

## FACTUAL INDETERMINACY IN INTERNATIONAL TAX LAW

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*Legal indeterminacy comes in a variety of forms identified here as: (i) general legal indeterminacy; (ii) factual indeterminacy; and (iii) Mach/Feyerabend factual indeterminacy. The concept of general “legal indeterminacy” refers to problems in legal interpretation and has been extensively studied. “Factual indeterminacy” refers to the indeterminacy of facts as a matter of tax law when derived from separately indeterminate fields of law. “Mach/Feyerabend factual indeterminacy” refers to fact words as derived from legal theory which provide the content for legal interpretation. The “facts” in tax law are not transcendent to law; in addition, the “fact” words of tax law cannot be simply imported from the field of economics. The incremental question of the origins of theory (as discussed by Karl Popper and Albert Einstein) is also analyzed here. The theory of tax law originates with “sympathy with experience” or “intellectual love” (tr. Einfühlung) of tax law by lawyers as reflected in the special heuristics and practices of the profession. Legal theory accordingly functions in similar fashion to scientific theory where a particular legal theory can be falsified (qua Popper) or understood in pluralistic terms by incorporating auxiliary ideas.*

*Keywords: indeterminacy; legal science; Mach; Feyerabend; Popper.*

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### 1. Introduction

The identification of “facts” is a critical aspect of legal interpretation. If the respective “facts” to which a law will be applied are not consistently determinable then legal outcomes may be indeterminate. But, the potential for *factual* indeterminacy is not what is meant by the general usage of the term “legal indeterminacy”. In the theory of positive law (particularly as relevant to tax law) “legal indeterminacy” refers to the potential for differing interpretations of a given law.<sup>1</sup> For example, where the legislature did not contemplate a particular situation in drafting a law the codified result may then be indeterminate in application. Both legal realists and positive law scholars allow for the potential of legal indeterminacy.<sup>2</sup> However, the question not normally addressed by positive legal theory is: *Where do legal “facts” come from?* Here, the reference to “facts” means the fact words necessary to identify the “facts” relevant to legal interpretation under the law.<sup>3</sup> As recently identified by Mikhail Antonov, Continental European positive law scholars have insufficiently addressed the pertinent question about the origin of legal “facts”.<sup>4</sup> One proposal is that the

<sup>1</sup> See Michael Potács, *Legal Theory* (Vienna: Kluwer, 2015), at ch. V, sec. A, pt. 2 (“Even Kelsen stressed the exact opposite: All previously developed methods of interpretation always lead only to a possible, not a single correct result. The assumption here is that legal positivism constitutes an objective meaning (or content) of legislation. However, this assumption does not exclude the possibility that the objective meaning of legislation is vague or indeterminate.”).

<sup>2</sup> Karl N. Llewellyn, *The Bramble Bush: Some Lectures on Law and Its Study* 26 (New York: Columbia University Press, 1930) (“Is it not obvious that as soon as you pick up this statement of the facts to find its legal bearings you must discard some as of no interest whatsoever, discard others as dramatic hut as legal nothings? And is it not clear, further, that when you pick up the facts which are left and which do seem relevant, you suddenly cease to deal with them in the concrete and deal with them instead in *categories* which you, for one reason or another, deem significant?”); Cristoph Möllers, *Towards a New Conceptualism in Comparative Constitutional Law, or Reviving the German Tradition of the Lehrbuch*, 12(3) *Int’l J. Constitutional Law* 603 (2014) (“Perhaps the most important element in the realist critique of legal concepts has stressed their indeterminacy. This is surprising because there is virtually nobody in the classical formalist era of ‘Begriffsjurisprudenz’ or common law formalism à la Langdell to have claimed that legal concepts were determinate.”).

<sup>3</sup> See *infra* part 3.

<sup>4</sup> Mikhail Antonov, *Systemicity of Law: A Phantasm?* 3(3) *Russian Law Journal* 110 (2015) (“[T]he paradigm of interpretation of reality dictates, or is interrelated with, the paradigm of facts. In continental legal doctrine, the concept of a ‘legal system’ constitutes the predominant paradigm of interpretation, which in turn indicates that law shall be described and interpreted as a whole. Even if this approach can appear intuitively correct within the continental legal paradigm, it remains basically devoid of any serious analytical evidence.”); see also Антонов М.В. О системности права и «системных» понятиях

content of legal “fact” words comes from the meanings of everyday language. And, since legal words have the meaning given in everyday language, positive law scholars are thus able to reject the theory of Ernst Mach (and refined by Paul Feyerabend) that words must derive their content from theory.

Some Continental scholarship says that legal “facts” correspond to everyday language, so if a positive codified law has words, the meaning of those words has some content because it is based on the everyday usage of language.<sup>5</sup> And, that might very well be true in criminal law, for example. Yet, the countervailing thesis given here is that tax words do not correspond to everyday language. This is particularly true of the important tax words upon which international tax planning is conducted. Tax words are not derived from everyday language and often vary in meaning from colloquial usage; for example, a “hybrid” refers to something entirely different in everyday language usage taken in comparison to the usage of tax practitioners. The practical issue can then be given with a hypothetical where a statute is codified that says “All hybrids will be taxed at a rate of 20%.” One (of many) problems is the inherent issue of *factual* indeterminacy in the meaning of the word “hybrid.” Even if an attempt to define the word were made in the positive law, in order to know the meaning of the word “hybrid” in situations *not* covered by the statutory definition (which in taxation often turns out to be *all* situations) one needs to be familiar with the *theory* of taxation. Mikhail Antonov (citing Wittgenstein) nicely explained the backdrop to this view as follows:

[L]aw is not a set of natural facts that can be inspected directly. Rather, it is an “institutional fact” setting out a scheme of interpretation under which certain acts acquire a special meaning. That is why, according to MacCormick, such facts are dependent on human activity. That assignment of meaning to a social fact (i.e., a speech or behavioral act) depends on the scheme of collective intentionality in general, and, for the sphere of law, on frameworks of legal reasoning in each particular legal community.<sup>6</sup>

The alternative is to say that uncovered factual situations are just “null” results under the positive law. To avoid such “null” results, the determination of “facts” must come from the legal theory of taxation and cannot be derived by some combination of positive law and everyday language taken in isolation. The additional question then

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в правоведении, 1 Известия высших учебных заведений. Правоведение 24 (2014) [Mikhail V. Antonov, *On Systemicity of Law and on “Systemic” Notions in Legal Science*, 1 News of Higher Educational Institutions. Legal Studies 24 (2014)].

<sup>5</sup> Potács 2015, at 21.

<sup>6</sup> Antonov 2015, at 117 citing Neil MacCormick & Ota Weinberger, *An Institutional Theory of Law: New Approaches to Legal Positivism* (Boston: D. Reidel Pub., 1986); Ludwig Wittgenstein, *Philosophical Investigations* 198 (Oxford: Wiley-Blackwell, 2009).

arises of: *Where does legal “theory” comes from?* And, notably, both Karl Popper and Albert Einstein addressed that question in identifying the origins of scientific theory.<sup>7</sup> The answer given here with respect to legal theory is effectively the same answer given in the theory of science. That is, legal theory comes from the intellectual love of tax law as reflected in the heuristics and specialized knowledge and practices of tax lawyers. As discussed in detail below, this is a different answer than that given by Hans Kelsen (and as further developed by positive law scholars) who said that legal theory apart from positive law comprises “sociology” or something other than pure law.

*Factual* indeterminacy in legal interpretation is not a “myth” in the context of tax law.<sup>8</sup> In the field of taxation, tax planning is often premised on *factual* indeterminacy. So, the question given here: *Where do legal “facts” come from?* is really the central point of inquiry as a matter of the theory of tax law. A common issue in international tax law is the treatment of a legal entity classifiable either as a regarded entity (i.e., a corporation) or a pass-through entity (i.e., a partnership). This sort of classification issue was at one point so significant to tax law in the United States, the Internal Revenue Service gave up on attempting to classify legal entities as a *matter of fact* and adopted the check-the-box regulations.<sup>9</sup> Under the check-the-box regulations, taxpayers can now elect the *factual* classification of the legal entity and thereby avoid legal indeterminacy as to entity classification. But, in the international context, legal entity classification is still a significant matter of international tax planning because the factual classification of an entity can be mismatched between jurisdictions. The seeking-out of *factual* indeterminacy is actually the primary activity of international tax planning. So, to the extent legal theory ignores *factual* indeterminacy, and focuses only on the positive law concept of general legal indeterminacy, such theory is mostly irrelevant to the actual practice of international tax law. As such, it is necessary to identify precisely the categories of indeterminacy that can arise under the law.

There are at least three forms of indeterminacy in law. Each are listed here with a brief explanation, as follows:

(i) Legal Indeterminacy (i.e., the meaning of the legal provision is subject to doubt).

Llewellyn speaks of premises “mutually contradictory as applied to the case at hand,” and it is important to note that the clusters of premises he has in mind are not formal contradictories as, say, “*Pacta sunt servanda*” and “*Pacta non sunt servanda*”

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<sup>7</sup> Karl Popper, *The Logic of Scientific Discovery* 8 (2<sup>nd</sup> ed., Vienna: Springer, 1935; reprinted: London: Routledge, 2002) (“[M]y view of the matter, for what it is worth, is that there is no such thing as a logical method of having new ideas, or a logical reconstruction of this process. My view may be expressed by saying that every discovery contains ‘an irrational element’, or ‘a creative intuition.’”) citing Albert Einstein, *Mein Weltbild* 168 (Amsterdam 1934) [= *The World as I see It* 125 (A. Harris, tr., London: Lane, 1935)].

<sup>8</sup> John Gardner, *Legal Positivism: 5½ Myths*, 46(1) *American J. Juris.* 199 (2001).

<sup>9</sup> Internal Revenue Code, 26 U.S.C. § 7701 (the “check-the-box” regulations).

would be. The sort of cluster Llewellyn has in mind is not of the form “P and not-P” but of the more complex form “If P then R and if Q then not-R.” Trouble arises only if “the case at hand” presents both P and Q and there is no metarule determining when to follow the “P” rule and when to follow the “Q.”<sup>10</sup>

Here, “legal indeterminacy” means interpretational problems regarding the law itself with the fact words taken as given (perhaps derived from everyday language). This comprises the prior discussion of indeterminacy in the context of positive law and legal theory.

(ii) Factual Indeterminacy (i.e., the judge must find *the facts* to apply the positive law).

Factual indeterminacy in tax law is distinguishable from general legal indeterminacy. Indeterminate fact patterns typically arise where a finding of a separate body of law, such as corporate law, is taken as a matter of fact for the application of tax law. Such situations are ubiquitous to tax practice and continuously arise in new and differing forms. The classic example is Original Issue Discount (OID) where a bond is issued at a discount to par value, which creates factual indeterminacy as to the characterisation of such a discount as either interest income or capital gains (each with differing tax consequences). Other frequent examples as a matter of international taxation include hybrid debt/equity arrangements, transfer pricing of intangibles, and hybrid entity mismatches.<sup>11</sup>

Here, “factual indeterminacy” means the application of indeterminate law taken as “fact” from the perspective of tax law. This is, in part, the denial of the positive law synthesis idea where all law is taken together as one grand structure of which tax law is one component part. In tax law, we need to determine the application of some other substantive area of the law first, then, we proceed with application of the tax law. If the other area of the law is indeterminate (as positive law scholars admit that it is), then we have factual indeterminacy in respect of the tax law. The use of factual indeterminacy in international tax planning is now so ubiquitous this aspect of indeterminacy is probably beyond reasonable question in practical terms.

(iii) “Mach/Feyerabend” Factual Indeterminacy (i.e., *the facts* (or fact words) are dependent upon *legal theory* and special language).

Taking all this into account we see that the theory which is suggested by a scientist will also depend, apart from the facts at his disposal, on the tradition in which he participates, on the mathematical instruments he accidentally knows, on

<sup>10</sup> William Edmundson, *The Antinomy of Coherence and Determinacy*, 82 Iowa L. Rev. 4 (1996).

<sup>11</sup> Bret Bogenschneider, *Manufactured Factual Indeterminacy and the Globalization of Tax Jurisprudence*, 4(2) Univ. College London J. Law & Juris. 250, 251–252 (2015); see also Frans Vanistendael, *Judicial Interpretation and the Role of Anti-Abuse Provisions in Tax Law in Tax Avoidance and the Rule of Law* 132 (G.S. Cooper, ed., Amsterdam: IBFD, 1997) (“The tax avoidance that is considered problematic typically occurs when factual situations are moulded in legal forms that bear less tax than would alternative forms.”).

his preferences, on his aesthetic prejudices, on the suggestions of his friends, and on other elements which are rooted, not in facts, but in the mind of the theoretician and which are therefore subjective... the freedom of theorizing granted by the indeterminateness of facts is of great methodological importance.<sup>12</sup>

Here, "Mach/Feyerabend factual indeterminacy" refers to the origin of facts in the theory held by the practitioner or judge. So, if the legal theory changes then, by necessity, the "facts" also change. There is no transcendent idea of "facts". This is also to say that the meaning of facts is indeterminate.

The remainder of the paper is organized as follows. First, the origin of the indeterminacy thesis is explored in the context of tax law. This frames the importance of the issue to the field of legal theory particularly given that various tax scholars have proposed importing the meaning of words from the field of economics. Second, the question: *Where do legal "facts" come from?* is explored in detail. The conclusion based on Mach/Feyerabend is that facts come from theory. Third, the question: *Where does legal "theory" come from?* is explored. The corollary issue is taken from Popper/Einstein that theories arise from the German word *Einführung* (translated as "intellectual love"). Here, the idea is the heuristics (i.e., specialized language) of the tax profession constitute the theory which gives rise to the "factual" content of words. Finally, the method of replacing legal theories is discussed in the context of tax law.

## 2. The Indeterminacy Thesis

Tax law is derived from many sources. This is true both in Europe and the United States. And, that is simply to say in most countries an underlying tax code codifies a system of positive law, but the tax law also includes principles as determined by courts or the taxing authority in respect of particular cases. In the modern era, this observation is increasingly important for Europe as the common law tax rulings of the European Court of Justice now overlay sharply positive law traditions in much of Continental Europe;<sup>13</sup> in the United States, extensive Treasury regulations are combined with broad enforcement discretion by the taxing authority, which is more characteristic of an inquisitorial legal system.<sup>14</sup> The result is an extraordinary diversity

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<sup>12</sup> Paul Feyerabend, *Realism, Rationalism and Scientific Method: Philosophical Papers Volume 1* (Cambridge: Cambridge Univ. Press, 1981); Paul Feyerabend, *Knowledge, Science and Relativism: Philosophical Papers Volume 3* 12 (J. Preston, ed., Cambridge: Cambridge Univ. Press, 1999) ("A special feature of Mach's philosophy is that science explores all aspects of knowledge, 'principles' as well as theories, 'foundations' as well as peripheral assumptions, local rules as well as the laws of logic; it is an autonomous enterprise, not guided by ideas imposed without control from its own ongoing process."); see Ernst Mach, *Die Analyse der Empfindungen und das Verhältnis des Physischen zum Psychischen* (5<sup>th</sup> ed., Vein, 1906).

<sup>13</sup> See Nial Fennelly, *Legal Interpretation at the European Court of Justice*, 20(3) *Fordham Int'l L. J.* 656 (1996).

<sup>14</sup> See Brian Camp, *Tax Administration as Inquisitorial Process and the Partial Paradigm Shift in the IRS Restructuring and Reform Act of 1998*, 56(1) *Florida L. Rev.* 1 (2004); Bret Bogenschneider, *Foucault and Tax Jurisprudence*, 8(1) *Wash. U. Juris. Rev.* 59 (2015).

of legal thought as applied within the context of international tax law. Any reference to legal indeterminacy means that with this composite jurisprudence of taxation in the practice of international tax law outcomes are often unpredictable.<sup>15</sup>

The legal training of tax lawyers is highly relevant to tax jurisprudence since such training will typically be undertaken either predominantly from a positive law or common law tradition thus reflecting ideas of legal realism. And, as was famously pointed out by William Edmundson, the positive law tradition tends to favor *determinative* outcomes whereas the tradition of legal realism tends to favor *coherent* outcomes.<sup>16</sup> Edmundson explained as follows: “Two appealing ideas about law turn out to be in conflict. The first idea is that the law is or should be *coherent*... the law should or does make sense as a whole, hang together, or fit together. . . . The second idea is that the law is or should be *determinate*. . . fixed and unambiguous.”<sup>17</sup> Many doctrinal debates between tax lawyers trained in the various traditions, such as the role of GAARs (general anti-avoidance rules) reflect at least in part simply a preference for *determinacy* over *coherence*, or vice versa.<sup>18</sup> Tax law is often taught by tax practitioners, and at least as an historical matter, this turns out to be significant because it reflects the distinction between the theories of legal realism of Karl Llewellyn<sup>19</sup> and empirical positive legal science of Christopher Langdell<sup>20</sup> (taken here in parallel to the German-language tradition of Hans Kelsen).<sup>21</sup>

<sup>15</sup> See Ken Kress, *A Preface to Epistemological Indeterminacy*, 85 Nw. Univ. L. Rev. 1340 (1990); Chris Kutz, *Just Disagreement, Indeterminacy and Rationality in the Rule of Law*, 103 Yale L. J. 997 (1994); Nikolas Rajkovic, *Rules, Lawyering, and the Politics of Legality: Critical Sociology and International Law's Rule*, 27(2) Leiden J. Int'l L. 331 (2014).

<sup>16</sup> Edmundson 1996, at 8.

<sup>17</sup> *Id.* at 1–2; Michael Waibel, *Demystifying the Art of Interpretation*, 22(2) European J. Int'l L. 571, 576 (2011) (“Interpretation in international law is a legislative function... counterbalanced by the need for positivism to provide a measure of legal certainty in an international legal order often characterized by a lack of consistency, clarity, and completeness.”).

<sup>18</sup> See Judith Freedman, *Interpreting Tax Statutes: Tax Avoidance and the Intention of Parliament*, 123 Law Quart. Rev. 53 (2007); Judith Freedman, *Improving (Not Perfecting) Tax Legislation: Rules and Principles Revisited*, 6 British Tax Review 718 (2010); John Avery Jones, *Tax Law: Rules or Principles?* 6 British Tax Review 580 (1996).

<sup>19</sup> Edmundson 1996, at 4 (“Llewellyn is making the simple point that deductive reasoning proceeds from premises and, in law, disputed cases typically involve a dispute as to which of two competing major premises should be given effect.”).

<sup>20</sup> See Michael H. Hoeflich, *Law and Geometry: Legal Science from Leibniz to Langdell*, 30 American J. Legal History 95 (1986); Thomas Grey, *Langdell's Orthodoxy*, 45 Pitt. L. Rev. 1 (1983); Nancy Cook, *Law as Science: Revisiting Langdell's Paradigm in the 21<sup>st</sup> Century*, 88(1) N. Dak. L. Rev. 21 (2012).

<sup>21</sup> Hans Kelsen, *The Pure Theory of Law* (Knight, tr., 2<sup>nd</sup> ed., Berkeley: University of California Press, 1967); Hans Kelsen, *The Pure Theory of Law and Analytical Jurisprudence*, 55 Harv. L. Rev. 44 (1941); Jochen von Bernstorff & Thomas Dunlap, *The Public International Law Theory of Hans Kelsen* (Cambridge: Cambridge University Press, 2011); see also Cook 2012, at 29–30 (“The basic principles underlying Langdell's pedagogy have been simply stated: Law involves a scientific analysis able to reveal the life-giving principles of the common law. This science of law could be advanced only by specially trained researchers – not practitioners – who were committed to disciplined analysis... Like other sciences, law should be pursued under circumstances most conducive to scientific thought, viz, in a university rather than in the hurly-burly world of law offices and courts where law is learned, at best, unscientifically.”).

Notably, in his advocacy for law as empirical positive legal science Langdell set out to exclude law practitioners from legal scholarship and instruction entirely.<sup>22</sup>

To set the table on indeterminacy in tax law, let us first consider a general description of legal instruction in international tax law. If you were to sit in on a course in international tax law in nearly any country chances are the professor would at some point begin to draw intricate diagrams comprised of carefully-labeled boxes and circles on the board in the classroom, usually containing sets of arrows or lines connecting the boxes and circles. But, then, something else more important happens: From these diagrams the professor will begin to talk about *tax law* as applied to the boxes and circles; notably, the applicable *tax law* is mentioned only after the boxes, circles and arrows appear on the board. If the course is a matter of tax treaty interpretation the professor will refer to the articles of the applicable tax treaty as *law*. The law can be applied to the boxes and circles in a determinative or “correct” way and the purpose of the legal instruction is to explain that determinative legal analysis to reach the correct answer. However, problems arise where various provisions of law might seem to simultaneously apply to a certain set of boxes and circles. The professor will normally explain how logically to determine which provision of law to apply in that situation based on a certain method of legal interpretation. A test for the tax course will then ultimately be administered to determine if the student was able to apply the proper article of the tax treaty under a new and previously unknown fact pattern, for example. At least in European tax circles, the positive law instruction will usually also involve a brief mention of the countervailing approach of “normative” legal analysis.<sup>23</sup> This is presented as the wrong way to do legal interpretation (i.e., to allow “policy” considerations to enter into the legal analysis). The Kelsenian argument reiterates that the delegates at the Vienna Convention precluded the consideration of “policy” analysis from the international interpretation of treaties. Malgosia Fitzmaurice has published a considerable number of articles emphasizing this distinction between “policy” and “law,” with each article citing Sir G. Fitzmaurice with the famous quote:

This, of course, however excellent, is not law but sociology: and although the aim is said to be “in support of search for the genuine shared expectation of the parties,” it would in many cases have – and is perhaps subconsciously designed to have – quite a different effect, namely, in the guise of interpretation, to substitute the will of the adjudicator for that of the parties.<sup>24</sup>

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<sup>22</sup> Cook 2012, at 29–30.

<sup>23</sup> See George G. Fitzmaurice, *Vae Victis or Woe to the Negotiators! Your Treaty or Our “Interpretation” of It*, 65(2) *American J. Int’l L.* 372 (1971).

<sup>24</sup> See, e.g., Malgosia Fitzmaurice, *Review of Recent Books on International Law* (R.B. Bilder, ed.), 104(2) *American J. Int’l L.* 329 (2010); Malgosia Fitzmaurice, *Book Review: Richard Gardiner, Treaty Interpretation*, 20 *European J. Int’l L.* 952 (2009).

So, every *positive law*-trained tax lawyer ought to know by now *not* to use the New Haven School of legal interpretation because it ostensibly constitutes a violation of the rule of law.<sup>25</sup> Prebble has famously taken this argument to an even further extreme by saying that tax words must correspond directly to natural law or economics to have any meaning, as everything else is “normative” or incomprehensible; “[T]he problem is that lawyers’ and accountants’ distinction between income and capital is not a distinction that is fundamental to natural law, nor to economics, for that matter.”<sup>26</sup> Prebble takes this as true because any legal outcome whatsoever could result from such “normative” interpretation, thus representing a legal outcome the drafters of the tax code did not intend. For now, suffice to say, there is the potential for other methods of legal interpretation that might better account for the indeterminacy of law.<sup>27</sup> As explained in detail below, this can be illustrated by reference to Ernst Mach’s and Paul Feyerabend’s description of science where a parallel issue is described in terms of positive science.

The problem then arises in setting out to actually advise a client in legal practice (say, a multinational engaged in tax planning).<sup>28</sup> On the instance of first setting out to advise the client, the process typically plays itself out as follows: (i) The new lawyer says to the client: “Please give me the diagram of boxes, circles and arrows and I’ll give you the correct legal answer on how much taxes you should pay.” The client then replies, “I don’t have any diagram, that’s exactly why I called you. I want you to construct the diagram so that I don’t have to pay taxes on the upcoming dividend payment.” The new lawyer must then begin to go about making the diagram and quickly discovers that the client must not be found to be in the standard *factual*

<sup>25</sup> Julian D. Mortenson, *The Travaux of Travaux: Is the Vienna Convention Hostile to Drafting History?* 107 *American J. Int’l L.* 780, 781 (2013) (“Rather, the delegates were rejecting Myres McDougal’s view of treaty interpretation as an ab initio reconstruction of whatever wise interpreters might view as good public policy. They objected to the purpose for which New Haven School interpreters wanted to use travaux – not to drafting history as a source of meaning per se. To the contrary, the drafters repeatedly reiterated that any serious effort to understand a treaty should rely on a careful and textually grounded resort to travaux, without embarrassment or apology.”).

<sup>26</sup> John Prebble, *Why is Tax Law Incomprehensible?* 4 *British Tax Review* 380, 388 (1994) (“But the tax lawyer knows that the ultimate answers in taxation can never be found. It is the province of most legal scholarship to build a coherent intellectual discipline on foundations of tested and true principle. The tax lawyer tries to build a coherent intellectual discipline on foundations of sand and clay. That is the real challenge.”); *but see* Bret Bogenschneider, *Wittgenstein on Why Tax Law is Comprehensible*, 252(2) *British Tax Review* (2015); *see also* Christian Zapf & Eben Moglen, *Linguistic Indeterminacy and the Rule of Law: On the Perils of Misunderstanding Wittgenstein*, 84 *Georgetown L. J.* 485 (1996).

<sup>27</sup> *See* Nancy Levit, *Listening to Tribal Legends: An Essay on Law and the Scientific Method*, 58(3) *Fordham L. Rev.* 263, 277–79 (1989) (“Classical analysis, according to the realists, failed to account for the indeterminacy of legal rules and the manipulability of legal reasoning. As a theory of science, classical analysis did not adequately account for changes in law.”).

<sup>28</sup> *See* Jeffrey Waincymer, *The Australian Tax Avoidance Experience and Responses: A Critical Review in Tax Avoidance and the Rule of Law* (G.S. Cooper, ed., Amsterdam: IBFD, 1997) (“University law courses tend to underplay the importance of facts. Students are usually encouraged to concentrate on appellate court decisions and discern principles from them. However the nature of legal practice in general and the tax avoidance area in particular show how fundamental fact finding is to the judicial function.”).

situation as then taxation will presumably result. The client is essentially authorizing the tax lawyer to structure the facts so as to be indeterminate by falling outside the typical “valid legal norm” under a set of facts. Of course, this indeterminacy planning is what international tax planning is all about.

Any easy questions (i.e., where a tax treaty can be simply applied to avoid taxation) without re-structuring the facts are not the predominant part of international tax practice. Gardner described the importance of the “null” (i.e., no valid legal norm on certain facts) result as follows: “If judges are professionally bound to decide cases only by applying valid legal norms to them, the argument goes, then there are necessarily some cases that they should refuse to decide, for there are necessarily some cases not decidable only by applying valid legal norms.”<sup>29</sup> Gardner then describes these as “gaps” in positive law adjudication (the idea of which is also applicable to tax planning). In international tax law characterized by manufactured indeterminacy planning by multinational firms the “gaps” between “valid legal norms” is effectively all international tax planning. So, as a practical matter, any easy questions are quickly resolved, and tax lawyers are working almost entirely on “gap” matters in tax planning. Accordingly, all of the prior sets of boxes, figures and arrows previously contemplated by the new lawyer do not describe the set of facts the lawyer now encounters in the actual practice of law.

So, what to do? At this point, if the problem involves tax treaty interpretation the new lawyer might go and look to the Vienna Convention on the Law of Treaties and finds it necessary to determine original intent as that is the determinative factor in treaty interpretation under the Vienna Convention. If the new lawyer is diligent she might also find various books or law journal articles that say how exactly to interpret Articles 31 and 32 of the Vienna Convention.<sup>30</sup> This might include, for example, situations where the intent seems to have changed, or even to contemplate a situation where the parties did not have a common intent when the treaty was signed. Various commentators say if more than one article applies at the same time we apply the “crucible” approach where everything gets mixed together and then out from the crucible “pops” the determinative result (much like a piece of bread “pops” out of the toaster oven).<sup>31</sup> But, this approach is strange because the fact pattern described here is entirely novel and it could not have been contemplated by the lawmakers in drafting the law.

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<sup>29</sup> Gardner 2001, at 212.

<sup>30</sup> Ulf Linderfalk, *Is Treaty Interpretation an Art or a Science? International Law and Rational Decision Making*, 26(1) *European J. Int'l L.* 169, 175 (2015) (“Despite the existence of Articles 31–33 of the VCLT, to some extent, issues of interpretation still have to be resolved at the discretion of the law-applying agents themselves. The crucial question is whether this makes treaty interpretation an art and not science. As I will argue in the following section, the answer to this question inevitably depends on the approach taken by each and every law-applying agent in disposing of the discretion given to her.”).

<sup>31</sup> Fitzmaurice 2009, at 952 (“The ILC named this system of interpretation a “crucible” approach to treaty interpretation which it describes as follows: “[a]ll various elements, as they were present in any given case, would be thrown into the crucible, and their interpretation would give the legally relevant interpretation.”); Fitzmaurice 2010, at 330.

Nonetheless even if we use the “crucible” approach this still does not render a strictly “positive” result at least from the perspective of the new lawyer. As far as the new lawyer is concerned, there was substantial doubt as to the legal outcome in her mind when she first encountered the problem. This causes a crisis for the new lawyer as she begins to realize that there is no “positive” outcome to the legal question at issue; the new lawyer is “free to choose” (as Jean-Paul Sartre said) from a variety of potential outcomes in advising the client on questions of positive tax law.<sup>32</sup> But the new lawyer does not want to be “free to choose” in classic Sartrean terms. She does not want to tell the client that there is not a determinative legal outcome to the question at bar. The law is supposed to be determinate in application to “facts”; the legislature gave its pronouncement on all questions of law and that ought to be the end of the matter. And, this is merely to observe the tax law is not *determinate*. But, the *common law*-trained lawyer also suffers what might be called a reverse-“existential crisis” particularly in tax treaty interpretation. That is, in the case of the strange “null” result (e.g., double taxation, or, double non-taxation) – where a “null” means the treaty does not apply to the particular “facts” as given. For the common law-trained lawyer the “null” legal result is utterly baffling. The very purpose of common law is to resolve a novel legal problem in the ostensibly best manner; here, there is no potential to legally resolve a problem under the terms of the treaty at all. The lawyer is supposed to arrive at the best resolution of the legal problem.<sup>33</sup>

We are now in a position to respond to Fitzmaurice (in a partial defense of the American system of legal interpretation) as it is premised on resolving issues of both legal and factual indeterminacy. Prior English-language discussions of “law-as-sociology” either disregard the potential for indeterminate outcomes entirely, or refer to the first problem of “legal indeterminacy” and not “factual” indeterminacy. Kelsen’s discussion of “normative” legal interpretation is accordingly incomplete because the theory of legal realism as given by Llewellyn deals in part with the second problem of factual indeterminacy (where the judge must find the facts in order to apply the positive law).<sup>34</sup> Furthermore, at the end of the Nineteenth century legal scholars in the United States first adopted the law as positive science method directly from German legal institutions;<sup>35</sup> this was inspired by Langdell who was the Dean at Harvard Law School at that time. Langdell used the positive legal science methodology (including

<sup>32</sup> See Jean-Paul Sartre: *Basic Writings* (S. Priest, ed., New York: Taylor & Francis, 2001).

<sup>33</sup> See Kutz 1994 citing Ronald Dworkin, *Law’s Empire* 65, 271–275 (Cambridge: Harvard University Press, 1986).

<sup>34</sup> Christoph Kletzer, *Absolute Positivism*, 42(2) *Netherlands J. Legal Phil.* 89 (2013) (“The validity and the content of the positive law cannot be derived from moral premises, then positivism present itself as a negative or relative position, i.e., as the rejection of certain normative relations of derivation. Positivism, understood in this way, first and foremost tells us what law is not.”).

<sup>35</sup> Cook 2012, at 35 (“The German system, from which Langdell borrowed, as well as other civil law systems, still approaches law as a set of fundamental norms which, by deduction, govern operative facts.”).

the common law) to convince other scholarly disciplines within Ivy League institutions that legal studies was a *scientific* discipline; the positive law doctrinal method of case law illustrated that the subject of law was really scientific and worthy of being included in the university curriculum. However, after the legal community succeeded in incorporating legal studies into the university curriculum this method of legal science was quickly abandoned. This was not done to abandon the “rule of law”; rather, the method was abandoned because it was not found to yield determinative, predictable, results since every case seemed to involve a new set of *facts*.

Accordingly, we need to begin any legal analysis by asking the question: *Where do the facts come from?* The “facts” that the lawyers or judge chooses to cognize are based on legal language and often determine the outcome of legal cases as a practical matter.

### 3. Where Do Legal “Facts” Come From?

In the prior section the link between legal analysis and linguistics was formally given; legal “facts” come from language (i.e., linguistic methods) and language is to varying degrees malleable which allows legal words to function on an ongoing basis; Feyerabend wrote: “[A] language does not change by itself. It is a product of the human beings who speak it, and, therefore, it reflects the ideas, the views, and also the behaviour of those human beings.”<sup>36</sup> In this respect, Ulf Linderfalk has very recently applied a linguistic approach to treaty interpretation under the Vienna Convention.<sup>37</sup> In reviewing Linderfalk’s theory, however, Malgosia Fitzmaurice skeptically pointed out that linguistic meanings are not normally investigated in treaty interpretation;<sup>38</sup> furthermore, Linderfalk did not explain why he was engaged in linguistic analysis in treaty interpretation.<sup>39</sup> The reason for linguistic analysis as explained by Feyerabend is that such is necessary for positive law interpretation because a true “stability thesis” for any positive law is unworkable in practice;<sup>40</sup> as

<sup>36</sup> Feyerabend 1999, at 43.

<sup>37</sup> Linderfalk 2015, at 171 (“By the legally correct meaning of a treaty, international lawyers generally understand the communicative intention of the treaty parties – that is to say, the meaning that the parties intended the treaty to express.”).

<sup>38</sup> Fitzmaurice 2010, at 332 (“The VCLT’s textualism is also rejected by Linderfalk in On the Interpretation of Treaties. Instead, he adopts an approach based on linguistics and pragmatics, using terms such as ‘applier’ or ‘utterer’, which are not commonly used in relation to treaty interpretation.”).

<sup>39</sup> Linderfalk 2015, at 172 (“The communicative intention of the treaty parties can only be assumed. Thus, the interpretation of a treaty is no different than the understanding of any verbal utterance produced by a person or group of persons, whether orally or in writing. As emphasized by modern linguistics (pragmatics), an utterance can be understood only on the assumption that whoever produced it acted rationally.”).

<sup>40</sup> Feyerabend 1999, at 40 (“[O]bservation statements are statements which can be explained without reference to theories and whose meaning is also independent of changes in the ‘theoretical superstructure’... I call the claim that the meaning of observation statements is independent of change of theories the stability thesis.”).

he says, pure stability will cause the positive law terminology applied to become subjective in application. Feyerabend wrote: "We are forced to say (as is admitted by all positivists from Berkeley to Ayer) that our elements turned out to be subjective: positivism sooner or later leads to subjectivism."<sup>41</sup> In simple terms, even the purest of positive law systems has to bend (or expand or contract) a little every time it gets applied to a new situation; even if two factual situations are held to be identical the meaning of the words has thus shifted to account for this equivalency. Likewise, Feyerabend's point in logical terms is akin to Llewellyn's in that if the positive law meant previously only P and Q (with no other implications), a determination that it either does or does not entail R must be subjective.<sup>42</sup> Accordingly, Linderfalk is correct in that the shifting of the legal meaning of words is relevant to positive law interpretation; it represents the origin of "facts" into the context of legal theory.

The objective in identifying where "facts" come from in positive tax law is to try to move beyond Prebble's idea that tax law should take its "facts" directly from a transcendent idea of sense-impression-words (tr. *empfindungen*) applicable to all human observations. In economic theory the link from sense impression to empirical knowing is Jeremy Bentham's familiar theory of utility; the field of econometrics has further increasingly moved toward the idea of science as given by Francis Bacon.<sup>43</sup> Feyerabend of course rejected Bacon's approach in the context of the philosophy of science.<sup>44</sup> He wrote:

The principle of phenomenological meaning as well as the principle that descriptions are uniquely determined by facts will appear to be correct and Bacon's philosophy will appear to be the only reasonable one... But this interpretation is not conferred upon them because they "fit", but it is an essential presupposition of the "fitting". This is easily seen when considering

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<sup>41</sup> Feyerabend 1981, at 35.

<sup>42</sup> This is setting aside the "null" result of tax treaty interpretation discussed above.

<sup>43</sup> Feyerabend 1981, at 42 ("According to the realistic interpretation, a scientific theory aims at a description of states of affairs, or properties of physical systems, which transcends experience not only insofar as it is general (whereas any description of experience can only be singular), but also insofar as it disregards all the independent causes which, apart from the situations described by the theory, may influence the observer or his measuring instrument."); see also Feyerabend 1981, at 212 ("First we find the facts (or, 'phenomena', in Newton's terminology). Then we derive laws. Finally, we devise hypotheses for explaining the laws. Hypotheses and facts must be kept apart. It is not the imagination of the theoretician but the skill of the experimenter that determines what counts as a fact and how the facts are to be presented."); Sir Francis Bacon, *Novum Organum* 50 (J. Devey, ed., 1902).

<sup>44</sup> Feyerabend 1999, at 99, 105 ("As is well known, there are empiricists who demand that science start from observable facts and proceed by generalization, and who refuse the admittance of metaphysical ideas at any point of this procedure. For them, only a system of thought that has been built up in a purely inductive fashion can claim to be genuine knowledge... Bacon and Descartes are quite explicit about their enterprise and they oppose common sense from the outset.").

signs whose interpretation has been forgotten; they no longer fit the phenomena which previously evoked their acceptance.<sup>45</sup>

Feyerabend also draws the general idea that a fully stable positivist system is totally content free (i.e., it does not cover any situation at all as a theoretical matter, as is often observed in the actual practice of tax law). He wrote: “[I]t is a theory or a general point of view which has been conserved because it appears to be phenomenologically adequate. The price we have to pay if we proceed in this way is that the chosen theory will finally be completely void of empirical content.”<sup>46</sup> And, this links the current discussion back to the introduction of the new tax lawyer who encounters a client in legal practice. The positive legal knowledge the new lawyer qua scientist thought she had would not *in actual* practice cover the real legal situation. So, positive “facts” (whether in positive science or positive law) come from the malleability of language. The question then is how to incorporate a degree of malleability into positive legal language to avoid a subjective meaning of words.

#### ***a. Feyerabend’s “observational language” versus everyday language***

New language formation can also be divided into borrowing from other disciplines versus created in a “local” context. Positivist scholars in tax law usually have in mind the particular defining of tax words; whereas Prebble has in mind borrowing tax words from natural law or economics. In either case, “[t]his procedure quite obviously presupposes that the meaning of the observational terms is fixed independently of their connection with theoretical systems.”<sup>47</sup> The Mach/Feyerabend thesis of factual indeterminacy is the rejection of the claim given in the prior sentence. As a matter of positive science (here positive law) such linguistics become the “observation method” of language to arrive at facts. Feyerabend wrote:

[L]anguage must satisfy in order to be acceptable as a means of describing the results of observation and experiment. Any language satisfying those conditions will be called an observation language... the condition of decidability... Secondly, it is demanded that in the appropriate situation the associated series should be passed through fairly quickly. This we call the condition of quick decidability.<sup>48</sup>

The immediate question is then how to define what positive law legal “interpretation” actually means. Legal “interpretation” of course forms the basis for

<sup>45</sup> Feyerabend 1981, at 26–27.

<sup>46</sup> *Id.* at 35.

<sup>47</sup> *Id.* at 53.

<sup>48</sup> *Id.* at 18.

nearly all positive law tax analysis. If positive law applies a fixed set of legal terms such “interpretation” ought not to be necessary; the question might be posed as whether “interpretation” is intended to mean something like “translation”. Feyerabend specified that legal interpretation actually means the specification of additional conditions to applying “observational language.” He wrote: “Any complete class of such further conditions will be called an *interpretation*. A particular observation language is completely specified by its characteristic together with its interpretation.”<sup>49</sup>

And, Feyerabend appears to be exactly correct if we look to Linderfalk’s theory of treaty interpretation; Linderfalk expressly began to specify linguistic rules for positive law “interpretation” (and listed them as purported interpretational “rules”). Linderfalk wrote:

Rule 1: If a treaty uses elements of conventional language (such as, for instance, words, grammatical structures, or pragmatic features), the treaty shall be understood in accordance with the rules of that language. Rule 2: If one of the two possible ordinary meanings of a treaty provision makes a part of the treaty redundant, whereas the other ordinary meaning does not, then the latter meaning shall be adopted. Rule 3... [and so on].<sup>50</sup>

This setting out to identify the “rules” of positivist legal “interpretation” leads directly to the proposal for “everyday language” where the transcendent rules will be layered over the transcendent facts. In the terms of Feyerabend, as explained in detail below, Michael Potács said that everyday language is the applicable “observational language” for positive law.<sup>51</sup> However, as discussed in detail below Feyerabend expressly rejected for positive science what Potács proposed for legal theory. Feyerabend wrote:

At this stage it seems appropriate to make a few remarks about the role of everyday language in scientific practice. It has been frequently asserted that the language in which we describe our surroundings, chairs, tables and also the ultimate results of experiment (pointer-reading) is fairly insensitive towards changes in the theoretical “superstructure.” It seems somewhat doubtful whether even this modest thesis can be defended; first, because a uniform “everyday language” does not exist. The language used by the “everyday man” (whoever that may be) is a mixture of languages, as it were,

<sup>49</sup> Feyerabend 1981, at 19.

<sup>50</sup> Linderfalk 2015, at 174.

<sup>51</sup> Feyerabend 1999, at 21 (“[A]n observational concept is a concept which is constructed so that a singular statement which contains only this concept is not only arrived at immediately, without reflecting on it at all, but is also a statement which does not require further justification other than pointing out that a certain observation was made. Observation statements are certain, not hypothetical.”).

i.e., it is a means of communication which has received its interpretation from various and often incompatible and obsolete theories. Secondly, it is not correct that this mixture does not undergo important changes: terms which at some time were regarded as observational elements of “everyday language” (such as the term “devil”) are no longer regarded as such.<sup>52</sup>

Feyerabend further rejected even the idea that “everyday language” could allow for “interpretation”. He continued:

It also becomes clear that the analysis of everyday language cannot provide us with an interpretation either.

On the basis of the foregoing discussion we may now tentatively put forward our *thesis I: the interpretation of an observation language is determined by the theories which we use to explain what we observe, and it changes as soon as those theories change.*<sup>53</sup>

To next apply this philosophy of science to legal theory, Potács declined to apply the Mach/Feyerabend thesis, and argued instead that legal language is always imbued with theory because the legal words correspond to everyday language. Potács argument is that legal words are not generally ascribed different meanings other than ordinary meanings. Potács identified the importance of this line of reasoning in the context of legal theory. He wrote:

This situation is referred to... as “transcendence of perception” that there is no uninterpreted visual sense-data, no “facts” (*empfindungen*: translated as “sense data”) for the purposes of Mach. What sets legal analysis apart is that it is “always given,” law is already interpreted theoretically, decrypted, imbued with hypotheses. The theories in the empirical sciences as the natural or social sciences (economics and sociology) is only a continuation of this practice of everyday knowledge.

But, that claim is obviously contrary to that given by Prebble in the context of tax law, where Prebble claimed that the words of tax law were so far removed from ordinary meanings that it rendered the tax law incomprehensible to lay persons.<sup>54</sup> Bogenschneider subsequently gave the Wittgensteinian response to Prebble that the meaning of tax words was determined by the heuristics of the tax profession. But, this also constitutes a *de facto* rejection of Potács argument for the positive law

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<sup>52</sup> Feyerabend 1981, at 30–31.

<sup>53</sup> *Id.* at 31.

<sup>54</sup> Prebble, *supra* note 26.

in the context of legal theory because the claim is that the “foreign language” of tax words may not be understandable to laypersons. The next point of investigation then is if tax “facts” do not come from everyday language and instead come from legal theory, then *where does “legal theory” come from?*

#### 4. Where Does Legal “Theory” Come From?

The Mach/Feyerabend thesis is that “facts” are not separable from theory.<sup>55</sup> The origin of “facts” is legal theory including positive legal science (as discussed in further detail here). Therefore, it is potentially fruitful to discuss the origin of scientific theory as a matter of the philosophy of science since this parallels the origin of legal theory and the origin of “facts.” However, in the first place there cannot truly be a wholesale importation of words from the field of economics into taxation without substituting also the theory of economics for the theory of taxation. Rather, the “facts” (and also the meaning of words) are malleable and determined by changes in legal theory; “[The] argument against meaning invariance is simple and clear. It proceeds from the fact that usually some of the principles involved in the determination of the meanings of older theories or points of view are inconsistent with the new, and better, theories.”<sup>56</sup> Simply put, as legal theory changes this also changes the words of tax law.

The practice of setting out specialized (i.e., “stable” word meanings) in positive-law tax research may limit the usefulness of that research to future scholars if the meaning of words *necessarily* shifts. However, the use of defined words is a tacit rejection of the everyday language meaning in the context of taxation. New legal ideas that shift the meaning of words are not provided by “facts”, but by legal theory. Feyerabend wrote: “Interpretations of this kind could not possibly emerge from close attention to the ‘facts.’ It follows that we need a non-observational source for interpretations. Such a source is provided by (metaphysical) speculation which is thus shown to play an important role within realism.”<sup>57</sup>

Nonetheless, some tax words are given in ordinary language. This dichotomy within tax law represents the further distinction between “common” and “abstract” theories as explained by Feyerabend (given here as the difference between Potács’ conception of public law and Prebbles’ conception of tax law). Feyerabend discussed further as follows:

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<sup>55</sup> Feyerabend 1999, at 16 (“A concept is a theoretical concept if in order to determine the truth-value of a singular statement which contains it, theories, in addition to observations, are also required. To be brief and imprecise, an observation statement is accepted (or rejected) by merely looking (or listening, etc.). A theoretical statement is accepted or rejected by looking and thinking (calculating).”).

<sup>56</sup> Feyerabend 1981, at 82.

<sup>57</sup> *Id.* at 36.

What has just been said applies most emphatically to the relation between (theories formulated in) some commonly understood language and more abstract theories. That is, languages such as the “everyday language,” that notorious abstraction of contemporary linguistic philosophy, frequently contain (not explicitly formulated, but implicit in the way in which its terms are used) principles which are inconsistent with newly introduced theories, and they must therefore either be abandoned and replaced by the language of the new and better theories even in the most common situations.<sup>58</sup>

However, if tax law is more consistent with Potács’ conception of everyday language as imbued within legal theory, then we would need to observe tax terminology that has a colloquial meaning. The Prebbles also object to any malleability because they see a shift in word meanings as a violation of the rule of law;<sup>59</sup> that issue was also addressed by Craig Latham in response to Prebble along pragmatic lines.<sup>60</sup> To simply continue with Bogenschneider’s helpful example of “Original Issue Discount” (OID) in the tax context – referring to a bond issued below par value – this does not at all comprise ordinary or everyday language usage imbibed with theory. Rather, the words “original issue discount” are meaningless outside the tax context; furthermore, in parallel fashion the concept to which OID refers, i.e., “discounted bond” are meaningless in the context of taxation without reference to the tax concept of OID. The point is, the special tax words “OID” actually are at once the legal theory but the words are not ordinary; this is worth repeating: *Special tax words are imbued with legal theory but the words do not arise from everyday language.*

The conclusion that special tax words do not arise from ordinary language changes the prior results of general legal theory because Potács’ rejection of Ernst Mach on the grounds of everyday knowledge falls apart. So, as explained by Feyerabend in the context of positive science, theory is *necessary* in order to arrive at the meaning of words; “theories shape and order facts.”<sup>61</sup> Feyerabend wrote: “[F]actual adequacy can be asserted only after it has been confronted with alternatives whose invention and detailed development must therefore precede any final assertion of practical success and adequacy. This, then, is the methodological justification of a plurality of theories.”<sup>62</sup>

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<sup>58</sup> Feyerabend 1981, at 78.

<sup>59</sup> Rebecca Prebble & John Prebble, *The General Anti-Avoidance Rule and the Rule of Law* in John Prebble, *Ectopia, Formalism, and Anti-Avoidance Rules in Income Tax Law in Prescriptive Formality and Normative Rationality in Modern Legal Systems* (W. Krawietz et al., eds., Berlin: Duncker and Humblot, 1994).

<sup>60</sup> Craig Latham, *A Tax Perspective on the Infrastructure of Regulatory Language and a Principled Response*, 1 *British Tax Review* 65, 73 (2012).

<sup>61</sup> Feyerabend 1999, at 183.

<sup>62</sup> *Id.* at 80.

An alternative source of legal theory other than setting out definitions of word or importing tax words from economics (qua Prebble) is accordingly required for tax law which is of course legal theory. Legal theory is hence strictly necessary for taxation; and, it will not suffice to simply set out a series of “definitions” of positive terms at the beginning of a tax research paper. An entirely “stable” set of defined terms are meaningless because they are outdated as soon as they hit the page. This conclusion is strikingly reinforced in the context of tax law because multinational firms are constantly “manufacturing” new ideas (i.e., “facts”) to throw at positive law theory. So, the theory of positive law must be highly malleable and not fixed in order to withstand this “manufacturing” of words in the context of taxation. Mach and Feyerabend argue the origins of legal theory are in an historical and pluralistic account of theory. Preston explained:

Pluralism, [Feyerabend] assures us, affords us our best chance of securing knowledge... Knowledge so conceived is an ever-increasing ocean of alternatives, each of them forcing others into greater articulation, all of them contributing, via this process of competition, to the development of our mental faculties.<sup>63</sup>

The pluralistic idea of science as proposed by Feyerabend allows for science in the context of indeterminacy where legal theories are taken as in aggregate comprising a composite, pluralistic, view. Knowledge of as many competing legal theories as possible is therefore desirable for the lawyer or legal scholar since “facts” are derived from legal theory.

## 5. Legal Science and Indeterminacy

The thesis that tax law is “incomprehensible” was given by Prebble in a series of articles and lectures delivered at Vienna University.<sup>64</sup> Prebble develops numerous specific cases where tax law fails to correspond to the underlying economics of the case; with the lack of correspondence, Prebble then arrives at the conclusion that tax law is “incomprehensible” and further violates the “rule of law” because it is not determinative in positive law terms.<sup>65</sup> However, the heuristics of tax law are indeed *knowable* to tax lawyers engaged in the practice of law.<sup>66</sup> Hence, incoherency does

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<sup>63</sup> Preston citing Feyerabend at 5.

<sup>64</sup> See Prebble, *supra* note 26; John Prebble, *Ectopia, Tax Law and International Taxation*, 5 *British Tax Review* 383 (1997).

<sup>65</sup> Prebble & Prebble 1994, at 367.

<sup>66</sup> This view of the science of tax law is similar to that given by Prof. Nagel for positive science. Feyerabend 1999, n. 23, at 83 (“Professor Nagel... [wrote] ‘the expressions peculiar to a science will possess

not preclude positive knowing particularly with the benefit of hindsight. Prebble sets out to correspond tax law to economic reality, which he described as the “physical facts of the world.”<sup>67</sup> This becomes an analogous approach to what Feyerabend termed: “Naive realis[m]. Many scientists and philosophers belong to this group [and] assume that there are certain objects in the world and that some theories have managed to represent them correctly.”<sup>68</sup> The search is for a “pure” theory of law (in Kelsenian terms) that also corresponds to economic “reality” which Prebble refers to as the “physical facts” or “natural law”; that is, a factual description of taxation as analogous to “[s]cientific realism [representing] a general theory of (scientific) knowledge... assum[ing] that the world is independent of our knowledge-gathering activities and that science is the best way to explore it.”<sup>69</sup>

In the context of the philosophy of science, Feyerabend discussed the same issue in reference to the positive theory of physics given by Albert Einstein. Einstein’s version of positive scientific realism looks like Prebble’s vision of tax law as a Kelsenian version of positive economic realism. Einstein, as quoted by Feyerabend, wrote as follows:

Out of the multitude of our sense experiences we take, mentally and arbitrarily, certain repeatedly occurring complexes of sense impressions... and correlate to them a concept – the concept of a bodily object. Considered logically this concept is not identical with the totality of sense impressions referred to; but it is a free creation of the human (animal) mind. On the other hand, this concept owes its meaning and its justification exclusively to the totality of the sense impressions we associate with it. The second step is to be found in the fact that, in our thinking (which determines our expectations), we attribute to this concept of a bodily object a significance which is to a high degree independent of the sense impressions which originally gave rise to it. This is what we mean when we attribute to the bodily object a “real existence.”<sup>70</sup>

The corollary argument for tax law is that the field of taxation attributes significance to the observations of economics to ascertain *factual* significance for application of law. The positive law *theory* should then be built on the economic

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meanings that are fixed by its *own* procedures and are therefore intelligible in terms of its own rules of usage; whether or not the science has been, or will be [explained in terms of] the other discipline.”) citing E. Nagel, *The Meaning of Reduction in the Natural Sciences in Philosophy of Science* 301 (A. Danto & S. Morgenbesser, eds., New York: World Publishing, 1960).

<sup>67</sup> Prebble 1997, at 387 (“The logical separation of the world of physical facts and the world of abstract concepts is the fundamental reason for the difficulty of relating income to a particular jurisdiction.”).

<sup>68</sup> Feyerabend 1981, at 8.

<sup>69</sup> *Id.* at 3.

<sup>70</sup> *Id.* at 10–11.

foundations of these sense impressions (e.g., as Prebble argued in the context of economics a distinction between “income” versus “capital”).<sup>71</sup> Feyerabend applied the positive theory given by Einstein for the illustration that the system of physics is also a construction of the human (qua animal) mind. So, the analogous economic “facts” are subjectively given by the scientists in the choosing of the scientific structure; thus, Feyerabend’s primary objective is to show “facts” are not transcendent to the theory of physics.<sup>72</sup> Feyerabend then identifies the differences between Mach and Einstein as follows: “Mach differs from the positivists ([Einstein’s] version, explained above) in two ways: he does not assume a two layer model of knowledge (except locally) and he examines the historical (physiological, psychological) determinants of scientific change.”<sup>73</sup> In simple terms, this means that positive law is constructed by human beings as an arbitrary set of knowledge conditions that are not transcendent in Kantian terms.<sup>74</sup>

The positive science of physics is similar to the positive science of tax law because it is a human construct (and not a human measurement of a separate physical world); and, again very similar to physics, the problems of the discipline of taxation are not set forth in everyday language.<sup>75</sup> The idea of law as a human construct is actually easier to understand than a transcendent idea of taxation (i.e., taxes as akin to absolute space or time). However, it is Feyerabend’s further averment to scientific *change* that becomes particularly important to the positive legal science idea of tax law. That is, Feyerabend proposes that science is dynamic, not static. Indeed, tax law is seemingly always malleable. And, it is exactly the contrary “stability thesis” central to Prebble’s claim regarding tax law that Feyerabend next addressed:

Any philosopher who holds that scientific theories and other general assumptions are nothing but convenient means for the systematization of the data of our experience is thereby committed to the view (which I shall

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<sup>71</sup> Prebble 1994, at 386 (“The tension between natural law and lawyer’s law is seen in many areas, but nowhere so markedly as in the distinction between capital and income... Explaining the difference between capital income and income items in terms of time illustrates the difficulty of drawing a distinction between the two concepts at all.”).

<sup>72</sup> Feyerabend 1981, at 13 (“In other words, *science explores all aspects of knowledge, ‘phenomena’ as well as theories, ‘foundations’ as well as standards; it is an autonomous enterprise not dependent on principles taken from other fields.*”).

<sup>73</sup> *Id.*

<sup>74</sup> Feyerabend 1999, at 128 (“[T]he new creed generates technical problems of its own which are in no way related to specific scientific problems (Hume), and how there arises a special subject that codifies a science without looking back on it (Kant).”).

<sup>75</sup> *Id.* at 20 (“The problem of the intensity of the gravitational field at a certain location on the earth’s surface is not formulated in everyday language – what one doesn’t know, one doesn’t speak about. But as soon as the problem is formulated there is the possibility of recruiting an entirely everyday action... for solving it ‘by observation.’”).

call the stability thesis) that interpretations do not depend upon the status of our theoretical knowledge. Our first attack against positivism will consist in showing that the stability thesis has undesirable consequences. For this purpose it is sufficient to point out that we make assertions not only by formulating (with the help of a certain language) a sentence (or a theory) and asserting that it is true, but also by using a language as a means of communication.<sup>76</sup>

To briefly summarize, the malleability of words allows for positive science (or, in this case, positive law to shift in meaning) is essential for any workable theory of science or law. However, as will be discussed in detail here, tax words in comparison to general legal words are to a much greater degree not used as everyday language. If tax words are not part of the ordinary language that could change as usage changed over time then we will need to explore other determinants of legal change. Science is not rigid or “stable” sets of definitions followed by deduction syllogisms;<sup>77</sup> however, this idea reflects perhaps a common misunderstanding of positive legal science. The colloquial idea of positive law as legal science (which may correspond to the theory of Bertrand Russell)<sup>78</sup> appears to be premised on an idea of science as “scientific realism” where predictability in legal rules might be achieved through the stability of meaning in legal words. This approach is essentially equivalent to what Feyerabend referred to as “reductionism.”<sup>79</sup> Feyerabend advocated science through a plurality of knowledge; “[plural] knowledge so conceived is an ocean of alternatives channeled and subdivided by an ocean of standards. It forces our mind to make imaginative choices, and thus makes it grow. It makes our mind capable of choosing, imagining, criticizing.”<sup>80</sup> In any case, pursuant to the linguistic explanation set forth above any definition of legal science needs to describe a dynamic (not static) process including the potential for the emergence of new “facts” in positive law; in general, the purpose of legal theory is to encounter these new “facts” particularly in tax law.

To simply explain what Feyerabend meant by the “plurality” idea of science, the easiest way is to distinguish the “reductionist” idea of scientific realism and the

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<sup>76</sup> Feyerabend 1981, at 20.

<sup>77</sup> Feyerabend 1999, at 42 (“[Epistemological problems] are not solved by proofs, but by decisions, as well as by the (empirical or logical) evidence that the decisions are realizable.”).

<sup>78</sup> *Id.* at 41 (“A coherence theory is untenable. It is missing reference to facts, and thus, and this is Russell’s argument, there must be a language which does not depend on any theory, and this is the observation language.”).

<sup>79</sup> *Id.* at 47 (“We must answer Russell’s argument... every language is a theoretical language, i.e., a language which contains an abstract, detailed, and changeable system of categories, and that the observation language is... the sum of all those parts of different theoretical languages now in use, of which human individuals can quickly come to a decision which will be unanimous.”).

<sup>80</sup> *Id.* at 184.

“instrumental” idea of scientific method given by Popper.<sup>81</sup> Feyerabend explained the distinction as follows:

[One might] den[y] a descriptive function to the sentences of a theory and by declaring that these sentences are nothing but parts of a complicated prediction machine (instrumentalism), or by conferring upon these sentences an interpretation that completely depends upon their connection with the observational language as well as upon the (fixed) interpretation of the latter (reductionism).<sup>82</sup>

Simply put, the reductionist idea of legal science corresponds to the inductive problem which Popper was trying to address. Feyerabend explained this by reference to Aristotle where the idea is to inductively verify sets of claims to arrive at truth.<sup>83</sup> Potács concisely explained as follows:

In traditional terms verification of a theory is carried out in accordance with the “principle of induction”, which can be inferred from a number of individual observations on the accuracy of a general statement. Accordingly, the verification due to an inductive inference is both a criterion of demarcation between “empirical-scientific” and “metaphysical” theories as a methodological principle of the empirical sciences.<sup>84</sup>

### ***a. The Testing of Legal Theory by Theory***

Popper set out to eliminate the metaphysical (i.e., inductive) verification element of theory. Popper did this by tearing down rather than building up; that is, by identifying what scientists do as falsifying rather than verifying. This focuses on using empirical verification to falsify theory based on the observed results. Feyerabend gave the “instrumental” terminology for Popper’s method as follows: “Instrumentalism maintains that the new theory must not be interpreted as a series of statements, but that it is rather to be understood as a predictive machine whose elements are tools rather than statements and therefore cannot be incompatible with any principle already in existence.”<sup>85</sup> Again, Potács concisely described Popper’s falsification method of science:

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<sup>81</sup> Feyerabend 1999, at 183 (“One answer which is no longer as popular as it used to be is that science works by collecting facts and inferring theories from them. The answer is unsatisfactory as theories never *follow* from facts in the strict logical sense.”).

<sup>82</sup> Feyerabend 1981, at 52.

<sup>83</sup> Feyerabend 1999, at 146 (“The rule that a theory which contradicts experience must be excluded from science and replaced by a better theory was invented by Aristotle.”).

<sup>84</sup> Potács 2015, at sec. B, pt. 3.

<sup>85</sup> Feyerabend 1981, at 83.

The falsification as demarcation criterion means, as I said, that only those theories are “not metaphysical” are regarded as “scientific.” The check is based on the empirical reality and will refute most theories. Such a review is carried out by statements about observations of individual events, which are called “log records” or “base sets.” This is mainly for the legal rules of interpretation of meaning that can be regarded as theories of language use. On the applicability of the falsification principle is conceivable as a demarcation criterion. Accordingly, only those rules of interpretation should be recognized as lawful for the interpretation, their acceptance and use in the practice of communication can be checked refutable by observation.

Potács then explores whether it is plausible to link Kelsen to Popper as a matter of legal theory. Obviously, for a German-language legal audience linking Kelsen and Popper has extraordinary appeal because it would render legal science a function of positive law norms, exclusively. Potács concludes that positive law is based on everyday language, but does not constitute “empirical” science; “[a]lthough is now the status of the legal doctrine as science largely beyond dispute, if one understands science gained under due process of rational knowledge. However, it seems doubtful whether the legal doctrine may be regarded as ‘empirical’ science.” Potács then quotes Kelsen for legal theory,<sup>86</sup> and says that law is built on everyday language with the facts and theory implicit.<sup>87</sup> He wrote:

Natural languages have to a greater uncertainty than formal art languages. The importance of formal art languages is determined by fixed rules, while on the other hand in natural languages the meaning of expressions is characterized by its practical use... [S]ince laws are written in natural language, they are also to be interpreted according to the rules in everyday language. Because right to use translators to communicate their arrangements of natural language, they want to be understood according to the rules of natural language.<sup>88</sup>

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<sup>86</sup> Potács 2015, at ch. V, sec. A, pt. 1 (“Hans Kelsen said as follows: “If within the meaning of philosophical positivism may be the subject of a science only the ‘given,’ and the given... facts, can the postulate of philosophical positivism in provisions no, or at least are not directly applicable, since legal norms are no facts but the sense of facts, namely the sense of looking at human behavior as volitional acts”)

<sup>87</sup> *Id.* (“Rather, in particular Karl Popper and Hans Albert have shown that any form of perception occurs because of a theoretical pre-knowledge and is thus ‘bound by theory’ [here, everyday language]. This is especially true for everyday observations (e.g., a glass of water), which is always certain theoretical ideas (e.g., on certain regular features of a ‘glass’ and ‘water’ in it) require.”).

<sup>88</sup> *Id.* at ch. V, sec. A, pt. 1.

Potács then goes on to say that the results of legal theory can be observed rendering them partially scientific.<sup>89</sup> However, the idea of tax terminology as everyday language does not seem to be apropos; the practical end result of Potács' analysis of Kelsen, Popper (and Alberts) seems to be that law is itself typically everyday language and therefore partly scientific to the extent it relies on testable observation; and, thereby rejecting Ernst Mach's claim that there must be ideas in language beyond the everyday usage of language. This would presumably allow for empirical testing by falsification under the Popperian conception of science if legal words.<sup>90</sup>

Simply put, lawyers in a common law jurisdiction apply legal theory to what Gardner called "gap" situations as a matter of tax planning or in adjudication of tax disputes. Where the positive tax law as set forth in the statute and is not sufficient then the theory of tax law is the means to resolve the "gap" thereby avoiding the potential for "null" results under a strict version of positive law. An obvious illustration (as previously given in the tax context) is OID (original issue discount). If a bond is intentionally issued below par value to create built-in gain as opposed to interest, thereby changing the applicable tax rate, every tax lawyer in the world ought to know that looks like OID. The OID term has been codified in many countries including the United States.<sup>91</sup> In other words, the legislature actually codified the existing heuristics of the tax profession (which is what we would expect to see in a healthy legal system). Of course, that word came from theory where a tax lawyer somewhere acted with "intellectual love" to create the terminology of "OID" which was then rightfully incorporated into law.

And, this process of the codification of tax words happens in a quasi-scientific manner as different tax lawyers propose novel means, for example, to deal with a discounted bond as a matter of tax practice. Such scientific analyses of tax theory can be found in law journals. As an example, a Popperian article on discounted bonds might say that the understanding of interest/capital gain must be abandoned entirely (i.e., falsification) in favor of some other approach to taxation in light of the

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<sup>89</sup> Potács 2015, at ch. V, sec. A, pt. 2 ("Decisive for the determination of this 'will' of a translator, and thus the contents of positive legal norms are thus the rules in everyday language. These rules in everyday language can be divided into semantic and pragmatic rules. Under semantics is understood here linguistic communication with due regard to the usual in the language use of words (word semantics) and sets (set semantics).").

<sup>90</sup> *Id.* at pt. 2 ("So it's not as if the group referred to Kelsen some sciences (such as the natural or social sciences) with 'facts' involved and in contrast, the legal doctrine of 'the sense of facts' incorporated... Between the findings of the natural and social sciences and the legal doctrine in this respect there is no difference, because the knowledge of the legal doctrine constitute (legal norms) interpretations of sensory perceptions (e.g., texts) in the light of theories (interpretation rules than general statements about the use of language). It follows that the findings of the natural and social sciences alike as those of legal doctrine 'not direct observation, but only the understanding accessible' are... 'immediate perception' is possible in any of these studies. The legal doctrine is therefore the natural and social sciences to the extent 'empirically equivalent.'").

<sup>91</sup> Internal Revenue Code, 26 U.S.C. § 1273 ("Determination of Original Issue Discount").

new practice of the issuance of discounted bonds to avoid the payment of interest which renders the prior theory incoherent. Another article might say that a new auxiliary concept (such as OID) can be incorporated into the theory of “interest” known by tax lawyers to augment the existing theory of interest/capital gains. In any case, the factual content of the word “interest” is subject to change based on the heuristics and practices of the tax profession which we call the “theory” of taxation. The evolution of such legal theory is similar to the evolution of scientific theory.

## 6. Conclusion

Mach/Feyerabend factual indeterminacy refers to the first identification of a situation that cannot be expressed under the existing framework of tax words. An obvious historical example might be a limited liability company defined as a partnership for tax purposes under the laws of the United Kingdom, but which is treated as a corporation in the Netherlands. Of course, this eventually came to be known as a “hybrid” entity for purposes of tax theory, likewise new circumstances eventually gave rise to the term “reverse-hybrid”, and so forth. Notably, once the new words (i.e., hybrid, reverse-hybrid) exist it is still possible to have general factual indeterminacy under the tax law, but at least the word-categories exist to formulate a decision about the “facts.” This example should further illustrate that the proposal everyday language would suffice for tax law is clearly unsatisfactory; such an idea is ostensibly inapplicable in the tax context (i.e., since as an example “hybrid” now actually refers to a car in colloquial language).

The phenomenon of Mach/Feyerabend factual indeterminacy is of further significance to international tax law for at least the following three reasons. First, an additional answer can be given to the Fitzmaurices in the repeated criticisms of the (non-positivist) common law of taxation. For example, if a strict positive law were applied to a previously unknown form of legal entity (i.e., a “limited liability company”) the tax classification of that entity would be automatically *subjective* as explained by Feyerabend; at the minimum, legal entity classification would then be determined under Rule 1, 2, 3, and so on, in the manner akin to that given by Linderfalk under interpretation of the Vienna Convention. But, in the case of an interpretational rule of original legislative intent, the positive law could potentially be *more subjective* than a form of legal realism under the common law. Indeed, there is no possibility of achieving legal coherence where identification of original legislative intent cannot operate because the category of “fact” did not exist when the law was drafted.

Second, the importation of words from economics cannot remove incoherency from the field of taxation. Take the example of an economic *profit*. Each of wages, capital gains, even gifts might meet the condition of the economic word “profit”; note further that *inflation* is typically *not* considered economic profit (yet it is taxable).

Where a common law court encounters a question of measuring “taxable income” it actually cannot use the economic definition of profit (even the Haig-Simons definition) without incorporating some (or even all) aspects of economic theory. So, economic “fact” words like “profit” cannot simply be substituted even for *exactly the same word* if that word happened to appear in the positive law. As Feyerabend explained, this is a nonsensical proposal for tax law; the “factual” meaning of words must be determined by the operation of the *legal theory* of taxation just as in any other area of the law. Accordingly, the idea of “profit” as a “fiction” (and weakness of the tax system) as Prebble stressed is not helpful as a matter of legal theory;<sup>92</sup> to the contrary, such flexibility in encountering new situations with shifts in the meaning of words is a fundamental aspect of any legal (or scientific) system.

Third, with Mach/Feyerabend factual indeterminacy the importance of the GAAR to tax systems becomes rather obvious. In the situation where a new “fact” word arises, as under a codified system of tax law, such would automatically create an “interpretational” dilemma for strict positive law systems in particular.<sup>93</sup> The GAAR then becomes appealing where legal theory has been partially excluded from the law under a positive law framework.

In conclusion, legal theory functions in much the same manner as scientific theory. Tax lawyers function as clinicians of taxpayer behavior and with practical knowledge are in position to derive legal theory (and, to test it). Potács provided an extensive explanation of the limits of the falsification method vis-à-vis Popperian theory for positive legal science. A further limitation of the Popperian theory of scientific method was given by Feyerabend in that even falsified theories still contribute new concepts to science. Perhaps the most important lesson from the philosophy of science with respect to tax law is Feyerabend’s link between “facts” and theory. He wrote: “[T]he descriptions of the observable facts contradict a theory often only because the concepts with which they were formulated belong to older theories. In this case, the contradiction is not between theory and ‘fact,’ but between newer theory and older theory.”<sup>94</sup> Accordingly, the idea of “naïve scientific realism” previously offered as critique of tax law as “fictions” (reflecting the idea that legal theory does not properly reflect economics “facts”) radically understates the fundamental importance of legal theory to tax law. For example, if legal theory were found not to correspond to “economic reality” in a given situation this reflects merely a difference as between legal theory and economic theory and accordingly not a misapplication of economic “facts” by lawyers.

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<sup>92</sup> Prebble 1994, at 387.

<sup>93</sup> See Judith Freedman, *GAAR as a Process and the Process of Discussing the GAAR*, 1 British Tax Review 22 (2012).

<sup>94</sup> Feyerabend 1999, at 169.

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