

INTERPRETATION OF TAX LEGISLATION

LITERAL, TELEOLOGICAL AND ECONOMIC INTERPRETATION IN THE ITALIAN PERSPECTIVE

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LITERAL INTERPRETATION

Definition, Application and Boundaries

In the Italian legal system there is a fundamental rule regarding the interpretation of law: it is **Article 12**, titled '*Interpretation of the Law*' of the **Provisions on the law in general**, preliminary to the Civil Code (March 16, 1942).

- According to the criteria set out in **Article 12** the **literal interpretation** of the law is the starting point for any interpretative process; it involves attributing to the text the meaning that the statement expresses on the basis of linguistic rules, both semantic - concerning the meaning of the words and terms that compose it - and syntactic, concerning the position of these words and terms and the relationships between them.
- The '**meaning of a word**' is that attributed to it by the '**language**' used to write a legal provision
- In order to understand the '**literal**' **meaning of a word** in a legal text, the interpreter cannot ignore the rules of grammar, which are external (or, rather, pre-existing) to the legal provision

THE IMPORTANCE OF LEGISLATIVE WORDING IN THE ITALIAN CONSTITUTIONAL COURT APPROACH

The Italian Constitutional Court (no. 110/2023) admonished the legislator to *'comply with minimum standards of intelligibility of the meaning of legislative propositions'* with regard to *'rules governing the generality of relations between the public administration and citizens, or the mutual relations between the latter'*, highlighting how *'irretrievably obscure provisions, and therefore harbingers of intolerable uncertainty in their concrete application, are contrary to the principle of reasonableness of the law referred to in Article 3 of the Constitution'*.

THE INTERPRETATION OF LEGAL CONCEPTS BORROWED FROM OTHER AREAS OF LAW

- A traditional problem in Italian tax law is the interpretation of **legal concepts borrowed from other areas** of law, which, especially in the past (but also now), has been linked to the lively debate on the **autonomy of tax law** with respect to other areas of legislation.
- The question arises as to whether, where the tax legislator uses terms that have taken on a certain meaning in other sectors, or are expressly defined, the interpreter is required to attribute the **same (original and previous) meaning** or **adapt that definition** to the tax field.

INTEGRALIST OR ANTI-AUTONOMIST THESIS

- According to this thesis, the need to safeguard the **unity of the legal system** and **terminological consistency**, requires the interpreter to attribute to the words and institutions referred to in tax law the meaning they have in the legal sector to which they (originally and previously) belong, according to the model of **intra-institutional linkage**.
- The interpretation must start from the literal meaning of the provision, from which **it is possible to deviate** in order to admit an interpretation according to the so-called '*intention of the legislator*' ('ratio legis' or underlying reason or logical basis of the law), **only if the latter is compatible with the rule itself and is expressly provided for**.
- The literal meaning of the statement represents the boundary/limit to the application of the teleological (purposive or functional) method. **This boundary can only be exceeded in exceptional cases, expressly provided for by the law.**

ITALIAN CASE LAW

- In a case of indirect taxation of a corporate demerger, the Court of Cassation defined the scope of application of Article 4 Law no. 131/1986, which regulates **registration tax**, limiting its application to a fixed amount (rather than a proportional amount), by virtue of a **literal interpretation** of the regulatory provision that distinguishes between **companies** and **entities other than companies** (C. C. no. 2305/2022)
- In a case on the **tax regime for sports associations**, the Court of Cassation reiterated the established principle that **tax relief rules are to be interpreted 'strictly'** (C. C. no. 17976/2021)
- In a case concerning the **extension to VAT** of the **benefits** provided for in Article 11 of Law no. 289/2002 on **registration, mortgage and cadastral taxes** for the purchase of a **first home**, the judges of legitimacy specified that the aforementioned benefits "are in no way applicable to cases and situations **not attributable to the relative literal meaning**" (C. C. no. 18574/2016)

THE 'AUTONOMIST' THESIS

- According to this thesis, the interpreter has to attribute to words and institutions a **meaning** that is '**proper**' to **tax law** and therefore different from that of civil law, on the basis of the existence of with respect to other legal domains. **principles of tax law**, which would **make it ontologically peculiar and autonomous**
- In **the most recent**, in-depth and mature elaborations of the autonomist thesis, there is a **tendency to opt for a casuistic approach (case by case)**, which allows one to go beyond semantic consistency in specific cases **supported by particular justifications.**

THE PREVAILING THESIS

- **Tax legislation is second-level legislation**, which (often) involves pre-existing legal phenomena in other areas of law,
- therefore, **words and concepts** specific to other branches of law must be given **the meaning they have in the previous branch of origin**.
- This does not necessarily mean that the term cannot take on a different meaning in tax law from that which it has in its domain of origin, **but the assignment of a different meaning** must in fact be considered an **exception and not a mere and physiological function of the reference to the context**
- This **different meaning** has to be allowed only when expressly **provided for by the rule**.

PURPOSIVE/TELEOLOGICAL/FUNCTIONAL INTERPRETATION

Definition, Application and Boundaries

- **The aforementioned Article 12** of the Provisions on the law in general, allows for **functional interpretation** with regard to the purpose that the legislator intended to pursue by enacting a specific regulatory provision.
- Nevertheless, the **teleological argument, based on the ‘*the intention of the legislator*’**, serves to clarify the meaning of the term used in the tax provision where, **in its branch of origin, it is subject to a variety of interpretations**; on the other hand, **it could serve** to assign a meaning to the term or concept that is **different** from that which it assumes in its branch of origin.

SUBJECTIVE OR OBJECTIVE TELEOLOGICAL ARGUMENT?

The so-called '*intention of the legislator*' or '*ratio legis*' should be identified by considering what the legislator intended to say, or by looking at the text of the law detached from the subject who produced it?

- **Subjective teleological argument (*minority thesis*)**

According to the 'subjective teleological interpretation', the meaning of the legislative act must be attributed to it by taking into account the 'will' of the legislator

- **Objective teleological argument (*majority thesis*)**

According to the 'objective teleological interpretation', on the other hand, the intention of the legislator is disregarded and regard is had to the will of the law, understood in an objective sense. In other words, the objective 'ratio' of the law consists in its objective purposes, on the assumption that the text has its own 'intrinsic purposes'.

ECONOMIC PERSPECTIVES

OR

SUBSTANCE OVER FORM

- **The teleological argument in anti-avoidance perspective:** according to this approach the interpretation of tax provisions should have been based on concepts developed by economics, so as to bring within the scope of the rule even transactions not expressly mentioned but manifesting an economic force equivalent to the transactions mentioned
- This **functional interpretation** aimed at combating evasive transactions began to develop around the now repealed Article 8, Royal Decree no. 3269/1923 on registration tax (the historical predecessor of the current Article 20, L. no. 131/1986)
- The rule offered insights into the matter by talking about the **effects of deeds and contracts** (indeed, **this theory considered also economic effects and not just legal effects**)

THE ITALIAN COURT OF CASSATION APPROACH ON ART. 20 D.P.R. N. 131/1986

In recent years, numerous judgments of the Court of Cassation have followed the theory of teleological interpretation in anti-avoidance perspective, based on the following arguments:

- the interpretation of the aforementioned Art. 20, which speaks of taxation with registration tax of the effects of deeds and contracts, with a view to substantial economic effects;
- the nature of registration tax as a tax on deeds and contracts does not preclude the overall assessment of external interpretative elements and contractual links;
- only the consideration of meta-textual elements and contractual links identifies and measures the actual wealth and ability to pay underlying the deed/contract submitted for registration, pursuant to Article 53 of the Constitution;
- the recovery of external elements linked to the deed/contract submitted for registration responds to the need to highlight, precisely in implementation of the rule of substance over form, the 'concrete' or 'real' cause of that deed./contract

SPECIFIC CASE LAW, BETWEEN HYPOTHESES OF LOWER OR HIGHER TAXATION

- the transfer to a company, **in exchange of its shares**, of an asset or of real estate, linked to the subsequent sale of the shares of the transferee company to third parties is considered a **sale of the asset or of the real estate** (C. C. no. 12909/2018);
- the case of a **contractual link between a mortgage loan** and the **transfer** to the company of the **property on which the mortgage is encumbered**, even without a subsequent transfer of the company's shares, is **reclassified as a sale** (C.C. no. 4589/2018; no. 7637/2018);
- the related sale of **separate assets** considered individually but **functionally capable of being used** and organized for a single production **purpose is a transfer of a business - firm** (C.C. no. 1955/2015; no. 17965/2013; no. 31069/2017);
- the transfer of the **total amount of the shares** of an operating company is equivalent to a **transfer of a business - firm** (C.C. no. 24594/2015);
- the transfer of **land with an old building** behind it, linked to the subsequent request by the purchaser for a building **permit for demolition and reconstruction**, is equivalente to **the sale of building land** (C.C. no. 24799/2014 and no. 313/2018)

THE PREVALENT SCHOLARS APPROACH

- Scholars do not agree with the approach based on the prevalence of economic substance over legal form, believing instead that it is not the task of the interpreter to fill gaps and redefine the scope of application of the rules arbitrarily, but rather that it is the task of the legislator to select, from among several economically relevant facts, those deemed taxable.
- However, obviously, one must look not only at the legal form but also at the legal substance; however, an arbitrary, hypothetical and meta-legal economic substance is a very different scenario.
- This approach has been confirmed in the new (reiterated) wording of Article 20 (L. no. 205/ 2017), which expressly states that registration tax must be applied according to the intrinsic nature and 'legal effects' of the deed to be registered

CONCLUSIONS

- In the Italian experience the **literal interpretation is dominant and takes precedence over any other interpretative criterion**, but also allows the use of **other criteria** when these can be inferred from the specific provision under analysis or from the relevant regulatory framework
- This brings the reasoning back to the **need to anchor the interpretative process to the text**, while the argument linked to the **'intention of legislator'** ('ratio' of the rule) is only suitable for overcoming the literal 'limiting' meaning where the underlying reason **is made explicit by the rule** itself.
- The formula **'substance over form'** must be understood in terms of the ***prevalence of legal substance over legal form***, as it is limited by the principle of legality (art. 23 Cost.); if legal significance were to be given to economic substance without an *ad hoc* rule legalising the fact/economic fact, the **arbitrariness of the interpreter** would be clear, as they would effectively be acting as a legislator.

LEGISLATION

Provisions on the law in general (March 16, 1942)

- ***Art. 12, Interpretation of the Law***
- *When applying the law, it cannot be given any meaning other than that made clear by the specific meaning of the words according to their connection and by the intention of the legislator.*
- *If a dispute cannot be resolved with a specific provision, consideration is given to provisions regulating similar cases or analogous matters; if the case remains uncertain, it is decided according to the general principles of the legal system of the State.*

Registration Tax, Law n. 131/1886

- ***Art. 20 Interpretation of deeds***
- *The tax is applied according to the intrinsic nature and legal effects of the deeds submitted for registration, even if the title or apparent form does not correspond to it, based on the elements deducible from the deed itself, regardless of extratextual elements and documents connected to it, except as provided in the subsequent articles.*

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