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Input VAT Deductibility on Pre-Leasing Payments in Lease-to-Build Contracts

Pre-leasing payments settled prior to physical delivery qualify for immediate input VAT deduction where instrumental to the enterprise's economic programme: Italian Supreme Court of Cassation, Civil Division, Order no. 28210/2026

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Current Legal Framework as of 13 November 2026: The Italian Supreme Court of Cassation consolidates the principle whereby, in real estate lease-to-build contracts, input VAT deductibility on pre-leasing payments operates under the criterion of prospective business purpose pursuant to Article 19 of Presidential Decree no. 633/1972, standing in sharp contrast to the accrual, matching, and depreciation rules governing corporate income taxation.

ABSTRACT

By Order no. 28210 of 1 November 2026, the Italian Supreme Court of Cassation, Civil Division, held that **input VAT deductibility in lease-to-build contracts** with respect to pre-leasing payments operates immediately upon their settlement prior to the physical delivery of the real estate, provided that such expenses are directly linked to the lessee enterprise's economic programme and instrumental to its taxable business activities. The Court reaffirmed the structural separation between the **European Union principle of VAT neutrality**—anchored in the functional and prospective business purpose of capital investment goods—and the **tax accrual and period-matching rules under the Consolidated Income Tax Act (TUIR)**, which instead defer the deduction of negative income components until the asset actually enters into operational service. This article examines the operational repercussions of the ruling for corporate financial and accounting management, the **ten-year input VAT adjustment mechanism** governing buildings, and the evidentiary burdens that taxpayers must discharge in tax litigation against assessments issued by the Revenue Agency.

Key Takeaways

- **Immediate deduction on pre-financing instalments:** Input VAT charged on pre-leasing payments settled prior to the completion and handover of the building is deductible in full where the asset forms part of the corporate investment plan.
- **Autonomy between VAT and direct income taxes:** The temporal deferral of cost deductions until operational deployment under Articles 102 and 109 of the Consolidated Income Tax Act (TUIR) does not extend to harmonised value added tax, which is governed by the principle of fiscal neutrality.
- **Assimilation to capital investment goods:** In accordance with European Union case law, entering into a finance lease aimed at ownership transfer produces immediate contractual effects and is assimilated to the acquisition of depreciable capital assets.
- **Management of the burden of proof:** To defeat tax authority challenges alleging lack of economic rationale, the taxpayer must substantiate qualitative and prospective business relatedness through corporate resolutions, sworn technical appraisals, and preliminary agreements.

CASE DOSSIER

JURISDICTION
Italy (Civil Law)

SUBJECT AREA
Tax Law & Corporate Taxation & VAT

LEADING DECISION
Italian Supreme Court of Cassation, Civil Division, Order of 1 November 2026, no. 28210 — Recognises the immediate deductibility

Legal Principle / Editorial Headnote

In Value Added Tax matters, in the context of a real estate lease-to-build contract, input VAT charged on pre-leasing payments settled by the lessee prior to the physical delivery of the property is deductible pursuant to Article 19(1) of Presidential Decree no. 633/1972, in the version applicable at the material time, whenever such payments constitute costs integrated into the entrepreneur's economic programme, being inherent in its productive activity insofar as they are instrumental thereto.

01. LEGAL FRAMEWORK OF LEASE-TO-BUILD CONTRACTS AND SCOPE OF VALUE ADDED TAX

1.1 — Structure of the Finance Lease Agreement and Function of Pre-Leasing Payments

The issue of **input VAT deductibility in lease-to-build contracts** represents a critical juncture for the financial and tax management of real estate and industrial enterprises. Under the typical contractual scheme of a **real estate finance lease** involving properties yet to be erected (*leasing in costruendo*), the lessor company purchases the buildable land and finances the construction contract to erect the building in accordance with the technical specifications provided by the lessee. During the interval between the execution of the lease agreement and the completion of construction works, the asset is not yet capable of physical use and enjoyment. Throughout this time frame, the financed enterprise pays so-called **pre-leasing payments** or pre-financing instalments, consisting essentially of interest accrued on the sums progressively disbursed by the leasing company to pay suppliers and building contractors.

From a corporate and business-economics standpoint, these disbursements do not constitute an isolated financial remuneration. Rather, they represent the expenditure incurred by the lessee in order to secure the future availability of an **instrumental real estate complex** dedicated to the pursuit of its business enterprise. The Italian Supreme Court of

Cassation has clarified that the transaction embodies a **unitary contractual cause**, aimed at enabling the enterprise both to utilise and ultimately to acquire ownership of the productive facility[1]. The pre-leasing phase is functionally connected to the subsequent phase of ordinary finance leasing, which commences only upon the physical handover of the completed building.

For statutory auditors and tax advisers alike, it is essential to observe that invoicing these interim instalments entails the regular charging of **value added tax** by the lessor company. Consequently, the lessee enterprise records a substantial volume of **input VAT credit** on payments settled prior to physical delivery. Where promptly deducted in periodic VAT settlements, that tax credit alleviates **corporate cash-flow needs** and curtails bank borrowing throughout the demanding construction-site phase.

1.2 — Autonomy of the VAT Regime Vis-à-Vis Direct Income Tax Deductibility

In the course of tax audits, the Italian tax administration has long maintained that direct income tax rules and VAT regulations are tightly intertwined. Within the sphere of **corporate business income** governed by the Consolidated Income Tax Act (TUIR), charges incurred prior to physical delivery cannot be deducted immediately on a cash basis or within the financial year of accrual. Pursuant to Articles 102 and 109 of the TUIR, pre-leasing costs qualify as **multi-year deferred charges** strictly attributable to an asset under construction.

For direct taxation purposes, the deductibility of these negative income items is therefore deferred over time. The accounting technique of **multi-year prepaid deferrals** requires the expenditure to be spread across the entire term of the finance lease starting from the financial year in which the asset achieves **operational deployment**. That strict mechanism serves the revenue interest of safeguarding the temporal matching principle between costs incurred and revenues actually generated through the operational use of the building.

Nevertheless, automatically extending this deferral rule to harmonised indirect taxation constitutes a serious conceptual and systematic flaw. The European Union VAT system rests upon the **fundamental principle of fiscal neutrality** for taxable persons. The right to **input VAT deduction** arises at the exact moment when the tax becomes chargeable pursuant to Article 19 of Presidential Decree no. 633 of 26 October 1972, irrespective of the distinct timing restrictions imposed by domestic accounting and **corporate income tax** legislation.

02. FACTUAL BACKGROUND OF THE DISPUTE AND GROUNDS FOR THE TAX AUTHORITY'S DISALLOWANCE

The dispute brought before the Supreme Court of Cassation originated from an extensive tax audit conducted against a limited liability company operating in the real estate development and enhancement sector. During the 2007 tax year, the corporate taxpayer had entered into a **finance lease agreement** concerning an industrial building yet to be constructed. Under that contractual relationship, the lessor company issued an invoice for a substantial **initial balloon instalment** encompassing pre-leasing payments as well as registration tax. The lessee company recorded the accounting invoice and claimed an input VAT deduction on the tax passed on by way of statutory recourse in the amount of EUR 128,447.01.

The Italian Revenue Agency served a notice of tax assessment disallowing the claimed VAT deduction in full and simultaneously clawing back the underlying expenses for **corporate income tax (IRES) and regional production tax (IRAP)** purposes. According to the reconstruction advanced by the tax auditors, the commercial transaction lacked the requirement of **concrete effectiveness of the supply**. The tax office argued that, because the company had not obtained physical possession of the property until late autumn of the following financial year, the payments could not be regarded

as inherent in its business enterprise. On the Revenue Agency's view, instalments paid prior to handover had to remain fiscally suspended and deferred until the completed structure entered into operational service.

The tax assessment further alleged a lack of economic rationale and tax avoidance traits. Specifically, the tax office contended that paying interim instalments was designed merely to channel financial funding to the construction contractor, stripping the transaction of any genuine causal justification. The Provincial Tax Commission partially upheld the taxpayer's challenge (annulling the assessment regarding the disputed VAT deduction of EUR 128,447.01 and recognising deductibility for the lesser amount of EUR 49,400.00 attributable to leasing instalments paid in 2007), whereas the Regional Tax Commission of Lombardy dismissed the Revenue Agency's appeal. The lower tax courts ascertained the genuine existence of the legal transaction and the full **economic business relatedness of the costs**, emphasising that entering into the finance lease was consistent with the company's corporate purpose and expansion plans. Both the valid execution of the contract and the verified progress of construction works ruled out any fictitiousness of the challenged supplies.

In its appeal before the Supreme Court of Cassation, the Revenue Agency reiterated that the impossibility of physically enjoying the asset precluded reliance on the ordinary VAT deduction regime. Under that restrictive revenue stance, acquiring assets not yet ready for physical use was equated with expenditure lacking an immediate nexus to core business operations. Such a narrow reading, however, disregards the systematic framework established by Supreme Court case law with respect to **buildings under construction**. Addressing the tax monitoring of real estate assets, the Supreme Court of Cassation had already clarified that the special regime for buildings and the corresponding ten-year input VAT adjustment period begin to run solely from the date of formal completion of the structure[2]. The legal system accords full recognition to expenditure incurred during the preparatory phase, safeguarding the exercise of the right of deduction prior to final technical inspection and sign-off.

03. INPUT VAT DEDUCTIBILITY IN LEASE-TO-BUILD CONTRACTS UNDER SUPREME COURT CASE LAW

3.1 — Prospective Business Purpose and Assimilation to the Acquisition of Capital Investment Goods

The ruling handed down by the Italian Supreme Court of Cassation dismantles the formalistic approach of the tax administration at its root by foregrounding the concept of **prospective business relatedness**. For the purpose of deducting upstream input VAT, it is immaterial that the expenses were incurred prior to securing physical availability of the real estate complex. What is decisive is that the costs fit coherently within the **entrepreneur's economic programme** and prove instrumental to its productive activity.

In accordance with the case law of the Court of Justice of the European Union, entering into a **finance lease aimed at ownership transfer** is equivalent to acquiring a **capital investment asset**. Even prior to exercising the final purchase option, the lessee assumes the bulk of the economic risks and benefits associated with the asset. Interim pre-leasing instalments finance the creation of a depreciable capital good intended for the enterprise.

Furthermore, the tax legal order provides a dedicated safeguard against any subsequent diversion of the asset towards VAT-exempt transactions or uses extraneous to core business operations. Specifically, the statutory regime governing **input VAT deduction adjustments** for buildings establishes a strict monitoring period of ten years[3]. That ten-year observation window fully protects the revenue interests of the Treasury, rendering any attempt to deny immediate input VAT deduction during the pre-leasing phase wholly unjustified.

> In lease-to-build contracts, the right to deduct input VAT arises upon contractual commitment: making the tax credit conditional upon physical handover of the asset breaches fiscal neutrality and paralyses corporate liquidity.

3.2 — Legal Relevance of Contractual Effects Prior to Physical Delivery

A central pillar of the Court's reasoning lies in the private-law characterisation of the transaction. A lease-to-build agreement constitutes a **consensual contract** involving reciprocal obligations, whose legal effectiveness is perfected upon the valid manifestation of mutual consent by the contracting parties. It is not a real contract whose validity depends upon physical delivery of the *res*. Accordingly, the **production of binding contractual effects** is immediate from the moment the agreement is signed.

Throughout the execution of the construction works, the lessor company disburses the agreed progress payments to the building contractor, while the lessee undertakes the obligation to pay periodic pre-financing consideration. Those outlays are neither gratuitous transfers nor non-repayable capital contributions: they represent the performance of specific **contractual obligations** inherent in the industrial investment. Indeed, the assumption of typical construction and contractor risks rests primarily upon the lessee, confirming the genuinely commercial character of the preparatory stage.

Recognising the full legal force of commitments undertaken prior to handover entails a straightforward tax consequence. **Pre-leasing payments** must be accorded the exact same VAT treatment applicable to ordinary lease instalments paid after final inspection and sign-off of the building. Provided that the building under construction is earmarked for carrying out transactions conferring a right of deduction, the input VAT paid by way of statutory recourse is immediately and integrally deductible under the **principle of VAT neutrality**.

3.3 — What Are the Conditions for Input VAT Deductibility in Lease-to-Build Contracts?

To exercise **input VAT deductibility in lease-to-build contracts** on pre-leasing payments, the lessee enterprise must demonstrate the effective relatedness of the transaction to its economic programme and the allocation of the property to taxable output transactions, whereas the absence of physical delivery of the asset during ongoing construction-site works remains legally irrelevant.

At an operational level, the business operator cannot merely produce the invoice issued by the finance leasing company. For the purposes of Article 19 of Presidential Decree no. 633/1972, formally holding the status of a commercial entrepreneur does not suffice on its own to substantiate the right of deduction. Rather, it is indispensable to document the **objective business allocation** of the structure through preliminary commercial lease agreements, sworn construction-site appraisals, forward-looking business plans, and formal resolutions adopted by corporate governing bodies.

Conversely, where the property is intended from the outset for carrying out VAT-exempt activities pursuant to Article 10 of the Italian VAT Decree, deducting input VAT on pre-leasing instalments is barred at the root under either the **general *pro rata* deduction rule** or specific non-deductibility provisions. By contrast, whenever the building is allocated to the manufacture of taxable goods or to commercial leasing subject to an express option for VAT taxation, the right to **immediate input VAT deduction** applies in full, preventing any undue financial burden upon the enterprise.

04. CASE LAW STRATIFICATION BETWEEN INPUT VAT ADJUSTMENT AND TRANSFER

TAXES

4.1 — Commencement of the Ten-Year Adjustment Period for Unfinished Buildings

The rules governing input VAT deduction cannot be examined in isolation, but must be coordinated with the provisions on the **ten-year monitoring period for buildings** set forth in Article 19-bis.2 of Presidential Decree no. 633/1972. With respect to instrumental real estate assets, statutory law mandates that a change in intended use or the performance of VAT-exempt output transactions triggers an input VAT adjustment proportional to as many tenths as the years remaining in the ten-year window. For complex construction sites and properties under development, practical uncertainty arose regarding the exact starting date of that observation period.

Supreme Court case law has established a foundational rule of operational clarity: the **ten-year VAT adjustment period** begins to run solely from the date of actual physical completion of the building. Prior to the completion of essential structural works, the property is incapable of effective operational deployment, meaning that any early sale or assignment cannot trigger the clawback reductions associated with assets that have already entered into service. This preserves in full the enterprise's input tax credit accrued on **construction-site expenses** and advance instalments paid.

From a private-law perspective, this analysis dovetails with the rules governing early dissolution of the lease relationship. Addressing cases of mutual termination of a lease-to-build contract prior to handover, the Supreme Court of Cassation reaffirmed that the lessor company legitimately retains the sums collected as pre-leasing payments[4]. The binding force of legal effects already produced confirms that such payments constitute genuine consideration for a financial transaction actually performed, barring arbitrary accounting reversals through credit notes under Article 26 of Presidential Decree no. 633/1972 and confirming the stability of the taxable transaction.

TAX AREA	RESTRICTIVE REVENUE AGENCY POSITION	SUPREME COURT RULING
Pre-leasing payments	REJECTED Non-deductibility of input VAT prior to delivery due to lack of immediate physical enjoyment	UPHELD Immediate deduction under Art. 19 of Presidential Decree no. 633/1972 based on relatedness to the economic programme
Input VAT adjustment	REJECTED Statutory forfeiture of the right or monitoring tied to the mere incomplete acquisition	UPHELD Ten-year period running from the date of actual completion of the building
Mortgage and cadastral taxes	DOCTRINE Exclusion of instrumental status for properties not yet completed	UPHELD Programmatic instrumentality and proportional taxation right from the leasing purchase

4.2 — Interplay Between VAT-Exempt Resale of Redeemed Property and Proportional Indirect Taxation

A further facet of this intricate tax framework concerns the treatment of **mortgage and cadastral transfer taxes** on acquisitions of unfinished buildings. Whenever a finance leasing company purchases a building under construction in order to grant it simultaneously under lease to the user, the transaction is subject to proportional rather than fixed-rate mortgage and cadastral taxes. The Italian Supreme Court of Cassation has held that the instrumental character of the real estate complex must also be assessed in light of its **programmatic function**, inasmuch as the building constitutes the designated means for carrying on the business enterprise[5].

Such convergence between indirect transfer taxes and VAT law underscores the unity of the underlying financial cause. If the tax legislature treats a building under construction as an instrumental business asset from the very execution of the notarial deed of purchase, there is no logical basis for denying **input VAT deduction on preparatory instalments** paid by the lessee. Indeed, the business operator shoulders the economic burden of the investment and bears the financial risk of construction.

Even so, utmost care is required when managing the subsequent purchase-option exercise and any onward disposal. Should the property be redeemed early and subsequently resold under a VAT-exempt regime prior to the expiry of the ten-year tax monitoring window, the enterprise will be required to repay the remaining tenths of the input tax originally deducted. Maintaining an accurate **depreciable assets register** and tracking annual adjustment quotas over time represent the sole effective safeguard against severe penalties during automated or formal tax inspections.

05. LITIGATION DEFENCE, BURDEN OF PROOF, AND ACCOUNTING MANAGEMENT OF THE TRANSACTION

5.1 — Burden of Proof in Litigation and Evidentiary Presumptions of Economic Relatedness

In tax disputes concerning **input VAT deductibility in lease-to-build contracts**, proper allocation of the burden of proof forms the linchpin of litigation strategy. As a general rule, the assessing tax office bears the burden of establishing serious, precise, and concordant circumstantial evidence capable of calling into question the economic reality of the transactions or demonstrating manifest lack of economic rationale in the invoiced instalments. Conversely, where the tax administration alleges lack of business instrumentality or an abusive avoidance purpose, it falls upon taxpayer's counsel to prove the lawful substantive basis of the claimed deduction.

In court proceedings, the taxpayer must substantiate the qualitative relatedness of the expenditure to its corporate business model. The Supreme Court of Cassation reiterated that merely holding the formal status of an entrepreneur is insufficient to justify VAT deduction; rather, one must verify the concrete instrumentality of the acquisition vis-à-vis business operations actually carried on or even merely planned[1]. Tax litigation counsel must therefore file a comprehensive evidentiary bundle comprising the original finance lease agreement, construction work-progress certificates endorsed by the site director, board of directors' resolutions, and traceable bank wire transfers.

This evidentiary framework mirrors the settled principles established by Supreme Court case law on the allocation of the burden of proof in cases involving alleged commercial fictitiousness, as likewise examined in *Metodo Giuridico* scholarship on subjectively non-existent transactions and cost deductibility[D1]. Whenever contractual and accounting records corroborate both physical construction progress and the genuine productive allocation of the building, mere rebuttable presumptions raised by the tax office are entirely overcome.

5.2 — Accounting Distinctions and Practical Safeguards for the Lessee Enterprise

In practical application, a rigorous **distinguishing** analysis is required vis-à-vis related corporate real estate transactions. The rule permitting immediate input VAT deduction on pre-leasing payments does not apply where the building under construction is earmarked from the outset for immediate resale as trading stock without an option for VAT taxation, or for conducting wholly VAT-exempt activities. Under those distinct factual scenarios, upstream VAT non-deductibility applies irrespective of the contractual form chosen, requiring calculation of the general *pro rata* deduction percentage.

Unlike value added tax, under **corporate income taxation** pre-leasing payments are not deductible in the financial year of payment. Proper accounting recognition requires booking the portion of interest and charges accrued prior to physical delivery under **prepaid expenses and deferred charges**. Their tax deduction will then run in equal instalments solely from the moment the depreciable asset enters into operational service.

Ultimately, to forestall Revenue Agency challenges as well as audit qualifications by the statutory board of auditors, enterprises entering into lease-to-build contracts should establish a robust **internal compliance procedure**. Retaining technical construction-site documentation, reconciling bank disbursements against invoices issued by the leasing company, and documenting the intended economic deployment of the investment constitute essential safeguards to secure the input VAT credit and avert costly multi-year tax adjustments.

References & Authorities Cited

Statutory Provisions

- Presidential Decree no. 633 of 26 October 1972, Article 19 — Input VAT deduction on goods and services acquired in the exercise of a business enterprise, trade, or profession.
- Presidential Decree no. 633 of 26 October 1972, Article 19-bis.2 — Statutory rules governing input VAT deduction adjustments for depreciable capital goods and buildings.
- Presidential Decree no. 917 of 22 December 1986 (TUIR), Articles 102 and 109 — General rules on tax period allocation of corporate expenses and depreciation of instrumental business assets.
- Law no. 124 of 4 August 2017, Article 1, paragraphs 136–140 — Comprehensive civil-law framework governing finance leases and real estate leasing contracts.

Case Law Cited

1. **Italian Supreme Court of Cassation, Civil Division, Order of 1 November 2026, no. 28210** — Recognises the immediate deductibility of input VAT charged on pre-leasing payments in lease-to-build contracts by virtue of their relatedness to the enterprise's economic programme. Outcome: appeal dismissed. Para.: 3.5–3.9.

2. **Italian Supreme Court of Cassation, Civil Division, Order of 28 May 2026, no. 16718** — Establishes that the ten-year period for input VAT deduction adjustment runs from the date of actual completion of the building rather than from the purchase or assignment of the unfinished asset. Outcome: appeal dismissed. Para.: 2.5–2.7.

3. **Italian Supreme Court of Cassation, Civil Division, Order of 18 December 2024, no. 33247** — Mandates a *pro rata temporis* adjustment of input VAT deducted on lease instalments and on the final purchase option in the event of a subsequent VAT-exempt resale within the ten-year tax monitoring period. Outcome: appeal upheld in part as set out in the reasoning, judgment quashed and remanded to the Tax Court of Second Instance (*Corte di Giustizia Tributaria*) of Liguria. Para.: 2.3–2.5.

4. **Italian Supreme Court of Cassation, Civil Division, Judgment of 13 October 2022, no. 30145** — Confirms the unitary consensual nature of lease-to-build contracts and the full binding force of contractual obligations concerning pre-leasing interest prior to physical delivery. Outcome: both appeals dismissed. Para.: 1.3–1.4 and 3.1.

5. **Italian Supreme Court of Cassation, Civil Division, Order of 12 July 2022, no. 22042** — Confirms that buildings under construction granted under finance leases are subject to proportional mortgage and cadastral taxes insofar as they qualify as instrumental assets within the productive circuit. Outcome: appeal upheld, judgment quashed and, deciding on the merits, original taxpayer petition dismissed. Para.: 1.13–1.16.

Legal Scholarship Cited

D1. Metodo Giuridico, *Operazioni soggettivamente inesistenti: IVA e deducibilità dei costi* [Subjectively Non-Existent Transactions: VAT and Cost Deductibility]. Analysis of the evidentiary standards governing business relatedness and the economic reality of corporate expenses.

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