The Italian Revenue Agency considers the impact of restrictions on movements of individuals caused by the COVID-19 pandemic on the application of Article 15 of the income tax treaty between Italy and China

With Ruling Reply no. 458 of 7 July 2021, the Italian Revenue Agency analysed, amongst other matters, the impact of restrictions of movements due to the COVID-19 pandemic on the application of Article 15 of the income tax treaty between Italy and China (the "**Treaty**"). The applicant was an Italian resident company belonging to a multinational group (the "**Applicant**") that represented that some of its employees that were seconded to its associated Chinese resident company (the "**Host Company**") returned to Italy in late January 2020 and remained in the country until July, August or September 2020, because of the restrictions on movements of individuals introduced by both Italy and China to react to the COVID-19 pandemic. While in Italy, those employees carried out their employment duties remotely for the benefit of the Host Company, in compliance with their secondment agreements. Due to these movement restrictions, some of the employees spent more than 184 days in Italy during 2020.

With respect to the represented scenario, the Applicant raised a number of questions concerning the taxation of the employment income earned by the employees.

First, the Revenue Agency clarifies that the guidance provided by the OECD Secretariat on the impact of COVID-19 on tax treaties (the "OECD Secretariat Analysis of Tax Treaties and the Impact of the COVID-19 Crisis" of April 2020 and the "Updated guidance on tax treaties and the impact of the COVID-19 pandemic" of January 2021) is only relevant for the purposes of the interpretation of tax treaties and not for interpreting Italian domestic legislation governing tax residence. Moreover, the Revenue Agency points out that – following the guidance of the OECD Secretariat – Italy signed specific agreements with neighbouring countries (*i.e.*, Austria, France and Switzerland) establishing, *inter alia*, that working days performed in their home country during the COVID-19 pandemic due to mobility restrictions shall be considered as performed in the State where workers should have carried out their employment activity in the absence of such measures. According to the Italian Revenue Agency, in absence of an agreement, such principle cannot be applied extensively with reference to other countries, such as China. The same Agency also points out that the position expressed in the Ruling Reply is in line with the reply of the Italian Government to Parliamentary question no. 5-04654 of 3 December 2020.

In the light of the above, the Revenue Agency, in relation to employees that did not qualify as resident of Italy for income tax purposes during 2020, takes the view that employment income attributable to the days in which the employment was exercised in Italy should be subject to income tax in Italy since:

- *(i)* under Italian domestic law and under Article 15(1) of the Treaty, employment income deriving from employment duties carried out in Italy should be regarded as Italian source income;
- *(ii)* the exception of Article 15(2) of the Treaty, which provides for exclusive taxation in the State of residence of the individual, does not apply. In this respect, the Revenue Agency points out that Article 15(2) attributes taxing powers exclusively to the Residence State (in this case, China) if, *inter alia*, the remuneration is not paid by a person resident of the Source State (in this case, Italy). According to the Revenue Agency, such condition in the case at hand is not met since the remuneration of the employees was paid by an Italian resident person (*i.e.*, the Applicant), therefore disregarding the circumstance that the employees had been seconded to the Host Company that was burdened from an economic viewpoint with the cost of such employees.

Second, the Applicant asked whether the employees who spent more than 184 days in Italy during 2020 should be regarded as resident of Italy for income tax purposes. In this respect, the Revenue Agency reiterates that issues on tax residence are not apt to be the object of ruling procedures since tax residence is strongly influenced by factual circumstances while ruling procedures are aimed to analyse interpretation of law. That being said, the Revenue Agency provides some general guidance on the determination of residence of individuals for domestic and treaty purposes in the specific circumstance. For domestic purposes, the Revenue Agency points out that – in the absence of specific provisions dealing with restriction on movement caused by the COVID-19 pandemic – residence of individuals shall be assessed pursuant to the ordinary application of domestic income tax rules. For treaty purposes, if the employees were to be regarded as resident of both China and Italy during 2020, their residence should be determined based on the tie-breaker rules laid down in Article 4 of the Treaty. In this respect, the Revenue Agency states that, as commented in paragraph 44 of the OECD Secretariat's analysis, in these cases, if the dual resident individual has a permanent home in both contracting States, her/his residence should be determined in the light of her/his habitual abode which, in turn, should be determined following the guidance provided for by paragraph 19 of the OECD Commentary on Article 4. Although the Revenue Agency mentions the analysis of the OECD Secretariat, it does not clearly state whether such analysis should influence the interpretation of the Treaty. In fact, paragraph 44 of the OECD "Updated guidance on tax treaties and the impact of the COVID-19 pandemic" provides, *inter alia*, that "[d]ays spent in a person's previous home jurisdiction because of travel restrictions imposed as a public health measure by one of the governments of the countries involved should not result in a change to the person's habitual abode".

Even if the Ruling Reply at hand addressed questions concerning the interpretation of Article 15 and Article 4 of the Treaty, it seems reasonable to conclude that the principles expressed by the Revenue Agency should be relevant also for the purposes of interpreting the Articles 4 and 15 of other treaties signed by Italy that, like the Treaty, are in line with the OECD Model.

Finally, the Applicant asked whether the taxable remuneration of the employees that qualified as resident in Italy during 2020 could be determined pursuant to the provision of Art. 51(8-*bis*) of the Italian Income Tax Code, which provides that income from employment carried out exclusively outside of Italy by resident individuals staying in the foreign country for more than 183 days in a 12-month period is not determined applying ordinary rules but on the basis of an annual Government Decree (such an amount is normally lower compared to the remuneration actually received by the individual). The Revenue Agency denied the application of such provision because, during 2020, the employees in the specific case did not physically stay in the foreign country for more than 183 days, to be computed in a 12-month period, but were physically present in Italy, where they performed their employment duties. In this respect, the Revenue Agency reiterates that the analysis of the OECD Secretariat does not have an impact on the interpretation of Italian domestic law provisions as it is only relevant for the purposes of interpreting tax treaties. In this respect, it shall be acknowledged that a similar approach on the application of Art. 51(8-*bis*) was taken by the Revenue Agency with Ruling Reply no. 345 of 17 May 2021.

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