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VICTORIA UNIVERSITY OF WELLINGTON LEGAL RESEARCH PAPERS

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**JOHN PREBBLE, EDITOR**
Professor of Law, Victoria University of Wellington, Honorary Research Fellow, Monash University
**john.prebble@vuw.ac.nz**



## Announcements

Special Issue: Ectopia, Fictions, and Autopoiesis: Income Tax Law from Perspectives of Analytical Jurisprudence, papers by John Prebble and co-authors

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# LEGAL SCHOLARSHIP NETWORK: LEGAL STUDIES RESEARCH PAPER SERIES
# VICTORIA UNIVERSITY OF WELLINGTON LEGAL RESEARCH PAPERS

**"Why is Tax Law Incomprehensible?"**
*British Tax Review, Vol. 4, pp. 380-393, 1994*
*Victoria University of Wellington Legal Research Paper No. 26/2011*

**JOHN PREBBLE**, Victoria University of Wellington, Monash University
Email: John.Prebble@vuw.ac.nz

Since the introduction of the Land and Income Assessment Act 1891 income tax has become the biggest earner of government revenues in New Zealand. Its development has been intrinsic to the creation of the modern civic infrastructure that the country now enjoys. However, it is an incomprehensible, challenging beast with tensions and contradictions littered throughout its complex systems of laws. This article offers a number of suggestions for the cause of complexity of income tax law and as to why it is so resistant to improvement.

**"Ectopia, Formalism, and Anti-Avoidance Rules in Income Tax Law"**
*PRESCRIPTIVE FORMALITY AND NORMATIVE RATIONALITY IN MODERN LEGAL SYSTEMS, p. 367, W. Krawietz, N. MacCormick, G.H. Von Wright, eds., Duncker and Humblot, 1994*
*Victoria University of Wellington Legal Research Paper No. 27/2011*

**JOHN PREBBLE**, Victoria University of Wellington, Monash University
Email: John.Prebble@vuw.ac.nz

Governments attack tax avoidance in a number of ways. Statutory anti-avoidance rules are one means. Such rules come in two forms: specific and general. General rules potentially apply to any kind of transaction that may result in tax avoidance. Section 99 of the New Zealand income Tax Act 1976 is a typical example of a general rule. Similar rules are included in the tax legislation of Australia, Canada, Hong Kong, Malaysia, and Singapore. The United States and the United Kingdom are two notable exceptions.

Fundamental flaws in the concept of income, such as the artificial concepts of space, time, and the capital/revenue distinction, contribute to an ectopia in tax law. “Ectopia” refers to a characteristic that distinguishes tax law from most other areas of law: the fact that tax law is in a sense detached and dislocated from its subject matter. Not surprisingly, the greatest opportunities for tax avoidance occur where the ectopia of tax law is most apparent. In response, large parts of the income tax legislation are given over to specific rules that are calculated to frustrate avoidance.

**"Ectopia, Tax Law and International Taxation"**
*British Tax Review, No. 5, pp. 383-403, 1997*
*Victoria University of Wellington Legal Research Paper No. 28/2011*

**JOHN PREBBLE**, Victoria University of Wellington, Monash University
Email: John.Prebble@vuw.ac.nz

"Ectopia" is a label given here to a feature of tax law that distinguishes it from most other forms of law. Income tax law is dislocated from the facts to which it relates. This dislocation leaves a gap, or "ectopia" between tax laws and the economic facts of the transactions or structures to which it relates. The ectopia of income tax law is pathological, serious and incurable, although governments strive to alleviate the problems to which the conditions give rise.

Problems that result from the ectopia of tax law or generally acute and particularly resistant to cure. The reason is that income tax taxes gains, but not all gains. Thus, there must be a concept of income. The concept of income cannot be defined by law because it is not something that exists as a physical fact or as an abstract thought like most other characteristics in law. What makes "income" fictional are the factors of space, such as geograhpical limits imposed by states, and time, which attempts to divide indefinite steams of profits into year long blocks, a process that underlies the essential irrationality of the capital/revenue distinction. Tax systems struggle to find ways of coping with the consequences of these fictions. This struggle results in problems with, inter alia, double taxation, withholding taxes, transfer pricing, and with controlled foreign companies.

**"Fictions of Income Tax"**
*Victoria University of Wellington Legal Research Paper No. 29/2011*

**JOHN PREBBLE**, Victoria University of Wellington, Monash University
Email: John.Prebble@vuw.ac.nz

We cannot have an income tax without a concept of income. For a number of reasons, our concept of income must be artificial. A principal reason is that income tax law generally taxes the results of legal transactions rather than their underlying economic substance, which causes a dislocation between tax law, on one hand; and business profits and other targets of tax law; on the other. In order to make income tax work at all, the law must make a number of assumptions that are not in fact correct, assumptions as to both the factual and the legal nature of the taxpayer's income. Particular reasons for the dislocation between income tax law and economic profits are, inter alia, that the law taxes the legal substance of transactions rather than the economic substance, the problem of place, and the problem of time. The author uses the term "ectopia" to identify this dislocation. In this article, the author addresses criticisms made of the ectopia thesis, namely, that accountancy rules are similar in character to income tax rules, that more detailed legislation could cure these ills, and, especially, that the law is well used to fictions.

**"Income Taxation: A Structure Built on Sand"**
*Sydney Law Review, Vol. 24, No. 3, pp. 301-318, 2002*
*Victoria University of Wellington Legal Research Paper No. 30/2011*

**JOHN PREBBLE**, Victoria University of Wellington, Monash University
Email: John.Prebble@vuw.ac.nz

There are several fundamental problems with the judicial concept of income, that is, the concept of income that the courts employ for tax purposes. First, the judicial concept sees income as a flow, rather than as a gain. Secondly, as a consequence, it taxes some apparent flows that do not entail gains. Thirdly, it omits gains that we call capital gains. Fourthly, it relies on legal transactions rather than underlying economic movements. The fictions of income tax law are of a different character from other legal fictions in that the classic legal

fiction entails pretence, but taxation fictions entail duplicity. These factors lead to ectopia, that is, a dislocation between tax law and the economic transactions to which it relates.

The ectopia of tax law explains why that law is unduly complex, why it is difficult, if not impossible, to simplify tax codes, and how general anti-avoidance laws are justifiable. Another consequence of ectopia is that people are forever trying to reform and improve income tax. The tax value method was one such attempt to respond to ectopia.

Ross Parsons predicted the demise of income tax because of the dislocation of tax law from the economic substance its addresses. Nevertheless, it appears that income tax will be with us indefinitely, despite its being terribly flawed. The result is a need to employ a patchwork approach in addressing shortcomings in the law.

**"Autopoiesis and General Anti-Avoidance Rules"**
*Critical Perspectives on Accounting, Vol. 21, pp. 545-559, 2010*
*Victoria University of Wellington Legal Research Paper No. 31/2011*

**GERALDINE HIKAKA**, Edmund Lawler & Associates Limited
Email: ghikaka@xtra.co.nz
**JOHN PREBBLE**, Victoria University of Wellington, Monash University
Email: John.Prebble@vuw.ac.nz

Autopoiesis is a post-modern, essentially positivist theory that tries to describe the true nature of law. Its principal tenets are the ideas of self-reproductive growth from reasoning that is self-referential and recursive, relative autonomy from, and "operative closure" against, other social systems, together with "cognitive openness" to "irritation" and to "noise" from outside the closed circle of the law.

The authors are skeptical about the ability of autopoiesis theory to illuminate the nature of law in general, but see it as shedding useful light on income tax law, particularly the quality that income tax law shows in inventing legal structures that have no reality beyond the world of fiscal affairs.

The authors argue that the general anti-avoidance rule punctures the autonomy and closure of income tax law, to allow the substantive norms of the economic and business system free play, or relatively free play, within tax cases. That is, while income tax law is in general a good example of legal autopoiesis, this observation is incorrect when a general anti-avoidance rule is in play.

Two implications for accounting are (a) that the operative closure of law results in a disconnection between income tax law and accountancy, and (b) that a general anti-avoidance rule may repair this disconnection in cases where accountancy records are governed by substance rather than form.

**"Justice Hill and the Autopoiesis of Income Tax Law"**
*Victoria University of Wellington Legal Research Paper No. 32/2011*

**JOHN PREBBLE**, Victoria University of Wellington, Monash University
Email: John.Prebble@vuw.ac.nz

The theory that law may best be understood as an autopoietic system has gained considerable ground since Luhmann advanced it in 1981.

Nevertheless, there have been few endeavours to apply the theory in any practical way or to

employ it to analyze particular areas of law. In a recent paper, Geraldine Hikaka and the present author proposed the thesis that Luhmann's theories usefully illuminate the field of income tax law. The present paper illustrates this thesis by analyzing a leading case from each of the Privy Council and the High Court of Australia, namely Europa Oil (NZ) Ltd v Commissioner of Inland Revenue and Federal Commissioner of Taxation v South Australian Battery Makers Pty Ltd. The paper will argue that the autopoietic nature of income tax law presents challenges to the judicial process that, as these cases illustrate, lead to income tax law becoming detached from the business profits that are an important part of its subject matter.

The paper will then turn to Macquarie Finance Ltd v Federal Commissioner of Taxation, one of the last tax judgments of the late Justice Graham Hill. It will be argued that in Macquarie Finance Ltd Justice Hill demonstrated a rare, almost unique, ability among judges: to reconcile the formalistic, autopoietic nature of tax law with the business substance that was the subject matter of the case. The paper turns first, however, to the question of what is meant by the autopoietic theory of law.

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## Solicitation of Abstracts

The Victoria University of Wellington was founded in 1899 to mark the Diamond Jubilee of the reign of Queen Victoria of Great Britain and of the then British Empire. Law teaching started in 1900. The Law Faculty was formally constituted in 1907. The first dean was Richard Maclaurin (1870-1920), an eminent scholar of both law and mathematics. Maclaurin went on to lead the Massachussetts Institute of Technology as President in its formative years. Early professors included Sir John Salmond (1862-1924), still one of the Common Law's leading scholars. His texts on jurisprudence and torts have gone through many editions and remain in print.

Alumni include Sir Robin Cooke (1926-2006), one of the leading judges of the British Commonwealth. As Baron Cooke of Thorndon, he sat on over 100 appeals to the Judicial Committee of the House of Lords, one of very few Commonwealth judges ever appointed to do so.

Since 1996 the **Law School** has occupied the Old Government Building in central Wellington. Designed by William Clayton and opened in 1876 to house New Zealand's then civil service, the building is a particularly fine example of Italianate neo-Renaissance style. Unusually among large colonial official buildings of the time it is constructed of wood, apart from chimneys and vaults.

The School is close to New Zealand's Parliament, courts, and the headquarters of government departments. Throughout Victoria's history, our law teachers have contributed actively to policy formation and to law reform. As a result, in addition to many scholarly articles and books, the Victoria SSRN pages include a number of official reports.

Victoria graduates approximately 230 LLB and LLB(Hons) students each year, and about 60 LLM students. The faculty has an increasing number of doctoral students. Ordinarily there are ten to twelve students engaged in PhD research.

Victoria University observes the British system of academic ranks. In North American terms, lecturers and senior lecturers are tenured doctrinal scholars, not legal writing teachers. A senior lecturer corresponds approximately to a North American associate professor in rank.

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