

The Act's spending rule provides that a person responsible for managing and investing institutional funds has a fiduciary duty to do so with

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50. The Met held \$197 million for capital projects and \$26 million held for other purposes in 2023. *Id.*

51. *Id.* at 17.

52. A passage of time restriction designates funds as "off-limits" for a period of time, often perpetuity. A purpose restriction allocates funds to a specific use. See Roger Colinvau, *Strings Are Attached: Shining a Spotlight on the Hidden Subsidy for Perpetual Donor Limits on Gifts*, 56 LOY. L.A. L. REV. 1169, 1174–77 (2023) (outlining types of donor limits).

53. PRICEWATERHOUSECOOPERS LLP, *supra* note 47, at 26.

54. The National Conference of Commissioners on Uniform State Laws promulgated UPMIFA to replace the Uniform Management of Institutional Funds Act (UMIFA). See Rachel M. Williams, *Transitioning from UMIFA to UPMIFA: How the Promulgation of the Uniform Prudent Management of Institutional Funds Act Will Affect Donor-Initiated Lawsuits Brought Against Colleges and Universities*, 37 J. COLL. & U.L. 201, 202–04 (2010).

55. *Prudent Management of Institutional Funds Act*, UNIF. L. COMM'N, <https://www.uniformlaws.org/committees/community-home?CommunityKey=043b9067-bc2c-46b7-8436-07c9054064a3> [<https://perma.cc/U42F-3EVM>].

56. See Susan N. Gary, *Charities, Endowments, and Donor Intent: The Uniform Prudent Management of Institutional Funds Act*, 41 GA. L. REV. 1277, 1304–05 (2007).

57. UNIF. PRUDENT MGMT. OF INSTITUTIONAL FUNDS ACT § 4(c) (NAT'L CONF. OF COMM'RS ON UNIF. STATE L. 2006).

prudence.<sup>58</sup> This duty requires them to preserve and grow the endowment's principal while generating income to support their organization's charitable mission. Unlike UMIFA,<sup>59</sup> the uniform act that predated UPMIFA, UPMIFA does not limit an endowment's principal to its historic dollar value.<sup>60</sup> Rather, the Act encourages a more generalized "preservation" of the principal, with a focus on maintaining the purchasing power of the funds.<sup>61</sup> In other words, when Frasier Crane donates \$1 million to the Seattle Opera and stipulates that his donation create an endowment, UPMIFA does not require the Seattle Opera to maintain the \$1 million gift principal in perpetuity. Rather, the Seattle Opera's Board of Directors can adjust the value of the gift principal to increase with inflation and decrease with deflation. This allows the Seattle Opera to make necessary and reasonable expenditures from their endowment in times of economic downturn.

UPMIFA also permits flexibility in defining a "prudent investment." What constitutes a "prudent investment" can depend on the charitable institution's mission, size, and financial policies, as well as economic factors, such as inflation rates, market conditions, and the expected total return of the fund.<sup>62</sup> A large museum endowment, for instance, might prioritize long-term growth and thus assume riskier investments. On the other hand, a smaller arts organization might embrace a more conservative investment approach and focus more on capital preservation and income generation to provide consistent support for ongoing programs and operations.

While the standard for a prudent investment allows for some flexibility in its application, UPMIFA's provisions on *imprudent* investments set forth a more rigid rule.<sup>63</sup> Under the provision, the "appropriation for expenditure . . . of an amount greater than seven percent of the fair market value of an endowment fund is presumed . . . to be imprudent."<sup>64</sup> An organization may rebut this presumption of imprudence by providing a rationale for its spending.<sup>65</sup> For example, an organization might need to spend more than seven percent of its endowment fund in order to complete

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58. *Id.* § 4(a).

59. UNIF. MGMT. OF INSTITUTIONAL FUNDS ACT § 2 (NAT'L CONF. OF COMM'RS ON UNIF. STATE L. 1972).

60. UNIF. PRUDENT MGMT. OF INSTITUTIONAL FUNDS ACT § 4(a) (NAT'L CONF. OF COMM'RS ON UNIF. STATE L. 2006).

61. *See* Gary, *supra* note 56, at 1310–13.

62. UNIF. PRUDENT MGMT. OF INSTITUTIONAL FUNDS ACT § 4(a) (NAT'L CONF. OF COMM'RS ON UNIF. STATE L. 2006).

63. *Id.* § 4(d).

64. Johnny Rex Buckles, *Should the Private Foundation Excise Tax on Failure to Distribute Income Generally Apply to "Private Foundation Substitutes"?* *Evaluating the Taxation of Various Models of Charitable Entities*, 44 NEW ENG. L. REV. 493, 531 (2010).

65. UNIF. PRUDENT MGMT. OF INSTITUTIONAL FUNDS ACT § 4(d) cmt. application of presumption (NAT'L CONF. OF COMM'RS ON UNIF. STATE L. 2006).

a capital campaign project. This one-time disbursement is likely to be found prudent, especially if the organization spends less from its endowment in surrounding years.

These parts of UPMIFA—the spending rule and the rebuttable presumption for imprudent spending—represent only a small portion of the Act’s provision and scope. However, together, they demonstrate how UPMIFA encourages nonprofit boards to limit endowment spending and to invest endowed assets so as to maximize long-term growth.

Before turning to the rationales for endowment growth, it is important to quickly underscore UPMIFA’s pervasiveness in the cultural sector. Many cultural organizations mention UPMIFA in their annual financial reports. For example, the Chicago Symphony Orchestra’s 2022 Financial Report includes a brief discussion of UPMIFA in the section summarizing its endowment investments.<sup>66</sup> Notably, the Report states that the Orchestra’s Board interprets UPMIFA as “requiring the preservation of the historical value of the original gift as of the gift date of the donor-restricted endowment funds absent explicit donor stipulations to the contrary.”<sup>67</sup> This comment demonstrates that while UPMIFA abandoned the historic dollar value standard present in UMIFA, some organizations may continue to utilize it, either due to confusion about the law or out of desire for a more clearly-defined standard for endowment preservation. Some cultural membership organizations have even incorporated UPMIFA’s “prudent financial management” standard into their membership guidelines. For example, the Association of Art Museum Directors (AAMD) penalizes institutions that choose to withdraw from their endowment principals.<sup>68</sup> As these examples demonstrate, UPMIFA and its preference for endowment growth play important roles in cultural organizations’ investment and endowment spending policies.

### *C. Rationale of Growing (Rather than Spending) Endowment Funds*

The decision to prioritize endowment growth has emerged not only to comply with fiduciary duties under UPMIFA. These decisions are also rationalized under various investment theories. This Section investigates two common rationales offered for endowment growth: first, that the endowment serves as a “rainy-day fund,” and second, that endowments

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66. RSM US LLP, CHICAGO SYMPHONY ORCHESTRA: FINANCIAL REPORT 39 (2022), [https://cso.org/media/e2douwhe/chicago-symphony-orchestra\\_22-short\\_fs\\_final.pdf](https://cso.org/media/e2douwhe/chicago-symphony-orchestra_22-short_fs_final.pdf) [https://perma.cc/8Z5E-PYF9].

67. *Id.*

68. Valentina Di Liscia, *Museum Directors Association Lifts Penalties on Museum Spending During Pandemic*, HYPERALLERGIC (Apr. 16, 2020), <https://hyperallergic.com/556328/aamd-spending/> [https://perma.cc/5HHE-24G7].

promote intergenerational equity. In summarizing these theories, I show that valid justifications for creating and expanding endowments exist, even if this Note ultimately argues that Congress should act, through endowment taxation reform, to curb endowment growth.

Endowments are sometimes referred to colloquially as “rainy-day funds.” A rainy-day fund is a pool of assets set aside for unexpected expenses or emergencies. In the context of endowments, maintaining low payout rates allows organizations to preserve capital for the future, offering a cushion should the organization experience an unexpected and extreme shortfall in revenue. Throughout history, and in particular during the COVID-19 pandemic, endowments have provided cultural institutions with emergency funding in times of need. The Metropolitan Opera, for example, withdrew nearly \$30 million from its endowment during the pandemic.<sup>69</sup> Charities do not always draw down from their endowments when situationally appropriate to do so, however.<sup>70</sup> An organization might instead choose to preserve their endowment’s value, even if that decision comes at the expense of cutting staff or other operational costs. Compare the Metropolitan Opera’s decision to withdraw from its endowment during the pandemic to that of the Guggenheim<sup>71</sup> and the San Francisco Museum of Modern Art,<sup>72</sup> both of which laid off staff in lieu of using endowment funds to retain employees, even as the Association of American Museum Directors lifted its penalty on drawing down endowment principals. This shows that while endowments may be portrayed as “rainy-day funds,” they do not always function as such.

Another theoretical justification for endowments is that they promote “intergenerational equity.” According to this theory, endowments preserve for future audiences the same quality of programming as that which is currently provided.<sup>73</sup> Cultural organizations often market their endowments

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69. See Javier C. Hernández, *Pandemic Woes Lead Met Opera to Tap Endowment and Embrace New Work*, N.Y. TIMES (Dec. 26, 2022), <https://www.nytimes.com/2022/12/26/arts/music/metropolitan-opera-endowment-contemporary.html> [https://perma.cc/M6FK-CEPM].

70. See, e.g., Peter Conti-Brown, Note, *Scarcity Amidst Wealth: The Law, Finance, and Culture of Elite University Endowments in Financial Crisis*, 63 STAN. L. REV. 699, 738 (2011) (“The endowment today, for better or worse, is seen as the total whole of the university’s capital reserves. If university administrators adopt the view that endowment preservation and growth is the hallmark of their appointment . . . it is wholly unsurprising that the trade-off between endowment liquidation and budgetary instability tilts decidedly toward the latter.”).

71. See Zachary Small, *Guggenheim Lays Off 10 Employees as Museums Face Fiscal Challenges*, N.Y. TIMES (Dec. 4, 2023), <https://www.nytimes.com/2023/12/04/arts/design/guggenheim-museum-lay-offs.html> [https://perma.cc/W5TG-FBNP].

72. See Tony Bravo & Aidin Vaziri, *SFMOMA Cuts 20 Staff Positions, Citing a 35% Drop in Attendance*, S.F. CHRON. (Nov. 14, 2023, 8:33 PM), <https://www.sfchronicle.com/entertainment/article/sfmoma-staff-cuts-pandemic-18491214.php> [https://perma.cc/JJ9V-YCNT].

73. See Henry Hansmann, *Why Do Universities Have Endowments?*, 19 J. LEGAL STUD. 3, 14 (1990).

as serving this exact purpose. Take, for example, the Colorado Symphony, which marketed its endowment in a recent fundraising campaign as “ensur[ing] that the Colorado Symphony is performing for generations to come.”<sup>74</sup> Chicago’s Steppenwolf Theater Company describes the purpose of its endowment in similar terms, stating that “[t]he future that we envision for Steppenwolf requires critical funds to invest in the development of new theatrical works, continued artistic excellence and financial stability.”<sup>75</sup>

Two other rationales for endowment growth are worth briefly mentioning. First, a sizeable endowment can support fundraising efforts. Because cultural institutions experience deficits in their annual budgets,<sup>76</sup> endowment growth can reassure donors that their gifts are going toward a financially stable institution. A promise of financial security, in the form of a healthy endowment, is particularly important for donors who receive fixed payments for life in exchange for their charitable gift, also known as a “charitable gift annuity.”<sup>77</sup> Second, an organization’s decision to prioritize endowment growth may merely reflect the professional occupancy of its Board members. As Professor Henry Hansmann argues in his seminal study on university endowments, trustees often choose to grow endowments due to their background in the corporate world, where profits are viewed as markers of success.<sup>78</sup> While Hansmann’s argument does not provide a normative justification for growing an endowment in perpetuity, it does help to contextualize why certain financial management practices persist.

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The endowment investment practices discussed in this Part, whether legally codified or merely institutionalized, have spawned massive and

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74. *Colorado Symphony Endowment Fund*, COLO. SYMPHONY, <https://coloradosymphony.org/support/ways-to-give/endowment/> [https://perma.cc/983E-R2G8].

75. *An Investment in American Theatre*, STEPPENWOLF ENDOWMENT, <https://www.steppenwolf.org/support-us/ways-to-give/the-steppenwolf-endowment/> [https://perma.cc/H5CC-CMC8].

76. See Michael Kaiser, *Every Arts Organization Has a Deficit*, HUFFINGTON POST (Jan. 28, 2012), [https://www.huffpost.com/entry/every-arts-organization-h\\_b\\_1116030](https://www.huffpost.com/entry/every-arts-organization-h_b_1116030) [https://perma.cc/Y8BG-FNFG]; see also ROBERT J. FLANAGAN, *THE PERILOUS LIFE OF SYMPHONY ORCHESTRAS: ARTISTIC TRIUMPHS AND ECONOMIC CHALLENGES* 3 (2012).

77. “A charitable gift annuity is a contract under which a person transfers money or other property to a charitable organization in exchange for the charity’s agreement to pay an annuity for life to the transferor and/or another designated beneficiary, where the present value of the annuity is less than the amount of money or the fair market value (‘FMV’) of the property transferred to the charity.” Sanford J. Schlesinger & Martin R. Goodman, *A Primer on Charitable Gift Annuities*, 36 EST. PLAN. 30, 30 (2009). Many cultural organizations currently enter into charitable gift annuities arrangements with donors. See, e.g., *Planned Giving*, NAT’L GALLERY ART, <https://www.nga.gov/support/planned-giving.html> [https://perma.cc/CKA9-X4V3]; *Charitable Gift Annuities*, MET MUSEUM, <https://www.metmuseum.org/join-and-give/support/planned-giving/charitable-gift-annuities> [https://perma.cc/EBX5-WYD7].

78. See Hansmann, *supra* note 73, at 37.

mushrooming cultural reserves. This Part has demonstrated how nonprofit corporate law does not simply encourage endowment growth. Under UPMIFA, it *mandates* prudent investing and *restricts by force of law* endowment spending. While the remainder of this Note addresses tax policy reforms, it is important to keep in mind UPMIFA's legal framework, in part, because as Congress explores potential reforms to endowment taxation, UPMIFA may restrict the amount that Congress can legally require exempt organizations to spend from their endowments, via, for instance, a minimum distribution requirement.<sup>79</sup> It is also important because advancing a nuanced argument in favor of limiting endowment wealth growth requires a familiarity with the laws, ideas, and practices that engender it.

## II. THE HARMS OF CULTURAL ENDOWMENT GROWTH

This Note has thus far detailed the laws, assets, donor restrictions, and investor rationales that shape cultural endowments. It now pivots from these factual inquiries toward a normative framing of endowment growth. Specifically, this Part answers the question: how does endowment wealth accumulation impact America's cultural economy?

This Part identifies three harms generated by cultural endowment growth. It argues that endowment growth (1) decreases charitable spending, (2) shields institutions from public accountability, and (3) produces a concentration of wealth among elite institutions that results in unfair competition over philanthropic dollars and diminishes cultural pluralism. Although some of these harms (e.g., prioritizing endowment growth over charitable spending) are prevalent in other parts of the exempt organization sector, others (e.g., effects on cultural pluralism) are unique to cultural institutions and therefore receive more comprehensive consideration.

### A. *Endowed Growth Occurs at the Expense of Charitable Spending*

One potential aim of endowment tax reform is to encourage charitable institutions to spend more of their endowment revenue to advance their charitable missions. This goal is well-examined in exempt organization scholarship. Professors Evelyn Brody and Daniel Halperin have argued that an excise tax on investment income could promote current spending, including spending toward charitable programs.<sup>80</sup> On higher education in particular, Professor Mae C. Quinn has argued that taxing university

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79. See *infra* Section III.B.

80. See Evelyn Brody, *Charitable Endowments and the Democratization of Dynasty*, 39 ARIZ. L. REV. 873, 945 (1997); Halperin, *Tax Policy and Endowments (Part II)*, *supra* note 16.

endowments could prompt colleges to provide more financial aid.<sup>81</sup> These scholars generally agree that endowment tax reform, whether a tax on investment income or a minimum distribution requirement, could encourage charities to put investment income toward advancing their charitable missions, rather than back in their investment portfolio.

Advancing a cultural organization's charitable mission can encompass a variety of spending activity. It can include investing in education, either by growing extant educational programs or designing new ones.<sup>82</sup> It can also include subsidizing ticket pricing, usually for students, educators, or veterans.<sup>83</sup>

Programs that provide educational benefits or ticket subsidies generally help to increase an organization's accessibility. For cultural organizations like opera companies and fine art museums that already cater to perceived upper-class interests, investing in accessibility and education is particularly important. As these organizations reinvest their endowment income, rather than putting that income toward education and accessibility, their tax-exempt status, a form of government subsidization, becomes more difficult to justify.<sup>84</sup> In fact, the Internal Revenue Service (IRS) and federal courts have gone so far as to strip charities of their exempt status when their activities become inaccessible, or begin to embody a "commercial hue."<sup>85</sup> To illustrate this point, consider an orchestra that charges thousands of dollars for its concerts and fails to offer discounted tickets. The IRS might consider this orchestra to embody a "commercial hue," because its programming would closely resemble that of a for-profit concert venue. And according to the IRS and federal courts, when a nonprofit's activities mirror those of a for-profit company, it makes sense to tax the nonprofit the same as the for-profit.

Spending endowment funds on charitable activities does more than simply safeguard an organization from challenges to their tax-exempt status.

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81. See Mae C. Quinn, *Wealth Accumulation at Elite Colleges, Endowment Taxation, and the Unlikely Story of How Donald Trump Got One Thing Right*, 54 WAKE FOREST L. REV. 451, 481 (2019).

82. Many symphony orchestras, for example, operate youth ensembles or host matinee performances for grade-school children. See, e.g., *CSO for Kids*, CHI. SYMPHONY ORCHESTRA, <https://cso.org/education-community/cso-for-kids/> [https://perma.cc/DXP7-F8VV].

83. See McCarden, *supra* note 40, at 393 ("Funds should be expended on making the artwork and holdings more accessible, rather than continuing to acquire and collect prominent works that systematically disadvantaged segments of society will never see.").

84. Arguments that arts organizations should lose their tax-exempt status due to lack of accessibility are not uncommon and can be found throughout history. See, e.g., Note, *Educational Charities of Limited Public Benefit*, 50 HARV. L. REV. 489 (1937); see also John Russel, *Art: Should Museums Be Exempt from Taxes?*, N.Y. TIMES, Mar. 20, 1983 (§ 2), at 1.

85. See John D. Colombo, *The Role of Access in Charitable Tax Exemption*, 82 WASH. U. L.Q. 343, 358 & n.63 (2004) (citing *Living Faith, Inc. v. Comm'r*, 950 F.2d 365, 373–76 (7th Cir. 1991) and *Presbyterian & Reformed Publ'g Co. v. Comm'r*, 79 T.C. 1070, 1083 (1982), *rev'd*, 743 F.2d 148 (3d Cir. 1984)).

It, more importantly, amplifies the organization's societal impact. Cultural organizations play an important role in supplementing public arts education, fostering creativity and innovation, and preserving America's cultural heritage. Requiring organizations to spend a greater portion of their investment income could ensure that more money is put toward these important public services.

*B. Endowment Growth Shields Institutions from Public Accountability*

Reforming endowment taxation can also subject cultural institutions to increased public accountability. Well-endowed institutions are often less reliant on public funding. Because public funding for the arts is limited, difficult to acquire, and does not offer a fixed, periodic stream of revenue, like annual giving, organizations tend to prefer private funding sources over public ones. Whereas smaller arts organizations often must rely on foundation grants and public funding due to a lack of individual donors,<sup>86</sup> institutions with established donor bases can choose to diversify their revenue streams or even focus their development efforts on procuring private gifts.

The percentage of an organization's budget that comes from government sources matters because public funding introduces important accountability regimes for recipient organizations. These points of accountability can include mandatory grant reporting, conditions for funding, and public review of grant applications.

Take for example, the National Endowment for the Arts' (NEA) Our Town grant. To qualify for the grant, an organization must "establish new or deepen existing cross-sector partnerships" with community organizations and "demonstrate alignment with the NEA's commitment to diversity, equity, inclusion, and accessibility."<sup>87</sup> These application criteria encourage organizations to adhere to ethical standards and to increase the societal value of their programming. The organization's application is then reviewed by a panel of adjudicators.<sup>88</sup> The public review process promotes transparency, requiring organizations to disclose their activities and finances to government-employed grant reviewers. And finally, when recipient organizations complete their funded programs, the NEA requires them to

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86. See Kim Tran, *Allyship in Arts Grantmaking*, GRANTMAKERS ARTS (Oct. 2019), <https://www.giarts.org/allyship-arts-grantmaking> [<https://perma.cc/15S5-L33M>] ("[A]rts organizations of color — specifically those that are African American and Latino — have fewer individual donors and are more reliant on grants from foundations and government sources . . .").

87. See NAT'L ENDOWMENT FOR THE ARTS, OUR TOWN: GRANT PROGRAM DETAILS FY 2025, at 5–7, <https://www.arts.gov/grants/our-town/program-description#required> [<https://perma.cc/SY8Q-C37A>].

88. See *id.* at 24.

submit a final report, summarizing how grant funds were used and the impact of the funded program.<sup>89</sup> If reforming endowment taxation can encourage well-endowed institutions to seek out public funding opportunities, then it would also subject those organizations to these reporting procedures and stages of review. These facets of government grant-making are important, because they hold cultural organizations accountable to stakeholders beyond the members of their boards.

Lawmakers have long recognized the value of public accountability for charities. When Congress ratified the 1969 Tax Reform Act, its members voiced concern over private foundations' accountability to the public.<sup>90</sup> Lawmakers contended that private foundations, often controlled by familial or closely-knit groups, were less democratic and therefore less deserving of the bounty of tax benefits afforded to public charities.<sup>91</sup> Ultimately, these concerns led to the distinction between public charities and private foundations—a distinction which rests, in part, on an organization's degree of public support.<sup>92</sup> Congress permits public charities to collect more benefits than private foundations, because unlike foundations, charities report to and serve the needs of a broad, public constituency. Endowment taxation should ensure that this essential quality of public charities remains distinct.

### *C. Endowment Growth Produces a Concentration of Wealth Among Elite Institutions*

Finally, taxing cultural endowments can mitigate the increasing, unfair competition over philanthropic dollars in America's cultural sector and encourage cultural pluralism. America's cultural sector does not benefit from the same built-in funding opportunities present in other charitable subsectors. Unlike in higher education, where college graduates make donations to their alma maters and therefore more widely distribute

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89. See *id.* at 25.

90. See Hackney, *supra* note 40, at 237 (“Congress distrusted private foundations because control lay with a creator or family and not a broad public.”).

91. See Rob Reich, *On the Role of Foundations in Democracies*, in PHILANTHROPY IN DEMOCRATIC SOCIETIES: HISTORY, INSTITUTIONS, VALUES 64, 65 (Rob Reich, Chiara Cordelli & Lucy Bernholz eds., 2016) (“[Private foundations] were troubling because they were considered a deeply antidemocratic institution, an entity that could exist in perpetuity and that was unaccountable except to a hand-picked assemblage of trustees.”).

92. See I.R.C. § 509(a)(1), (2); see also Dana Brakman Reiser, *Foundation Regulation in Our Age of Impact*, 17 PITT. TAX REV. 357, 358 (2020) (“An organization is deemed a public charity if it can identify a significant class of small donors or consumers of their services. Those organizations supported primarily by a small group of large donors and without active charitable operations were instead deemed private foundations and ever since have been subject to a strict set of operational restrictions.”).

wealth,<sup>93</sup> and unlike the nonprofit hospital industry, where a limited number of nonprofit hospitals exist in each community,<sup>94</sup> the cultural sector cannot produce future donors in the form of alumni, nor can it rely on intra-community institutional paucity. When combined with a deficiency in public funding, these factors create within the cultural sector a competitive market for philanthropic dollars.

Endowment wealth accumulation further complicates these already competitive funding dynamics. Large endowments operate as symbols of prestige. They are, in the words of Professor Peter Conti-Brown, akin to “cowboys’ belt buckles: the bigger the buckle, the more impressive the cowboy.”<sup>95</sup> In a recent blogpost on college endowments, written in light of the controversy over university investments in Israel, Professor David Pozen remarked that “having a large endowment has become . . . an end in itself, a key measure of a university’s prestige.”<sup>96</sup> Because large endowments indicate financial stability and institutional success, they can divert philanthropic attention. This allows already sizeable institutions to collect further capital, while stymieing smaller ones<sup>97</sup>—a phenomenon that sociologists refer to as the “Matthew effect.”<sup>98</sup> As Professor James Fishman has argued, the “growing inequality of endowment wealth puts less endowed institutions at a competitive disadvantage, leading to a greater concentration of human capital and resources in very few institutions.”<sup>99</sup> While Professor Fishman was concerned with university endowments in particular, his thesis clearly resonates within the cultural sector. Today, the largest cultural institutions in America boast endowments that exceed \$1

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93. See Emma Whitford, *Charitable Gifts to Colleges Top \$52 Billion*, INSIDE HIGHER ED. (Feb. 16, 2022), <https://www.insidehighered.com/news/2022/02/17/giving-colleges-grew-7-percent-fiscal-2021> [<https://perma.cc/X3MD-YLHT>] (“Combined, donations from foundations and alumni accounted for 56.3 percent of higher ed giving in fiscal year 2021.”).

94. The St. Louis metro area, where I live, for example, has five hospital systems, even fewer of which are nonprofit hospitals, and over four hundred arts organizations. See *List of Hospitals in St. Louis*, WIKIPEDIA, [https://en.wikipedia.org/wiki/List\\_of\\_hospitals\\_in\\_St.\\_Louis](https://en.wikipedia.org/wiki/List_of_hospitals_in_St._Louis) [<https://perma.cc/XTS2-G5BM>]; *Arts Organizations in St. Louis*, REG’L ARTS COMM’N ST. LOUIS, <https://racstl.org/arts-organizations-in-st-louis/> [<https://perma.cc/622G-YL62>] (“St. Louis is home to more than 450 arts organizations and organizations who support the arts through programming.”).

95. See Peter Conti-Brown, *supra* note 70, at 704.

96. David Pozen, *Seeing the University More Clearly*, BALKINIZATION (May 6, 2024), <https://balkin.blogspot.com/2024/05/seeing-university-more-clearly.html> [<https://perma.cc/Y4FL-DPVR>].

97. See James J. Fishman, *How Big Is Too Big: Should Certain Higher Educational Endowments’ Net Investment Income Be Subject to Tax?*, 28 CORNELL J.L. & PUB. POL’Y 159, 196 (2018).

98. See Robert K. Merton, *The Thomas Theorem and the Matthew Effect*, 74 SOC. FORCES 379, 394 (1995) (defining the Matthew Effect as the “accruing of greater recognition by peers for particular scientific or scholarly contributions to scholars of great repute and the withholding of such recognition from [their collaborating] scholars who have not yet made their mark” (alteration in original)). It refers to Matthew 13:12 and 25:29: “Unto every one that hath shall be given, and he shall have abundance: but from him that hath not shall be taken away even that which he hath.” *Id.* at 394 & n.19.

99. Fishman, *supra* note 97, at 196.

billion in value,<sup>100</sup> whereas the smallest arts organizations can exist on as little as a few thousand dollars in annual operating revenue.<sup>101</sup>

Disparities in institutional wealth between cultural organizations are concerning because these disparities map onto historically defined cultural hierarchies.<sup>102</sup> Well-endowed organizations tend to promote Western European or “highbrow” art forms, such as ballet, opera, and fine arts. Indigenous, folk, and experimental art forms, on the other hand, are largely advanced by organizations with limited budgets. A 2017 study conducted by the Helicon Collaborative, an arts-industry-focused consulting and research group, found that:

Just 2 percent of all cultural institutions receive nearly 60 percent of all contributed revenue [from private and public sources in America] . . . . The 2 percent cohort is made up of 925 cultural groups that have annual budgets of more than \$5 million. . . . These organizations are symphonies, opera companies, regional theaters, art museums, ballet companies, and other large institutions – the majority of which focus primarily on Western European fine arts traditions. While most of these institutions have made sincere efforts to broaden participation in the past decade, their audiences remain predominantly white and upper income.<sup>103</sup>

The study goes on to report that “fewer than 50 cultural organizations whose missions focus primarily on artistic traditions from Africa, Asia, Latin America, the Middle East and Native America . . . receive enough funding to maintain budgets of \$5 million [per year].”<sup>104</sup> The list of cultural institutions with endowments exceeding \$200 million, found in Appendix A of this Note, further supports this idea; the list contains dozens of fine art museums, symphony orchestras, and opera companies, yet not a single organization dedicated to a non-white, non-Western cultural form.

When a small group of cultural institutions focused on promoting Western European art forms siphon off philanthropic dollars, cultural pluralism suffers. Pluralism matters because today’s cultural activity shapes America’s cultural legacy. Through their sizeable endowments, prominent cultural institutions become a powerful constituency in the realm of legacy building. Think of this as the “political power” of cultural institutions. Just

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100. See *infra* Appendix A.

101. See Woong Jo Chang, *How “Small” Are Small Arts Organizations?*, 40 J. ARTS MGMT. L. & SOC’Y 217, 223–31 (2010).

102. See generally LEVINE, *supra* note 37.

103. HELICON COLLABORATIVE, NOT JUST MONEY: EQUITY ISSUES IN CULTURAL PHILANTHROPY 5 (2017), [https://heliconcollab.net/wp-content/uploads/2017/08/NotJustMoney\\_Full\\_Report\\_July2017.pdf](https://heliconcollab.net/wp-content/uploads/2017/08/NotJustMoney_Full_Report_July2017.pdf) [<https://perma.cc/JPU9-5D3P>].

104. *Id.* at 6.

as personal wealth allows individuals to influence political decision-making,<sup>105</sup> large endowments enable cultural institutions to fund and consequently define what art deserves public attention and historical recognition. And if those organizations predominantly promote “highbrow” art forms, then “highbrow” art forms are more likely to define America’s cultural legacy, not due to public demand, but because of access to financial resources.

One might argue that the private sector’s inability to provide for cultural pluralism is exactly why we have public funding: public funding accounts for what the market cannot.<sup>106</sup> But it is important to remember that public entities too are limited in their capacity to provide for *all* cultural needs. To begin, federal and state government have limited cash to grant to organizations. The National Endowment for the Arts currently has an annual budget of \$207 million—an amount that has remained essentially stagnant for the past twenty years.<sup>107</sup> Moreover, the government cannot be relied upon to fund experimental or transgressive artistic works, given that government support of such artwork has been met in recent history with controversy and backlash, as exemplified by the brouhaha over Andres Serrano’s *Piss Christ* in 1989.<sup>108</sup> For these reasons, public funding cannot be expected to safeguard cultural pluralism when private actors fail to do so.

Finally, pluralism matters because courts have identified it as an essential quality of the charitable sector. In *Bob Jones University v. United States*, a seminal exempt organization case in which the Supreme Court upheld an I.R.S. decision to deny tax-exempt status to Bob Jones University, due to its enforcement of racially discriminatory policies,<sup>109</sup> Justice Powell, writing in concurrence, drew attention to the importance of protecting pluralism in

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105. See generally LAWRENCE LESSIG, *REPUBLIC, LOST: HOW MONEY CORRUPTS CONGRESS—AND A PLAN TO STOP IT* 89–127 (2011) (describing the effects of concentrated economic power on democratic government); JACOB ROWBOTTOM, *DEMOCRACY DISTORTED: WEALTH, INFLUENCE, AND DEMOCRATIC POLITICS* 2–5 (2010) (discussing five ways wealth inequality can impact political decisions).

106. See, e.g., Reich, *supra* note 91, at 73–74 (“It has long been understood that the commercial marketplace does not do well at providing public goods—goods that economists define as nonrival and nonexcludable. . . . Instead, the state can provide public goods, and this is commonly thought to be one of the basic functions of a state and its use of tax dollars.”).

107. *National Endowment for the Arts Appropriations History*, NAT’L ENDOWMENT FOR ARTS, <https://www.arts.gov/about/appropriations-history> [<https://perma.cc/4CVY-NSTW>].

108. Andres Serrano’s *Piss Christ*—a photograph of a plastic crucifix submerged in urine—was at the center of a public debate over federal funding for the arts, after the photograph was displayed in a National Endowment for the Arts (NEA) funded exhibition at the Southeastern Center for Contemporary Arts in 1989. Months after the exhibition, Senator Jesse Helms introduced a bill that proposed to cut the NEA’s visual arts budget by \$400,000 and to require external review of the NEA’s grantmaking process. See generally Peggy Phelan, *Serrano, Mapplethorpe, the NEA, and You: “Money Talks”: October 1989*, 34 *TDR* 4, 5–8 (1990).

109. See *Bob Jones Univ. v. United States*, 461 U.S. 574, 605 (1983).

America's charitable sector. While Justice Powell agreed with the majority's conclusion that racially discriminatory practices have no place amongst charities, he took issue with the court's rationale, which provided that the "critical question in determining tax-exempt status is whether an individual organization provides a clear 'public benefit.'"<sup>110</sup> Of particular concern to Justice Powell was the question of *who* gets to define a "public benefit" and, if the answer was the courts and Congress, the "element of conformity"<sup>111</sup> that such a system would provide. He wrote: "In my opinion, such a view of § 501(c)(3) ignores the important role played by tax exemptions in encouraging diverse, indeed often sharply conflicting, activities and viewpoints."<sup>112</sup>

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Some charities are dynasties, others are not. And while complete redistribution of wealth within America's cultural sector may not be feasible, encouraging dynastic institutions to put more endowment dollars toward charitable programs and to engage with a broader swath of the public through government grant-making is. I now turn to evaluating which endowment taxation reforms lend themselves best to achieving these goals.

### III. TOWARD A POLICY SOLUTION

This Note argues that the harms of cultural endowment growth can be mitigated through measured tax reform. This Part looks at two potential reforms, each of which would alter the tax treatment of charitable endowments: (1) a proposal to enact an excise tax on net investment income and (2) a proposal to subject endowments to a minimum distribution requirement. My goal in discussing each proposal is to evaluate its capacity to address the harms of cultural wealth accumulation defined in Part II.

I conclude this Part by turning to the question of *which* cultural institutions Congress should subject to endowment taxation reform. I argue that the basis or reach of each endowment taxation policy should be defined on a subsector-specific basis, rather than for the charitable sector as a whole, as this would allow Congress to tax cultural endowments without inequitably impacting smaller universities and nonprofit hospitals.

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110. *Id.* at 608 (Powell, J., concurring).

111. *Id.* at 609.

112. *Id.*

### A. Excise Tax on Net Investment Income

One potential reform would subject cultural institutions to an excise tax on their net investment income.<sup>113</sup> Legal scholarship has long weighed the benefits and consequences of placing an excise tax on charitable endowments.<sup>114</sup> Most recently, this scholarly discourse has focused on Section 4968 of the Code: the university endowment tax. Professor Edward Zelinsky, for example, has suggested that Congress apply Section 4968 to *all* public charities.<sup>115</sup>

Expansion of Section 4968 could encourage cultural institutions to spend more of their endowment income on charitable activity, if Congress appropriately tailors the provision. Congress generally enacts excise taxes to regulate behavior.<sup>116</sup> An excise tax on cigarettes, for example, is intended to discourage smoking. Similarly, the university endowment tax was enacted, in part,<sup>117</sup> to encourage universities to create scholarship funds and to address college affordability.

Because Section 4968 excludes from taxation those university assets used to carry out the institution's exempt purpose,<sup>118</sup> it already takes an important step toward encouraging charitable spending. But more can be done. Professor Bird-Pollan has suggested, for example, that rather than impose the tax on net investment income, Congress could impose the

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113. While many refer to the § 4968 excise tax on net investment income as an “endowment tax,” it bears mentioning that § 4968 does not tax the value of the endowment, but rather any income earned from the endowment and other investments. *See supra* note 21 (discussing the definition of “net investment income” under § 4968).

114. *See, e.g.,* Brody, *supra* note 80, at 945 (“If, however, current charitable spending is important to society, and society wants to use the tax system to encourage that goal, it can subject all or a portion of the charity’s investment income to income tax. A broader approach—applicable to contributed amounts as well as to income—would be to adopt a type of ‘accumulated earnings tax’ for charities that do not have concrete plans to spend investment assets within a specified period.”); Fishman, *supra* note 97, at 195–99; Marion R. Fremont-Smith, *Is It Time to Treat Private Foundations and Public Charities Alike?*, TAXNOTES (June 1, 2006), <https://www.taxnotes.com/exempt-organizations/exempt-organizations/it-time-treat-private-foundations-and-public-charities-alike/2006/06/01/18rr?> [https://perma.cc/48BJ-4PDS] (“[An excise tax on investment income] merely diverts funds that would otherwise be applied for public charitable purposes to the federal treasury—a policy that runs counter to all the other provisions designed to provide incentives for charitable giving.”).

115. *See generally* Zelinsky, *supra* note 23.

116. *See* CONG. RSCH. SERV., R46938, FEDERAL EXCISE TAXES: BACKGROUND AND GENERAL ANALYSIS 1 (2021) (defining four types of excise taxes: (1) sumptuary taxes, or taxes “imposed for moral reasons . . . to discourage a specific activity that is thought to have negative spillover effects (or externalities) on the consumer and society,” (2) regulatory taxes, or taxes “[i]mposed to offset external costs associated with regulating public safety or to discourage consumption of a specific commodity that is thought to have negative externalities on society,” (3) benefit-based taxes, or taxes “[i]mposed to charge users of a particular public good (e.g., a highway or national park),” and (4) luxury taxes, or taxes “imposed to raise revenue, particularly from higher-income households”).

117. Congress also enacted Section 4968 to mitigate the negative revenue consequences of the TCJA. *See* Bird-Pollan, *supra* note 22, at 1075.

118. I.R.C. § 4968 (West).

Section 4968 excise tax on “amount earned through the endowment that exceeds amounts spent on university operations or invested in capital assets that are used toward the [organization’s] charitable purposes.”<sup>119</sup> Alternatively, Professor Fishman has suggested that Congress could permit organizations to reduce their liability under the excise tax through charitable action, like using investment income to reduce ticket prices or to develop an educational program.<sup>120</sup> Either of these reforms, if adopted by Congress in expanding Section 4968, would further incentivize charitable spending.

Imposing an excise tax on charitable endowments might also incentivize cultural institutions to seek out government funding, potentially increasing public accountability. This would, however, depend on a variety of factors, including the financial health of the institutions subject to the tax, their ability to generate revenue through other means, and the availability of public grant programs. Even if the excise tax significantly impacts the financial position of those subject to it, institutions may opt to offset the tax burden by increasing ticket prices or recruiting additional donors, rather than applying for government funding. For these reasons, the impact of excise taxes on encouraging charities to apply for public funding remains uncertain.

### *B. Minimum Distribution Requirement*

Another reform, explored by several Congressional committees in the late aughts<sup>121</sup> and more recently proposed by Craig Kennedy, a senior fellow at the *Giving Review*,<sup>122</sup> would require charities to distribute a minimum percentage of their assets each year. Currently, Section 4942 of the Code imposes a thirty percent excise tax on private foundations that fail to spend five percent of their net assets on “qualifying distributions,” or distributions that advance the foundation’s exempt purpose.<sup>123</sup> So, a private foundation with \$500 million in net assets must spend \$25 million to further its exempt purpose; otherwise, it pays a significant excise tax on undistributed income. Craig Kennedy’s proposal would extend this requirement to all large, exempt organizations.

Generally, a minimum distribution requirement is thought to encourage organizations to redirect funds toward charitable activity. Proponents of

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119. Bird-Pollan, *supra* note 22, at 1080–81.

120. Fishman, *supra* note 97, at 201.

121. See Alexander M. Wolf, Note, *The Problems with Payouts: Assessing the Proposal for a Mandatory Distribution Requirement for University Endowments*, 48 HARV. J. ON LEGIS. 591, 597–600 (2011) (“[T]he possibility of a mandatory payout arose as early as December 2006 in Senate Finance Committee hearings on tax exemptions in higher education.”).

122. See Kennedy, *supra* note 25.

123. I.R.C. § 4942 (West).

payouts argue that consistent spending of endowment assets does more social good than allowing an endowment to grow in perpetuity.<sup>124</sup> Because minimum distribution requirements encourage charitable spending, this proposal would achieve similar results to an excise tax, while allowing charities to retain and redirect their investment income, rather than pay a portion of it to the federal government.

While payout requirements encourage charitable spending, they have pitfalls as well. To begin, payout requirements do not always promise that organizations will use distributed funds to support educational programs, ticket subsidies, or other mission-driven activities. Instead, organizations might divert these funds toward less-accessible ticketed programming or even executive salaries. As Professor Ray Madoff has demonstrated, private foundations often meet their 5% payout obligation by paying “salaries, trustee fees and other administrative expenses.”<sup>125</sup> Because these expenses keep the foundation operating, they indirectly meet Section 4942’s vague standard for a “qualifying distribution.”<sup>126</sup>

Moreover, payouts can deter organizations from spending more than the statutorily mandated amount. A payout rate not only *can*, as Alexander Wolf has argued, “become a ceiling, incentivizing institutions not to spend above it,”<sup>127</sup> empirical evidence demonstrates that Section 4942 *has* had this effect on private foundations.<sup>128</sup> This has led some to argue that eliminating the payout requirement could increase distributions.<sup>129</sup>

And finally, it is important to note that a minimum distribution requirement can conflict with the spending practices that UPMIFA endorses. As discussed earlier, one optional UPMIFA provision offers a presumption of imprudence for distributions above seven percent.<sup>130</sup> So, ideally, a payout requirement for charities would fall below UPMIFA’s presumptively imprudent payout rate.

While a minimum distribution requirement or an excise tax on net investment income could help to encourage charitable spending, it is difficult to imagine either policy addressing the systemic issues that have limited pluralism in America’s cultural sector. Neither a minimum distribution requirement nor an excise tax alters the behavior of donors or institutional funders and therefore cannot reorient philanthropic dollars

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124. See Wolf, *supra* note 121, at 600 (“Among the principal arguments made in support of a mandatory payout is that such a requirement will increase college affordability . . . . Proponents explain that a payout offers a means to limit tuition increases and boost financial aid to students.”).

125. Ray D. Madoff, *The Five Percent Fig Leaf*, 17 PITT. TAX REV. 341, 346 (2020).

126. See *id.* at 347.

127. Wolf, *supra* note 121, at 593.

128. See Halperin, *Tax Policy and Endowments (Part II)*, *supra* note 16.

129. See *id.*; Wolf, *supra* note 121, at 611.

130. See *supra* Section I.C.

toward underfunded artistic activities. Rather, the more appropriate avenue for fostering pluralism is perhaps through donor deduction reform, a policy item beyond the scope of this Note.

### *C. Taxable Base*

This Part has, up to this point, analyzed proposed modifications to the mechanics of endowment taxation, while ignoring the question: which organizations should Congress subject to these reforms? Whether enacting an excise tax on cultural endowments or introducing a minimum distribution requirement, Congress would need to determine which endowments, based on size, warrant restricted tax benefits.

Congress often defines the scope of a tax policy according to organizational or individual income or net assets. Section 4968, the excise tax on university endowments, for example, applies to private universities whose endowment holdings per tuition-paying student exceed \$500,000.<sup>131</sup> An expanded Section 4968 would likely apply, as Craig Kennedy has suggested, to all charities with net restricted assets in excess of a certain amount.<sup>132</sup> But from a normative perspective, should it?

I wish to argue that the scope of endowment taxation reform should be defined on a subsector-specific basis, rather than for the charitable sector as a whole. Tax scholars and policymakers should consider that wealth amassment impacts industries within America's charitable economy on a subsector-by-subsector basis. University endowments might, generally speaking, dwarf cultural endowments in value of net assets, but the higher educational industry also surpasses the nonprofit cultural industry in size,<sup>133</sup> with the smallest universities far outsizeing the smallest arts organizations. This matters because disparities in scale influence resource distribution. Competition for philanthropic dollars still exists among arts organizations. Endowment growth still disproportionately favors the elite in America's cultural sector. These dynamics simply unfold on a different economic scale.

It is important to tailor endowment taxation reform to charitable subsectors, in part, because the rationales for taxing endowments are subsector specific. Proponents of the 2017 excise tax on university endowments, for example, argued that universities should put more

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131. I.R.C. § 4968 (West).

132. See Kennedy, *supra* note 25.

133. See MOLLY F. SHERLOCK & JANE G. GRAVELLE, CONG. RSCH. SERV., R40919, AN OVERVIEW OF THE NONPROFIT AND CHARITABLE SECTOR 10 (2009) (demonstrating, based on data compiled by the National Center for Charitable Statistics, that the arts, culture, and humanities sector held 3.86% of all assets held by charitable organizations, whereas higher education held 21.21% and nonprofit hospitals held 29.13%).

endowment income toward financial aid for students.<sup>134</sup> Public health advocates have similarly argued that nonprofit hospitals should prioritize subsidizing medical costs for uninsured and underinsured patients over endowment growth.<sup>135</sup> And, as this Note demonstrates, there are several reasons to tax cultural endowments that are relevant to the cultural sector alone.<sup>136</sup>

The only way to equitably mitigate harmful endowment growth in each of these subsectors, including smaller charitable subsectors, like the cultural sector, is to define the taxable base of future endowment taxation reforms on a subsector-specific basis. Because the smallest university and nonprofit endowments still outsize the largest cultural endowments, a reform that alters the tax treatment of *all* public charities with endowments above a specified size may not capture cultural endowments. Lowering the endowed asset threshold for all public charities to include larger cultural organizations, however, might unfairly impact smaller hospitals and universities. Accordingly, subsector-specific bases are necessary to equitably mitigate the effects of wealth amassment across our charitable sector.

Such a proposal is feasible given the National Taxonomy of Exempt Entities' (NTEE) classification system. The IRS and National Center for Charitable Statistics (NCCS) use the NTEE system to classify exempt organizations by subsector and general activities.<sup>137</sup> The system divides the world exempt organizations into ten subsectors (e.g., Arts, Culture, and Humanities; Education; and Health), encompassing twenty-six "major groups," and provides a list of alphanumeric codes that exempt organizations use to reflect their charitable activities.<sup>138</sup> For example, the Metropolitan Opera's code is A6A; here, the "A" reflects the company's major group—Arts, Culture, and Humanities—and the "6A" reflects the company's specific activities—producing opera.<sup>139</sup> Because every exempt

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134. See, e.g., Alex Muresianu, *Should We Tax University Endowments?*, TAX FOUND. (Oct. 19, 2022), <https://taxfoundation.org/blog/university-endowment-tax/> [<https://perma.cc/9F6F-QW7X>] ("Some commentators advocate taxing endowments as a form of restitution for student loan debt. Under this theory, colleges and universities have not held up their end of the bargain to make students financially better off, instead leaving them with large amounts of loan debt. Therefore, colleges and universities should be the ones to foot the bill for student loan debt forgiveness, not the general taxpayer.").

135. See Ge Bai, Farah Yehia & Gerard F. Anderson, *Charity Care Provision by US Nonprofit Hospitals*, 180 JAMA INTERNAL MED. 606, 607 (2020) ("Nonprofit hospitals with substantial financial strength should consider more generous financial assistance eligibility criteria to reduce the financial risk exposure of disadvantaged uninsured and underinsured patients.").

136. See *supra* Part II.

137. See Jones, *supra* note 32.

138. See *id.*

139. See *Metropolitan Opera Association Inc.*, PROPUBLICA, <https://projects.propublica.org/nonprofits/organizations/131624087> [<https://perma.cc/K39A-VMFZ>].

organization either self-selects or receives an NTEE code upon approval for tax exemption,<sup>140</sup> Congress could use the NTEE's ten broad categories to efficiently sort exempt organizations for purposes of an excise tax or minimum distribution requirement with a subsector-specific base.

The relevant question then becomes, what is the appropriate taxable base for each subsector? Answering this question would require careful economic analysis, beyond the scope of this Note. But I will nonetheless note two considerations policymakers should keep in mind.

First, defining a taxable base on a subsector-specific basis could take on many forms. For instance, Congress could individually determine the base for each subsector, based on factors unique to that subsector's economy. Alternatively, Congress could author a general formula for determining which institutions will be subject to taxation and apply that general formula to each subsector; for instance, Congress could decide that all endowments valued at eighty percent of the highest-valued endowment in a subsector should be subject to taxation. This option has the benefit of upholding economic neutrality, or the notion that all similarly situated entities should receive similar tax treatment, while providing for different taxation thresholds for different charitable subsectors. Either way, Congress could rely on data from the National Center for Charitable Statistics (NCCS) to calculate appropriate bases.<sup>141</sup>

And second, an ideal base for any subsector would curb endowment growth among large institutions, while preserving current tax treatment for smaller organizations. This is particularly important for the cultural sector. In recent years, and particularly during the COVID-19 pandemic, many arts organizations drew down from their endowments or otherwise closed doors. In 2020, the Lyric Opera of the Chicago spent \$23 million from its \$173 million endowment,<sup>142</sup> and more recently, the San Francisco Art Institute<sup>143</sup> and San Antonio Symphony<sup>144</sup> filed for bankruptcy. Endowment taxation should not exacerbate these financial issues. It should instead only impact those cultural organizations that enjoy financial stability. The taxable base proposal discussed in this Section would further this goal by ensuring that

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140. See INTERNAL REVENUE SERV., *supra* note 33.

141. See *National Center for Charitable Statistics Data*, URB. INST., <https://www.urban.org/tags/national-center-charitable-statistics-data> [<https://perma.cc/QB5Y-23D5>].

142. See Graham Bowley & Julia Jacobs, *The Sacrosanct Endowment? Not Anymore for Some Arts Groups*, N.Y. TIMES (June 3, 2020), <https://www.nytimes.com/2020/06/02/arts/endowments-coronavirus.html> [<https://perma.cc/B6ZM-XBFU>].

143. See Angelica Villa, *Facing Continued Financial Strain, San Francisco Art Institute Files for Bankruptcy*, ARTNEWS (Apr. 27, 2023, 5:15 PM), <https://www.artnews.com/art-news/news/embattled-san-francisco-art-institute-files-bankruptcy-1234665855/> [<https://perma.cc/LHB4-6Y5G>].

144. See Javier C. Hernández, *San Antonio Symphony to Dissolve Amid Labor Dispute*, N.Y. TIMES (June 17, 2022), <https://www.nytimes.com/2022/06/17/arts/music/san-antonio-symphony-bankruptcy.html> [<https://perma.cc/T79A-J6WC>].

only the wealthiest organizations in each charitable subsector see their tax treatment altered.

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A palette of policy reforms is needed to address the harms of cultural endowment growth. Whereas either an excise tax on net investment income or a minimum distribution requirement can encourage charitable spending, donor deduction reform, a topic that is beyond the scope of this Note, is needed to facilitate a more equitable distribution of philanthropic dollars. And while the circulating proposals for endowment taxation reform would adhere a single, uniform taxable base to each of these proposals, it is important to remember that the harms of endowment wealth accumulation manifest on a subsector-by-subsector basis. Any reform aimed at redressing these harms should therefore be scaled to fit individual charitable subsectors.

#### CONCLUSION

Scholars and politicians have long recognized that the charitable sector is not a monolith. And yet, America's cultural industry, a significant portion of our charitable sector, has received little attention in tax policy scholarship.<sup>145</sup> This Note takes the first step in filling this scholarly lacuna. It argues that cultural endowment growth produces negative externalities that *can* and *should* be mitigated through measured taxation reform. It contends that endowment taxation reform should focus on encouraging institutions to divert funds toward their charitable missions and influencing philanthropic behavior so as to ensure more equitable distribution of charitable dollars. And finally, it argues for subsector-specific taxable bases as a means of equitably curbing wealth accumulation across America's charitable sector.

As tax policy scholarship continues to cast a critical eye toward personal and corporate wealth accumulation in America,<sup>146</sup> scholars should consider how wealth inequality impacts creativity and cultural production. Cultural activity in America matters. It fosters a sense of community, preserves historical traditions, stimulates innovation, and inspires social change. But as this Note demonstrates, our current tax laws have contributed to a system that benefits elite artistic institutions, while harming others and straining

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145. See *supra* note 34.

146. See, e.g., THOMAS PIKETTY, CAPITAL IN THE TWENTY-FIRST CENTURY (Arthur Goldhammer trans., 2014); EMMANUEL SAEZ & GABRIEL ZUCMAN, THE TRIUMPH OF INJUSTICE: HOW THE RICH DODGE TAXES AND HOW TO MAKE THEM PAY (2019); Ingrid Robeyns, *Having Too Much, in WEALTH: NOMOS LVIII* 16 (Jack Knight & Melissa Schwartzberg eds., 2017).

pluralism. Tax policy reform is necessary to redress these harms and to cultivate a diverse, equitable, and vibrant creative economy.

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## APPENDIX

Cultural Endowments Valued at Over \$200 Million in FY 2022<sup>147</sup>

Rank	Organization	End-of-Year Endowment Value
1	The Metropolitan Museum of Art	\$ 4,067,815,298
2	Cambridge University Press	\$2,880,339,115
3	Smithsonian Institute	\$2,323,063,719
4	Museum of Fine Arts Houston	\$1,478,063,857
5	Crystal Bridges Museum of American Art	\$1,312,496,139
6	Museum of Modern Art (New York, NY)	\$1,011,156,858
7	National Trust for Places of Historic Interest or Natural Beauty	\$864,673,000
8	Cleveland Museum of Art	\$854,407,000
9	Colonial Williamsburg Foundation	\$712,327,420
10	Museum of Fine Arts (Boston, MA)	\$703,387,703
11	American Museum of Natural History	\$670,649,092
12	National Gallery of Art	\$649,364,304
13	Huntington Library & Art Gallery	\$639,700,488
14	United States Holocaust Memorial Council	\$545,337,536

147. This list was compiled using the National Center on Charitable Statistics' (NCCS) 2019 501(c)(3) Charities Scope PZ Core Data Set. The NCCS Core Data Sets compile information reported by public charities on their Form 990s and 990EZs—forms the IRS requires exempt organizations to file each year. To identify the most well-endowed cultural institutions, I sorted the NCCS data set to include only organizations with NTEE codes beginning with "A" (i.e., organizations in the Arts, Culture, and Humanities major group) and then further sorted those organizations by their total assets, highest to lowest, to identify all organizations with total assets above \$100 million. (The NCCS core data sets do not include information from organizations' Form 990, Schedule Ds, the portion of the Form 990 where endowment data is reported, and so I used the "total asset" values as an initial proxy for endowment size, as an organization's total asset value will capture its endowed assets.) I then searched each remaining organization's FY 2022 Form 990, Schedule D, for its end-of-year endowment value.

Rank	Organization	End-of-Year Endowment Value
15	Philadelphia Museum of Art	\$528,704,141
16	Peabody Essex Museum	\$522,223,163
17	Field Museum of Natural History	\$489,084,778
18	Boston Symphony Orchestra	\$484,000,000
19	The Edison Institute	\$421,436,974
20	Carnegie Institute	\$414,230,323
21	Whitney Museum of American Art	\$410,832,000
22	Indianapolis Museum of Art	\$386,951,000
23	San Francisco Museum of Modern Art	\$365,365,940
24	The Detroit Institute of Art	\$365,343,109
25	Winterthur Museum, Garden & Library	\$364,761,196
26	WGBH Educational Foundation	\$360,589,860
27	Chicago Symphony Orchestra	\$359,969,000
28	Children's Museum of Indianapolis	\$344,706,839
29	Frick Collection	\$329,671,083
30	San Francisco Symphony	\$326,079,621
31	National Public Radio	\$322,673,461
32	Los Angeles Philharmonic	\$318,691,596
33	Woodruff Arts Center	\$315,888,139
34	Carnegie Hall	\$301,041,654
35	National Trust for Historic Preservation	\$297,729,719
36	Metropolitan Opera Association	\$292,599,111
37	Walker Art Center	\$283,763,358
38	San Francisco Opera	\$281,244,062
39	American Philosophical Society	\$270,577,742
40	The Musical Arts Association	\$269,793,420

Rank	Organization	End-of-Year Endowment Value
41	Lincoln Center for Performing Arts	\$267,877,928
44	Nelson Gallery Foundation	\$260,073,045
42	St. Louis Art Museum	\$255,009,403
43	Virginia Museum of Fine Arts	\$253,874,707
45	Skirball Cultural Center	\$238,912,676
46	St. Louis Symphony	\$238,715,010
47	Dallas Museum of Art	\$234,247,199
48	Mount Vernon Ladies Association of the Union	\$231,240,981
49	New York Philharmonic	\$228,493,580
50	Thomas Jefferson Foundation	\$227,436,091
51	Cincinnati Symphony Orchestra	\$224,568,209
52	Curtis Institute of Music	\$222,507,085
53	New York City Ballet	\$216,717,896
54	California Institute of the Arts	\$215,891,775
55	Music Center Foundation	\$204,875,662
56	WNET	\$200,876,042
57	Museum of Science	\$200,615,264