15 July 2021

Italian Tax Authorities (ruling no. 458 of July 7, 2021) address the matter concerning the tax treatment of workers that are temporarily in Italy during the Covid-19 pandemic

To counter Covid-19 pandemic, governments have imposed unprecedented measures. Given the domestic and tax treaty regulation, those measures may have an impact, *inter alia*, on (i) the tax residence of individuals and (ii) the tax treatment applicable to income from employment. The same holds true with respect to the application of the provisions laid down in the treaty concluded between the "current home jurisdiction" and the "previous home jurisdiction" (as well as the application of the provisions of their respective treaty network).

OECD Secretariat issued guidance regarding the interpretation of the provisions of the tax treaties during the Covid-19 pandemic[1]. The guidance in question deals *inter alia* with the concerns related to (i) change to the residence status of individuals and (ii) income from employment.

The guidance issued by the OECD Secretariat aims at helping the countries in interpreting the treaty provisions to avoid double taxation without creating double non-taxation.

The guidance is not binding for the countries as it merely reflects the general approach of jurisdictions experienced so far and describes how certain countries have dealt with the issues arisen from Covid-19 pandemic.

On July 7, 2021, the Italian Tax Authorities issued a statement of practice (Ruling No. 458/2021, the "**Ruling**") that deals with the tax treatment of workers that temporarily returned to Italy during the Covid-19 pandemic and could not leave Italy due to travel restrictions imposed by the People' Republic of China.

The Ruling is particularly interesting because it provides the Italian Tax Authorities view on the role of the guidance issued by the OECD Secretariat in the interpretation of the Italian law and the provisions of the Italian treaty provisions.

In detail, the case dealt with by the Italian Tax Authorities concerns certain employees of an Italian

[1] Reference is made to *OECD Secretariat Analysis of Tax Treaties and the Impact of the COVID-19 Crisis*, 3 April 2020; and *Updated guidance on tax treaties and the impact of the COVID-19 pandemic*, 21 January 2021.

Multinational company that prior to the Covid-19 pandemic outbreak were seconded to certain group subsidiaries located in China. The seconded employees were registered to the Register of Italians Living Abroad (so-called, A.I.R.E.). The employees became Chinese-tax residents in 2019.

Due to the Covid-19 pandemic, the seconded employees moved back to Italy in January 2020 and but kept performing their employment duties from Italy for the benefit of the Chinese subsidiaries in accordance with the secondment agreement. No interruptions nor contractual amendments occurred in relation to the seconded employees, and their cost continued to be borne by the Chinese subsidiaries during their stay in Italy.

The seconded employees returned to the People' Republic of China in 2020. Some of them got back to People' Republic of China on July 2, 2020 (spending in Italy less than 184 days in the relevant calendar year), while others got back to People' Republic of China respectively on July 29, 2020, in August and in September (spending in Italy more than 184 days in the relevant calendar year).

The Italian Multinational company (employer of the seconded employees) filed a tax ruling request seeking guidance on the following aspects:

1. whether the employment income received by the employees that spent less than 184 days in Italy in the relevant calendar year should be considered Italian-sourced income derived by non-Italian resident individuals to be subject to Italian taxation (triggering Italian withholding tax obligations for the Italian Multinational company);
2. whether the presence in Italy for more than 184 days may result in the employees acquiring the status in Italian tax resident in the relevant calendar year;
3. if question No. 2 above is answered in the affirmative, the Italian Multinational company asks the Italian Tax Authorities:
   (a) to clarify whether the taxable income would be determined on the basis of the provisions contained in Art. 51(8-bis) Italian income tax code ("ITC")[2];
   (b) to determine whether the 184-days threshold, provided for by Art. 51(8-bis) IITC, is met.

The Ruling clarifies that according to the OECD Secretariat it is for each jurisdiction to establish its own rules to deal with Covid-19 pandemic and to provide tax certainty to taxpayers; on the other

[2] Pursuant to Art 51(8-bis) of Presidential Decree no. 917 of 22 December 1986 (Italian Income Tax Code, or IITC), employment income deriving from activities carried out by employees outside Italy in a continuative and exclusive way, staying out of Italy for more than 183 days (*i.e.*, 184 days in case of leap year), equals to a forfeited amount determined by the Italian Ministry of Labor, regardless of the salary actually paid by the employer.

hand, Italian Tax Authorities made clear that the OECD guidance only applies to the interpretation of double tax treaties and it does not affect the interpretation of the Italian domestic tax laws.

The Ruling acknowledges that Italy (as suggested by OECD Secretariat) concluded specific administrative agreements with Austria, France and Switzerland; however, the contents of such administrative agreements can be applied only in connection with matters that regard the relevant contracting States and they cannot be extended or otherwise be intended to cover other cases that involve third countries irrespective of the fact that those countries have concluded a tax treaty with Italy.

In the light of that, the Italian Tax Authorities concluded that employment income deriving from the activities carried out by the seconded employees in Italy during the Covid-19 pandemic was to be subject to tax according to the "ordinary" rules provided for by (i) the Italian tax laws and (ii) the tax treaty between Italy and the People' Republic of China. From a practical standpoint, the above implies that in the view of the Italian Tax Authorities, they are not bound to disregard the days of physical presence of the seconded employees within its territory during the Covid-19 pandemic (regardless of the fact that these individuals got stranded in Italy due to the travel restrictions in force in the exceptional period).

As a result, with reference to the first question, the Italian Tax Authorities held that Italy had the right to tax the Italian-sourced employment income derived by the non-resident employees (those that spent less than 184 days in Italy), without its taxing rights being restricted by the tax treaty with People' Republic of China.

Indeed, income from employment carried out in Italy by a non-Italian tax resident individual is considered Italian-sourced income according to the relevant provision of Italian domestic tax law[3]; therefore, Italy intends to exercise its taxing rights on such income. Moreover, Italy-People' Republic of China treaty does not prevent Italy from taxing that item of income. Art. 15 of the treaty does not restrict the source State from taxing the employment income derived by an employee resident of the other Contracting State in respect of an employment exercised within its territory if: (a) the recipient is present in the source State for a period or periods exceeding in the aggregate 183 days in the calendar year concerned; or (b) the remuneration is paid by, or on behalf of, an employer who is a resident of the source State; or (c) the remuneration is borne by a permanent establishment or a fixed base which the employer has in the source State. In the case at stake, the Italian Tax Authorities

[3] Pursuant to Art. 23(1)(c) of the IITC.

held that the remuneration had been paid by an employer that was resident in the source State (*i.e.,* the Italian Multinational company - Italy); accordingly, Italy was not restricted from taxing the employment income sourced in its territory and derived by a non-Italian resident employee. People' Republic of China was also entitled to tax the income concerned but had to provide tax relief to the taxpayer in accordance with the Art. 23(3) of the treaty.

With reference to the second query reported in the ruling request, the Italian Tax Authorities clarified that the seconded employees that spent more than 184 days in Italy might be considered tax resident of Italy pursuant to Art. 2 of the IITC. According to Art. 2 of the IITC, individuals are deemed to be Italian tax resident if for the greater part of the calendar year (i) they are registered in the Italian Register of Resident Population, or (ii) they have their habitual abode in Italy, or (iii) they have their domicile in Italy. Hence, the employees might be considered resident taxpayers because of their domicile in Italy for the greater part of the calendar year. Dual resident conflicts arising from the Italian tax Authorities' position are to be addressed by means of the tie-breaker rules provided for by the applicable treaty.

Furthermore, as far as the third and fourth query reported in the ruling request are concerned, Italian Tax Authorities held that should the seconded employees be considered Italian-tax residents, the conditions set forth by Art. 51(8-bis) IITC would not be met and, consequently, the employment income could not be determined on a conventional basis: in order for Art. 51(8-bis) IITC to apply, the taxpayer must have spent more than 183 days abroad in the relevant 12-month period. In this respect, Ruling confirmed the view they expressed in Ruling No. 345 of May 17, 2021: Art. 51(8-bis) of the IITC requires the physical presence of the individual outside the Italian territory for a specific period of time (183-day period). As a result, days of physical presence in Italy fall outside the 183-day period regardless of the fact that that person kept performing his/her ordinary employment duties from home due to the travel restrictions imposed by the government to curb the Covid-19 pandemic outbreak.

This document is delivered for information purposes only.
It does not constitute a basis or guidance for any agreement and/or commitment of any kind.
For any further clarification or research please contact:

Fabio Chiarenza
Partner

Co-head of the Tax department
Rome
+39 06 478751
fchiarenza@gop.it

Stefano Grilli
Partner

Co-head of the Tax department
Milan
+39 02 763741
sgrilli@gop.it

Marco Busia
Associate

Tax department
Milan
+39 02 763741
mbusia@gop.it