

TP and promotional incentives: key principles from the Italian Court of Cassation

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Federico Vincenti and Carola Valente Della Rovere of Valente Associati GEB Partners/Crowe Valente analyse Ordinance No. 18145/2026, focusing on transfer pricing method selection and the distinction between taxable prize promotions and contractual arrangements involving reciprocal obligations

In [Ordinance No. 18145/2026](#), published on June 5 2026, the Italian Court of Cassation addressed two important issues in domestic tax law: the selection of transfer pricing methods for transactions between associated enterprises and the distinction between taxable prize promotions and contractual arrangements involving reciprocal obligations.

Selection of transfer pricing methods

A central issue in transfer pricing disputes is the selection of the method used to determine the arm's-length value of an intra-group transaction.

In the case under consideration, the tax authorities challenged the transfer pricing treatment of transactions involving a foreign subsidiary. The lower courts accepted the cost-plus method, taking into account the specific characteristics of the subsidiary's operations, including

the significant personnel costs borne directly by the subsidiary, unlike in other markets where such costs were borne by the parent company.

The Court of Cassation rejected the tax authorities' arguments against the use of that method and upheld the lower court's reasoning.

The decision confirms that the use of a transfer pricing method other than comparable uncontrolled price (CUP) does not, in itself, constitute a violation of Article 110(7) of the Italian Income Tax Code. Although CUP may be particularly reliable where sufficiently comparable uncontrolled transactions are available, its suitability does not automatically exclude other methods.

The court referred to the evolution of the OECD Transfer Pricing Guidelines, noting that the 2010 edition removed the formal hierarchy between methods found in the original 1995 guidelines. The decision also acknowledged the relevance of the Italian regulatory framework, including the Ministerial Decree of May 14 2018, which provides for a preference for traditional transaction methods, particularly CUP, where practicable.

Accordingly, the absence of a rigid hierarchy does not mean that taxpayers can select a method without justification. The choice must be supported by an analysis demonstrating why the selected method is appropriate to the transaction under review.

Comparability, functions, and economic circumstances

The court's reasoning highlights the importance of examining the actual economic circumstances of associated enterprises rather than applying transfer pricing methods mechanically.

The cost-plus method requires a reliable assessment of the relevant cost base and an appropriate gross profit margin. Its application must also take account of differences between the tested transaction and comparable transactions, including the functions performed, risks assumed, and relevant economic circumstances.

In the case under consideration, the personnel expenses borne by the foreign subsidiary were particularly relevant. The allocation of these costs differed from the arrangements in other markets, where the parent company directly incurred the corresponding expenses. This difference supported the conclusion that the transfer pricing analysis needed to reflect the subsidiary's operating structure.

For multinational groups, the implication is that transfer pricing documentation should explain not only which method has been selected but also why it provides a reliable measure of the arm's-length outcome.

A robust analysis should identify the functions performed by each group entity, the risks assumed, the assets employed, the relevant cost base, and the rationale for the profit margin applied. Where differences between the tested transaction and comparable businesses may affect the outcome, appropriate adjustments should be considered and documented.

Burden of proof in transfer pricing disputes

The court also rejected the tax authorities' argument that the taxpayer had failed to discharge its burden of proof in relation to the arm's-length value of the intra-group transactions.

The issue was not simply whether the taxpayer had used the same method as the tax authorities but whether the evidence supported the conclusion that the transactions were consistent with the arm's-length principle.

The lower courts had accepted the taxpayer's analysis based on the cost-plus method as an appropriate means of establishing respect of the arm's-length principle. The Court of Cassation found no legal error in that conclusion.

The ruling does not establish that taxpayers may freely choose any transfer pricing method or dispense with a proper comparability analysis. Rather, it confirms that the validity of the methodology and the supporting evidence must be assessed on their merits.

From a practical perspective, taxpayers should maintain contemporaneous documentation explaining the choice of method, the reasons for preferring it to alternatives, the determination of the cost base and mark-up, and any adjustments required to account for differences in functions, risks, and market conditions.

Commercial incentives: when does a benefit constitute a taxable prize?

The second issue concerned the tax treatment of a tourist trip offered to customers who undertook to place orders for specified purchase volumes within a given period.

The tax authorities treated the arrangement as a prize promotion subject to withholding tax. The lower appellate court agreed, considering the link between the achievement of the required turnover and the provision of the trip sufficient to classify the benefit as a prize.

The Court of Cassation reached the opposite conclusion.

It emphasised that the trip was incorporated into individual contractual arrangements involving reciprocal obligations. Customers undertook to purchase the relevant goods or to reimburse a lump sum of €2,000 towards the cost of the trip if they did not proceed with the required orders.

In the court’s view, this arrangement could not be classified as a prize promotion merely because the customer received a benefit linked to purchasing activity. The trip formed part of a bilateral contractual relationship in which the parties assumed reciprocal obligations, rather than constituting a promise made to an indeterminate group of people.

The court therefore distinguished a promotional offer falling within the relevant prize-promotion regime from a benefit agreed as part of an individual commercial contract. In support of this distinction, it referred to its judgment No. 30840/2017, concerning promotional activities structured through contractual clauses rather than public promises.

The second ground of the main appeal was consequently upheld, and the contested judgment was set aside on this issue, with the case remitted to the Lombardy Regional Tax Court of Appeal for reconsideration by a different panel.

The ruling does not mean that all customer incentives linked to purchases fall outside the prize-promotion rules. Their classification depends on the substance and structure of the arrangement, including whether the benefit forms part of a bilateral contract involving reciprocal performances or constitutes a promotional promise governed by the applicable legislation.

Businesses should therefore assess the contractual terms and economic substance of their incentive schemes before determining their tax treatment.

Practical implications

Ordinance No. 18145/2026 offers useful guidance on two broader principles of Italian tax law.

First, transfer pricing requires a case-specific and evidence-based assessment of the appropriate methodology. CUP may be particularly relevant where reliable comparable uncontrolled transactions are available, but alternative methods, including cost plus, remain available where justified by the circumstances and consistent with the applicable legal framework.

Second, the tax treatment of commercial incentives depends on the legal and economic substance of the underlying arrangement. A benefit granted in connection with a purchase should not automatically be classified as a taxable prize where it forms part of a bilateral contractual relationship involving reciprocal obligations.

For multinational groups and businesses operating in Italy, the decision reinforces the importance of clear contractual arrangements, reliable economic analysis, and appropriate documentation. In both transfer pricing and commercial incentive schemes, the relevant tax consequences must be determined by examining the substance of the transactions rather than relying solely on their formal description.



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