

# PROBABILITY AND THE LAW

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READING GUIDE – WEEK #8

**Lawsky.** In PART I, you'll read about two interpretations of probability: frequentist (p. 1027) and subjective (pp. 1027–1031).

In PART II, you'll read about tax law uncertainty. Pay particular attention to how the two interpretations of probability are relevant to understanding in what sense a tax position has a certain probability of being correct. The frequentist interpretation is discussed on pp. 1037–1041; the subjective interpretation on pp. 1041–1044. Lawsky claims that the subjective interpretation of probability statement is more suitable in the context of tax law. Pay attention to her argument on page 1038.

in PART III, Lawsky draws three implications of her claim in PART II. The first implication is that if lawmakers and taxpayers assign different (subjective) probabilities to whether a tax position is correct, a welfarist approach can support fault-based penalties. The second implication is that a subjective interpretation of tax probability statements provides a justification for regulations that impose rigorous requirements on how tax advisors should draft tax opinions. The third implication is that (given the subjective interpretation of tax probability statements) if taxpayers are averse to uncertainty, making tax law more predictable might decrease compliance.

**Response paper.** In the response paper for this week, please do the following:

**First.** State what it means that a tax position has an  $x$  percent probability of being correct, according to the subjective interpretation of probability and according to the frequentist interpretation. State Lawsky's argument for preferring the subjective interpretation.

**Second.** Explain equation (2) on page 1053 and explain Lawsky's statement that "if this is the relationship between  $\theta$  and  $q$ , then marginal-deterrence theory would require fault-based penalties: penalties would be higher when the taxpayer believed with greater-than-50% certainty that her position was incorrect" (p. 1056) (In particular, briefly describe marginal-deterrence theory, fault-based penalties, and the variables  $\theta$  and  $q$ .)