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Italian Revenue Agency Refers to DTC's Nationality Non-discrimination Rule to Interpret Domestic Maritime Exemption Provision

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The Revenue Agency confirms the exemption of income derived abroad by foreign maritime employees who are tax residents of Italy

The Italian Revenue Agency has recently issued a ruling (No. 134/2020) clarifying that the income derived by a Spanish citizen (and Italian-tax resident) maritime employee working aboard a ship flying a non-Italian flag for more than 183 days in a 12-month period is excluded from tax in Italy.

The ruling is interesting as it is one of the few cases where the domestic law of a country appears to discriminate taxpayers on the basis of their nationality (not tax residence).

The relevant legal framework

At the outset, it is worth recalling that, in the shipping sector, the territoriality of the income is generally linked to (i) the localization and (ii) the flag of the ship or aircraft, both of which are relevant in order to identify the portion of income that should be regarded as sourced abroad and which therefore might also be subject to other states' tax jurisdiction. With regard to Italy, the relevance of the flag is rooted in Article 4 of the Navigation Code, which provides that Italian ships on the high seas are regarded as Italian territory. Symmetrically, ships flying foreign flags are regarded as flag-state territory, except for when they are situated in the Italian territorial water.

Against this background, Italy applies – as a general rule – the worldwide taxation principle for income tax purposes, unless a specific tax treaty provision applies, so that Italian resident employees are usually taxed in Italy on both domestic and foreign income.

A special tax provision that deviates from the ordinary regime mentioned above is provided for in Article 51(8-*bis*) of the Consolidated Income Tax Act ("CITA"). That provision establishes an alternative rule for computing the tax base of income from employment activities performed exclusively abroad on an ongoing basis by Italian-resident employees that stay in the foreign country for more than 183 days in any 12-month period. Under Article 51(8-*bis*) CITA, the tax base corresponds to the "conventional remuneration" (*retribuzione convenzionale*) annually established by the Ministry of Labour and Social Welfare. The taxable base so determined is generally lower than the actual remuneration received by the employee, since it does not include any bonus or variable part of the remuneration.

Article 5(5) of Law 88 of 16 March 2001 provides for a specific application of Article 51(8-*bis*) CITA in the shipping sector, establishing that income derived by Italian maritime employees working aboard ships flying foreign flags for more than 183 days in a 12-month period is excluded from the Italian tax base, irrespectively of the localization of the ships and the tax residence of the employer and employee. Moreover, in such a case, the employee is not subject to any tax return obligation in Italy (see the Revenue Agency's Circular No. 55/E of 2002). With regard to the calculation of the days of actual presence of the worker abroad, the Ministry of Finance Circular Letter 207 of 16 November 2000 clarified that "it should be noted that the period to be considered should not necessarily be continuous: it is sufficient that the worker performs its work abroad for a minimum of 183 days in any 12 months. It is appropriate to point out that the legislature, by using the expression 'twelve months' did not intend to refer to the tax period, but the permanence of the worker abroad as provided for in the employment contract, which may also involve a period falling into two calendar years."

The ruling

With ruling No. 134/2020, the Revenue Agency has clarified that the notion of "*Italian maritime employees*", for the purpose of Article 5(5) of Law 88 of 16 March 2001, notwithstanding its wording, is not limited to Italian national maritime workers, but extends to foreign nationals (both EU and non-EU) to the extent they are tax residents of Italy. The taxpayers are also exempted from any obligation to indicate the above-mentioned income in their tax return. A different interpretation, according to the Agency, would have triggered a conflict with the principle of non-discrimination based on nationality encompassed in Article 24(1) of the Italy-Spain tax treaty, which is in line with Article 24(1) of the OECD Model Convention. It is just the case to note that a different conclusion would also have encroached the prohibition of nationality-based discrimination provided for by Article 45 of the Treaty on the Functioning of the European Union.

What is the impact of COVID-19 on the functioning of this special rule?

Another relevant aspect, which, however, is not dealt with in the ruling, concerns the impact of COVID-19 on the concrete application of the rule. In this respect, it would be appropriate for the Revenue Agency to clarify that, for the purpose of applying Article 5(5) of Law 88 of 16 March 2001, the days in which the employees could not work aboard ships flying foreign flags because of sanitary restrictions were nonetheless to be regarded as days worked aboard those ships. This conclusion would be substantially aligned with the solutions proposed by the OECD in the document "*Secretariat Analysis of Tax Treaties and the Impact of the COVID-19 Crisis*", where it was suggested that the effects of the COVID-19 crisis should be as far as possible neutralized, due to the major changes and exceptional circumstances that characterize this pandemic (for instance, with regard to the residence test, it was held that "*in the short term tax administrations and competent authorities will have to consider a more normal period of time when assessing a person's resident status*" – point 36 of the OECD's document).

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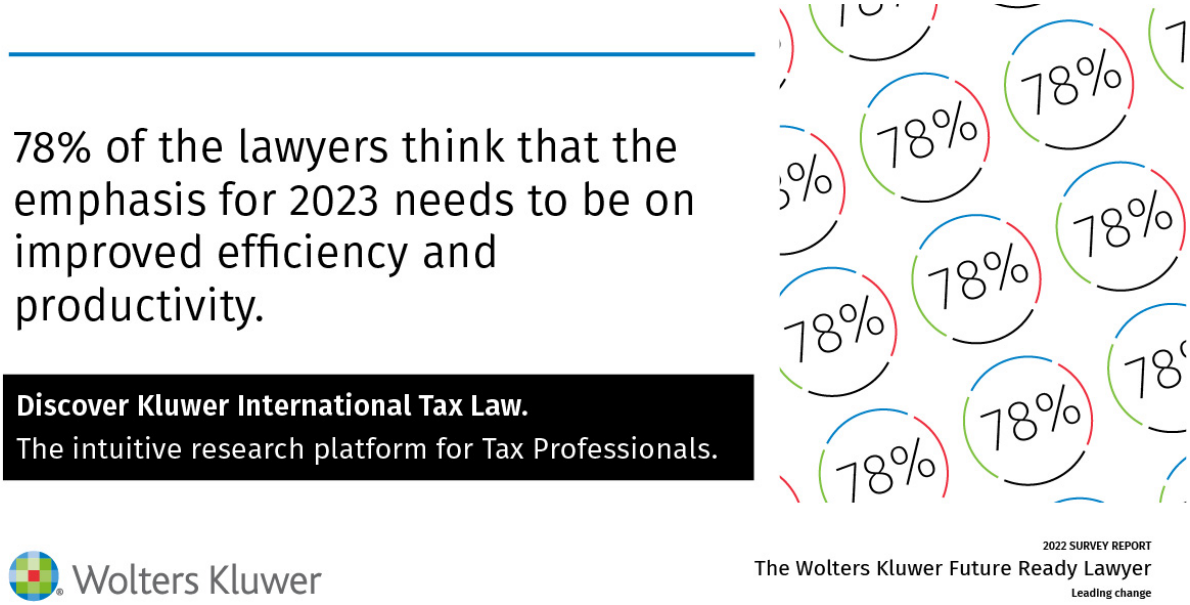

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