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TAX RESIDENCE IN ITALY: THE ITALIAN TAX REVENUE OFFICE GUIDELINES

Circular Letter 20/E of 4th November 2024.

A first comment by our International Tax Team in Milan, Italy

November 2024

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TAX RESIDENCE IN ITALY: THE ITALIAN TAX REVENUE OFFICE GUIDELINES

A first comment by our International Tax Team in Milan, Italy

From January 1st, 2024, a new definition of tax residence has been introduced into the Italian tax legislation. The Italian Tax Revenue Agency published on 4th November 2024 Circular Letter 20/E. Hereinafter a summary:

TAX RESIDENCE IN ITALY FOR COMPANIES AND ENTITIES

- Legislative Decree No. 209/2023 introduced from January 2024 new criteria for determining the tax residence of companies, aligning with international practices.
- The 'legal site' criterion remains.
- The concept of 'seat of administration' has been replaced with 'effective place of management' and 'place of principal ordinary management'. The 'main object' criterion has been eliminated, which previously caused interpretative difficulties.
- The new criteria emphasize the relevance of factual aspects over formal requirements. It must be judged in accordance with International and OECD guidelines.

From this perspective, the **Italian legislator has aligned the wording of the tax residence criteria in force in Italy with international practice**, first of all replacing the criterion of the 'seat of administration' with the two different criteria of the '**place of effective management**' and the '**principal place of management'**. These criteria were already implicitly contained in the concept of 'seat of administration'; however, the new wording of the legislation allows for a more accurate scope of application for defining tax residence and avoids extensive interpretations by clarifying without a shadow of a doubt the irrelevance of the place where shareholders reside and/or meet for the purpose of defining the tax residence of companies and entities. In fact, the new law specifies that:

- **place of effective management** means the place where the strategic decisions concerning the company or the entity as a whole are taken in a continuous and coordinated manner, not counting the decisions other than those having management content taken by the shareholders nor the supervisory activity and any monitoring of the management by the same;
- **place of principal ordinary management** means, on the other hand, the continuous and coordinated performance of the acts of day-to-day management concerning the company or the entity as a whole, thus making it possible to enhance the entity's actual rootedness in the territory of the State. In essence, this is senior day-to-day management, i.e. the intermediate level made up of managers responsible for groups of people and their performance as well as the implementation of the strategic decisions of top management.

Former law	The law since January 1st 2024
For income tax purposes, companies and entities that, for most of the tax period, have their registered office, place of administration, or principal business activity in the territory of the State are deemed to be resident. Collective investment undertakings established in Italy are also deemed to be residents, as are trusts and similar institutions established in jurisdictions other than those specified by the Decree of the Minister of Economy and Finance issued under Article 168-bis, provided that at least one settlor and one beneficiary are tax residents in Italy, unless proven otherwise. Trusts established in a jurisdiction other than those specified by the Decree of the Minister of Economy and Finance issued under Article 168-bis are also deemed to be residents in Italy if, after their establishment, an Italian resident makes a contribution to the trust that results in the transfer of ownership of real estate, the establishment or transfer of real property rights (including shares), or imposes destination constraints on these assets.	For income tax purposes, companies and entities that, for most of the tax period, have their registered office, place of effective management, or principal ordinary management in the territory of the State are deemed to be resident. The "place of effective management" refers to the ongoing and coordinated decision-making process regarding the overall strategic direction of the company or entity. "Ordinary management" refers to the continuous and coordinated execution of day-to-day management activities concerning the entire company or entity. Collective investment undertakings are deemed to be residents if they are established in Italy. Trusts and similar institutions established in jurisdictions not listed in the Decree of the Minister of Economy and Finance issued pursuant to Article 11, paragraph 4 (c), of Legislative Decree No. 239 of 1 April 1996, are also deemed to be residents in Italy, provided that at least one settlor and one beneficiary are tax residents in Italy, unless proven otherwise. Trusts established in jurisdictions not listed in the Decree of the Minister of Economy and Finance issued pursuant to Article 11, paragraph 4 (c), of Legislative Decree No. 239 of 1 April 1996, are further deemed to be residents, unless proven otherwise, if, after their establishment, an Italian resident makes a contribution to the trust that results in the transfer of ownership of real estate, the establishment or transfer of real property rights (including shares), or imposes destination constraints on these assets.

The same changes apply to **partnerships and similar entities**. According to Article 5, paragraph 3, letter d) of TUIR, as amended by Article 2, paragraph 2 of the Decree, "*partnerships and associations that, for most of the tax period, have their registered office, place of effective management, or principal ordinary management in the territory of the State are deemed to be resident*".

Tax Residence in Italy for Individuals

Legislative Decree No. 209/2023 introduced from January 2024 new criteria for determining the tax residence of individuals.

An individual is considered a tax resident in Italy if, for the greater part of the fiscal year:

- **Physical Presence**: The individual is physically present in Italy.
- **Residence**: The individual has a 'residence' in Italy, which is defined as their habitual abode, following the Italian civil code rules.
- **Domicile**: The individual has a 'domicile' in Italy, which is defined as the principal centre of their personal and family interests. It is worth to underline that the new rule inserts a new definition of '**tax domicile**' which differentiate from the civil code definition: "the place where the personal and family relations of the individual are principally developed".

The recent changes emphasize the **relevance of personal and family relationships** over economic and work-related interests when determining tax residence.

Individuals registered in the resident population register for most of the tax period are presumed to be residents, unless proven otherwise. Registration is mandatory for those who have their habitual abode in Italy.

Italy maintains the **reversal of the burden of proof of foreign residence** for **Italian citizens who transfer their residence to countries considered as 'tax havens'.** They are deemed to be resident in Italy, unless they can prove otherwise.

Tax residence is triggered if the individual spends more than **183 days** (or **184 days** in leap years) in Italy, with fractions of days counted as whole days.

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Former Law	The law since January 1st 2024
For income tax purposes, individuals who, for most of the tax period, are enrolled in the resident population registries or have their domicile or residence within the meaning of the civil code in the territory of the State are deemed to be resident.	For income tax purposes, persons who, for most of the tax period, also considering fractions of a day, have their residence within the meaning of the civil code or their domicile in the territory of the State or are physically present therein are deemed to be resident. For the application of this provision, domicile is defined as the place where personal and family relationships of the person mainly develop. Unless otherwise proven, also persons enrolled for most of the tax period in the resident population registries are presumed to be resident.

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THE TAX GUIDELINES PROVIDED CIRCULAR LETTER 20/E OF 4TH NOVEMBER 2024 ISSUED BY ITALIAN TAX REVENUE AGENCY

The new rules received various comments from practitioners and doctrine, including Assonime's Circular No. 15/2024, published on 30 July 2024, and few articles from our International Tax Team in Milan, publishing on the leading Italian tax magazines:

- The 'new' tax residence of natural persons and the impacts on multi-jurisdictional families
- The 'new' tax residence of companies and entities in the Italian tax reform

On 4th November 2024, the Italian Tax Revenue Office published the Circular No. 20/E, which provides guidance on the tax residency for individuals, companies and other entities.

With **Circular 20/E**, the **Italian Tax Revenue Office provides its interpretation and guidelines** of the new definition of tax residence for individuals, companies and other entities for income tax purposes.

A) CLARIFICATIONS PROVIDED ON LEGISLATIVE AMENDMENTS REGARDING THE TAX RESIDENCE OF NATURAL PERSONS

Regarding individuals, the new definition clarifies the meaning of tax residence based on "**tax domicile**" and according to the Circular 20/E now referring to "**personal and family relations**" which includes both family relationships and personal relationships. In particular states "*The notion of "personal and family relationships" comprises both the typical relationships regulated by the current law (for example conjugal relationships or civil partnerships) and stable personal relationships expressing an attachment to the Italian territory (as for example, a stable couple living together). Equally, taxpayer's stable social relationships can be relevant to the extent to such relationships result from concrete elements as, for example, the annual membership of a cultural and sports club.*" And "*In order to assess the configuration of a person's domicile in our State, it is therefore necessary to carry out a check that takes account of the above-mentioned circumstances, without neglecting, however, to consider also the conduct by which a person manifests with concrete actions an intention to maintain a close connection with Italian territory*".

The Circular 20/E addresses considerations for **remote or frontier workers**, and the application of treaty tie-breaker rules. To summarize the Administration thinking it is relevant to consider the following:

- **workers who perform their activity remotely from Italy** must pay attention to the new condition of the physical presence in Italy. If they trigger the rule, they are considered tax resident in Italy with the worldwide taxation principle being applicable.
- **workers who perform their activity from abroad (i.e. smart workers from abroad)**, it is understood that the new rules are applicable and therefore it is to be paid attention to the various criterion of the new art. 2 TUIR including the physical presence in Italy and the enrolment in the resident population registry

The Circular 20/E provides some examples meant to explain their interpretation

Example 1: Habitual Abode (Civil Law Residence) Test

An individual:

- resides habitually in Italy from **1 January 2024 to 29 February 2024**;
- moves abroad between **1 March and 29 August 2024**; and
- returns to Italy from **30 August to 31 December 2024**.

Despite the interruption during the taxable year, the individual is considered an Italian tax resident because they maintained a habitual abode in Italy for 184 days, constituting most of the calendar year.

Example 2: Domicile Residence Test

An individual:

- has homes in both Italy and another country ("the other State");
- has a son from a first marriage living in the Italian home;
- has a wife from a second marriage living in the home in the other State;
- works primarily in Italy;
- travels frequently outside Italy;
- spends weekends and holidays in the other State with his spouse; and
- spends **145 days in Italy, 120 days in the other State**, and **100 days in third countries**.

The Italian Revenue Agency notes the difficulty in determining the individual's domicile due to split family and personal interests between Italy (child) and the other State (spouse). However, it deems the criterion of the **prevalence of days spent** reasonable. Under these circumstances, the individual is considered to have an Italian domicile and thus to satisfy the tax residence requirement.
Double Tax Agreements and treaties are of course applicable in such circumstances.

The Italian Tax Revenue Office clarify that "*As a consequence of the amendments made by the Decree, from tax year 2024, clarifications rendered with respect to the notion of domicile, in the aforementioned Circular No. 25/E of 2023, paragraph 1.1, are no more applicable; nevertheless, such clarifications remain valid for the previous tax years.*"

Example 3: physical presence in Italy

An individual – not enrolled in the resident population registry and without residence and domicile in Italy – arrives in Italy by a plane that lands at 11:00 p.m. on 1st of July 2024 (leap year)

He/She remains uninterruptedly in the territory of the State until 1:00 a.m. on 31st of December 2024.

Due to the fraction of day criterion, the days of 1st of July and 31st of December 2024 are fully considered for tax purposes and, because of physical presence for 184 days, the taxpayer is considered to be resident in Italy.

Tax regimes for individuals transferring their residence to Italy for tax purposes.

Circular 20/E comments about the criterion of eligibility of the different regimes such as:

- The **HNWI New Tax Resident flat tax regime** (200k for the main applicant and 25k for any other)
- The **Pensioners regime**
- The **Talents regime ('impatriati')**

These regimes require not having been resident in Italy in previous tax periods and therefore the Italian Tax revenue Office comments about the new rules about tax residence. Administration comments that "*the new rules on the residence of natural persons introduced by the Decree will apply starting from the 2024 tax period. Accordingly, the requirement of non-residence for tax purposes in Italy, which is a prerequisite for access to the three regimes mentioned above, has to be assessed in light of the new Article 2, paragraph 2, of TUIR, only for the 2024 and subsequent tax periods.*" For former years the old rules are applicable.

Interaction with Double Taxation Conventions

According to Circular 20/E "*The new provisions introduced by the Decree may create new cases of conflict of residence that may need to be resolved through the mentioned tie breaker rules*". The circular letter makes some examples about employees living in a State bordering Italy, who cross the border daily to work in Italy (e.g. Slovenia). Based on the new criterion of physical presence, which counts fractions of a day, such natural persons could be deemed

residents for tax purposes in Italy if they are present in the Country on most days of the year (even if only for fractions of days). **The conflict of residence may be resolved by applying the tie-breaker rules in the Double Taxation Convention with Italy**. The Circular 20/E makes mention also to the so-called slit year (e.g. Germany, Switzerland and Panama). The Italian Administration also recognize, based on advanced tax rulings No. 50/2023, No. 73/2023, and No. 79/2023, and jurisprudence of the Supreme Court judgements No. 26638 of 10 November 2017, and No. 20285 of 23 May 2013, **primacy of substantive criteria under Double Taxation Conventions over formalistic requirements.**

B) Clarifications provided on legislative amendments regarding the tax residence of companies and other entities

According to Circular 20/E **companies** and **entities** as well as **partnerships** and **similar entities** are now under the new law, since January 2024. The above is applicable also to **funds** and to **trusts**. Actually "*the rule that the fulfillment of any one of the three criteria is sufficient to establish residence in Italy remains unchanged, as does the requirement that residence must be maintained for most of the tax period. Regarding collective investment undertakings, the connection criterion remains the same as in the previous legislation, where tax residence is determined by the location of establishment. No significant changes have been made to the rules governing the residence of trusts and similar institutions. The criteria for determining their residence remain the same as under the previous legislation.*". The determination of the residence of trusts is subject to an amendment as regards the burden of the proof. According to the new Article 73, paragraph 3, of TUIR "Trusts established in jurisdictions not listed in the Decree of the Minister of Economy and Finance issued pursuant to Article 11, paragraph 4 (c), of Legislative Decree No. 239 of 1 April 1996, are further deemed to be residents, **unless proven otherwise**, if, after their establishment, an Italian resident makes a contribution to the trust that results in the transfer of ownership of real estate, the establishment or transfer of real property rights (including shares), or imposes destination constraints on these assets" (emphasis added).

The place of effective management

According to Circular 20/E "*The principle of prevalence of substance over form permits, on one hand, to avoid making the connection criterion meaningless and, on the other hand, in a perspective of alignment with the legislations of the other States, to prevent possible conflicts of residence, as a result of the mismatch between the criteria adopted by the domestic laws to establish residence in the respective national territory.*" The Italian Administration aligns to the OECD guidelines and further specify "*as regards the material determination of the place of effective management, due to the technological development, it is possible that the place where the business is carried out and the place where strategic decisions are taken do not coincide.*

In this regard, since there are no consolidated practices at international level, a case-by-case analysis of the concrete cases that may be realised is needed."

The place of principal ordinary management

This criterion has an autonomous relevance and is alternative to the criterion of the place of effective management. According to the Explanatory Report to the Decree, in fact, the place of the principal ordinary management represents an effective connection of the company or the entity with the territory. Hereinafter the Circular 20/E: "*The intention is, therefore, once again to ensure greater legal certainty*." It is therefore consistent with paragraph 24.1 of the Commentary on Article 4 of the OECD Model.

The law specifies that management shall concern the undertaking as a whole, in order to distinguish the legal person's country of residence from the place where the permanent establishment is located. Article 2 of the Decree, in fact, introduced the clarification that the ordinary management shall be "principal", in order to distinguish it, as clarified in the Explanatory Report, from the permanent establishment.

Accordingly, "*The specification of the characteristics of the management to determine the tax residence in Italy does not preclude the possibility that the company has establishments located abroad, as long as the ordinary management activity is carried out mainly in Italian territory*."

Interaction with Double Taxation Conventions

When double residence occurs, resulting in double taxation, because of different criteria for the establishment of residence in its own territory, usually Conventions concluded by Italy contain a conflict resolution rule, that allocates the tax residence in the contracting State in which the place of effective management is set. As noted by the Administration, however, it should be noted that in certain international treaties concluded by Italy (see the Conventions in force with Canada and Chile), a version coherent with the current paragraph 3 of Article 4 of the OECD Model has been adopted, resulting with a conflict resolution by mutual agreement, with regard, in particular, to the place of its effective management, the place where it has been established or otherwise created and any other relevant elements. In the absence of such an agreement, that person shall not be entitled to claim any tax relief or exemption under the Convention.

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You can find an informally translated copy of Circular 20/E/2024 at this link.

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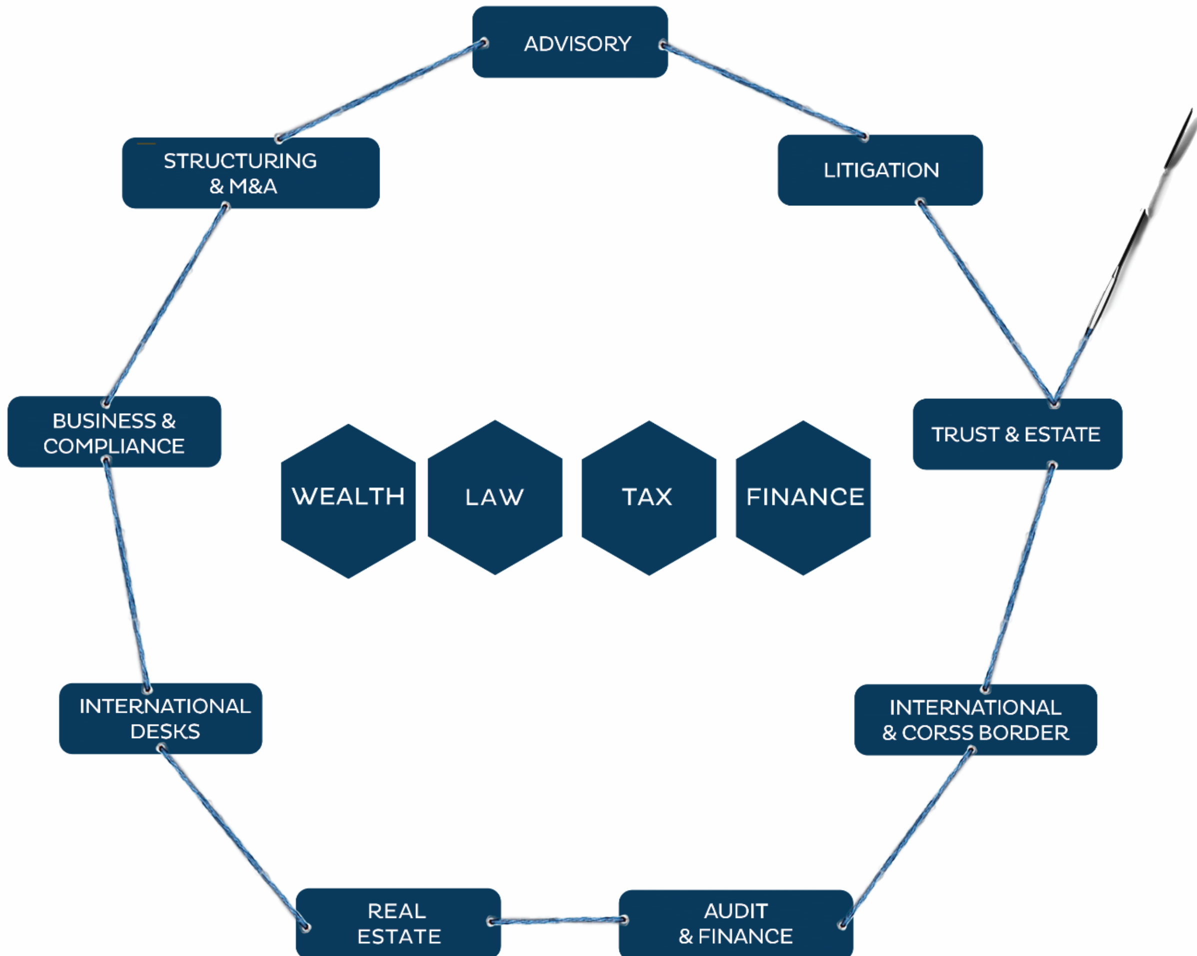

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