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FAMILIES, CHARITIES AND HNWIS

Tax residence of individuals: the “Risk rules” and other amenities

Italian tax rules defining the residence of individuals for tax purposes have changed effective from January 1, 2024. Through circular letter 20/E of November 4 (“the Circular”), the Revenue Agency has released its guidelines for the interpretation and application of the new rules.

The New Criteria

A person is resident of Italy if, for most part of the year he/she:

- has in Italy the residence as defined by Italian Civil Code, i.e., the habitual abode;
- has in Italy the domicile. The new rules define expressly such term, as the place where the personal and family relationships are mainly developed. There is no longer reference to the Italian Civil Code definition of domicile, which has led to huge interpretative issues especially as to the prevalence of personal/family relationships over economic/business ones;
- is physically present in Italy, even for a fraction of day;
- is registered in the list of resident population.

The “Risk rules”

The Circular makes the example of a person *(i)* who owns an abode both Italy and in another State, *(ii)* who has children from a previous marriage living in the Italian abode and the spouse living in the foreign State *(iii)* who ordinarily works in Italy, *(iv)* travels a lot in different States for professional purposes and *(v)* spends the weekends and holidays in the State where the spouse lives. The Circular acknowledges that in this case it might be difficult to determine where personal and family relationships are mainly developed and states that a useful criterion can be identified in the physical presence.

The example goes further: the person has spent 145 days in Italy, 120 days in the foreign State where the spouse lives and 100 days in other States.

The conclusion is that the person should be considered resident of Italy.

This is a confirmation of what is normally recommended: days spent in the State of formal tax residence should outweigh the number of days spent in any other single State.

Fraction of days: even few minutes matter

Physical presence for most part of the year is a formal new criterion even though de facto already used by tax authorities in the past.

The law states that fractions of day count as entire days. The Circular makes the example of a person who arrives at 23.00 of July 1st, 2024, and departs at 1.00 of December 31st, 2024: in this case, both July 1st and December 31st count as days of presence in Italy even if the relevant person spent just one hour in each day.

As a mitigant, the Circular states that care should be given to special situations where the presence in Italy is merely temporary and occasional.

The Circular makes one single example related to airport stopover due to coincidence in going in a foreign State. But other cases are equally relevant. Three examples:

- a person lives in Monaco and enjoys cycling. One usual circuit crosses over the Italian border for few kilometres;
- a person living in Monaco is used to go skiing in Saint Moritz and to this end drives through Italy. Is this equivalent to an airport stopover? And what if the same person stops for lunch/dinner or meets a friend or business parties for a couple of hours?
- a person lives in Lugano and travels extensively out of Switzerland. The closest airport facility is Malpensa airport in the Italian territory: can the consequent physical presence be disqualified? And what if the same person flies through Linate?

All these questions may look odd but have been raised in the past in the course of tax audits and likely will be raised again in the future.

Frontier workers and treaty tie breaker rules

The Circular makes also the example of a frontier worker who lives outside Italy and travels to Italy for work almost every single day returning to the home State where the family lives.

In this case, the frontier worker would be considered resident of Italy for domestic tax purposes but for treaty purposes might still be considered a resident in the other country.

Nothing new but good to read it so clearly!

Registration in the List of Resident Population as rebuttable presumption

The new rules have maintained as a residence criterion the registration (for most part of the year) in the List of Resident Population. Whilst this formal criterion amounted to a non-rebuttable presumption under previous law, the new rules clarify that the presumption is now rebuttable without however clarifying who can give contrary proof.

The Circular focuses on the contrary evidence from the taxpayer, without mentioning the chance for tax authorities to give the same evidence. The matter is not just theoretical, as tax authorities may have an interest in denying domestic residence for instance for “impatriate workers”.

This situation is not new in the Italian tax environment and in other situations the outcome was that the presumption can also be rebutted by tax authorities.

Chi vivrà vedrà!

Registration in the List of Resident Population and treaties

The Circular confirms the previous interpretation of the Revenue Agency under which the formal criterion of the registration in the List of Resident Population is relevant for the purposes of Article 4, para. 1, of treaties aligned to the OECD Model Treaty. In such case, tie breaker rules apply.

This conclusion cannot be agreed with as Article 4, para. 1, of the OECD Model refers to substantive ties and not to just formal ones. It is true that tie breaker rules may void interest in this *querelle* but there are cases where the matter is highly practical.

For instance:

- (i) Mr. X is resident in State A and receives income from State B, where is normally taxed under State B domestic tax rules;
- (ii) Mr. X comes to Italy and registers himself in the List of Resident Population whilst still living in State A only;
- (iii) the Treaty between State B and Italy provides that the relevant income is taxed in Italy only.

Can State B argue that Mr. X is not actually resident of Italy for treaty purposes?

Can State B try to rebut the presumption of Italian tax residence?

The issue is very important and triggers a more general question: are certificates of residence released by a State binding for foreign States? Can States fully rely on their peers?

This issue will be dealt in a following newsletter.

Hope you can wait!

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