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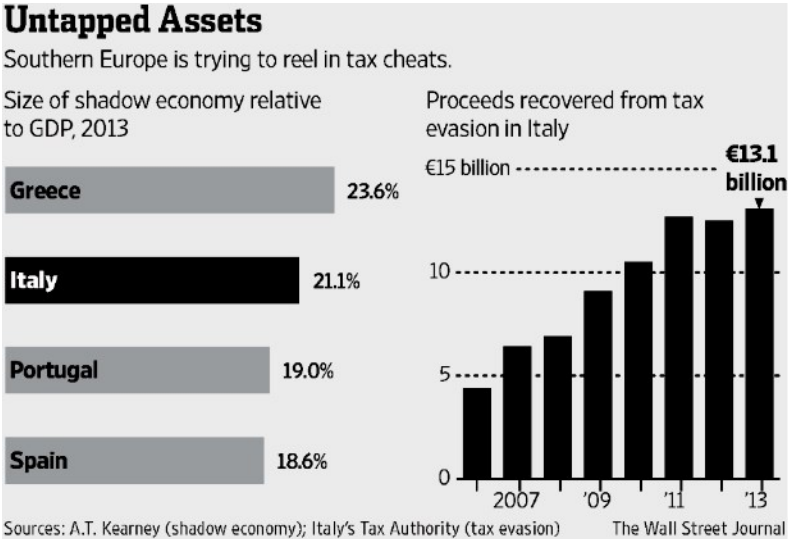
Southern Europe Tries Again to Tackle Tax Evasion



BY GIOVANNI LEGORANO

MILAN—Italy's latest effort to address its chronic tax evasion problem is keeping Tancredi Marino very busy. The Milan-based tax lawyer is hiring extra attorneys to handle dozens of requests from Italians looking to use an imminent amnesty to bring back money stashed in Switzerland and Monaco.

But Mr. Marino said he has also received—and spurned—15 requests from Italians wanting to shift money into other offshore centers to escape Rome's broad new crackdown on tax evasion, which annually robs Rome's coffers of €120 billion ($134 billion), or 7% of gross domestic product, according to an estimate by Italy's Audit Court.

"Many Italians just don't trust the system," said Mr. Marino of the law firm Pavia & Ansaldo. "Changing their mentality will take decades."

Mr. Marino's experience illustrates the stubborn resistance to aggressive government initiatives in recent years to stymie tax cheats, particularly in Southern Europe.

Even as Italy readies new efforts—including reaching an agreement Jan. 16 with Switzerland on exchanging account information—to claw back hidden funds and stem the flow of noncompliant money, tax evasion remains a scourge in much of Southern Europe, tax lawyers, experts and some political leaders say.

Alexis Tsipras, the leader of the far-left Syriza party who was sworn in Monday as Greece's new prime minister, says Athens's efforts to stop evasion have failed to target Greece's monied classes, whom many Greeks believe have salted away tens of billions of euros abroad. He promises a more just and effective clampdown to reversing the country's austerity regime.

"We need to stop this carnival of tax evasion and avoidance," Mr. Tsipras said during the campaign. He has also said "tax evasion by the oligarchs" is the norm in Greece.

The start of the financial crisis in 2008 kicked off a major global push to stop tax evasion, ranging from challenges to tax arrangements by companies such as Amazon and Starbucks to an aggressive U.S.-led battle to break down bank secrecy in Switzerland, the world's largest offshore financial center and a major haven for hidden funds from France, Germany and Italy.

The ensuing eurozone crisis pushed Southern European countries in particular to tackle the longtime scourge. Greece appointed a former counterterrorism prosecutor to lead its tax-collection effort and introduced tougher penalties for bribing tax officials and compulsory online filing of tax returns. It hired 400 new university-educated tax collectors last year.

Spain sharply limited a much abused program allowing small businesses to pay a fixed amount of value-added tax each year based on expected rather than real revenue. And in a carrot-rather-than-stick approach, Portugal last year organized a lottery for people who demanded receipts for goods and services they bought. The government has awarded more than 35 luxury Audis to winners since April.

When the financial crisis hit Italy, entrepreneurs there were evading an average of more than 50% of the income taxes they owed, according to Bank of Italy estimates. Those with money offshore just waited for Rome to launch one of its generous amnesties to bring money back; a 2010 amnesty allowed tax dodgers to pay a paltry 5% of hidden money. A tiny fraction of Italian tax evaders ever go to jail, lawyers say.

In 2011, Italy's huge debt—now 135% of GDP—and spiraling sovereign borrowing costs pushed Prime Minister Mario Monti to draconian measures. Tax police launched high-profile inspections of hotels, bars and restaurants in posh resorts such as Cortina. They stopped Ferraris and Bentleys to collect data on owners and cross-check them with declared income.

The push bore some fruit—proceeds recovered from tax evaders tripled from 2006 to 2013—but it also caused collateral damage. Sales of jewelry, vacation homes and luxury boats crashed because of the tax inspections and a new €1,000 ceiling on cash purchases.

Now the government of Prime

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Minister Matteo Renzi wants a fresh approach, using a new set of carrots and sticks. It is offering a new amnesty, which will go fully into effect in early February, allowing Italians to come clean on undeclared offshore funds. But penalties are high, in some cases possibly wiping out the entire amount hidden.

Those who don't take up the voluntary disclosure and are caught now risk eight years in jail. Economists expect at least €30 billion to be repatriated through the amnesty, yielding more than €6 billion in extra tax revenues.

At the same time, the government wants a more positive relationship with taxpayers. The tax authority will send pre-filled tax declarations to all taxpayers except the self-employed. It will conduct fewer but more targeted audits and will simplify the tax code.

Doubts linger, however, as to whether the tax clampdown in Southern Europe is succeeding in rooting out tax evasion.

In Spain, government data show efforts to lower tax evasion have consistently fallen short of targets in recent years, while tax revenue has often missed forecasts.

Moreover, undeclared assets in Southern European countries remain very high. According to the consulting firm A.T. Kearney, the share of the shadow economy in these countries' gross domestic product hasn't substantially changed since 2008. In Greece, it was around a fourth of GDP in 2013, and around a fifth in Italy, Spain and Portugal.

In Italy, tax lawyers say some clients have already moved assets to non-European offshore centers such as Dubai and the Bahamas. Others are using hidden cash to buy diamonds, expensive watches or gold, which they hope to bring to Italy undetected. Some individuals are considering shifting their nominal tax residence outside Italy.

In November, Italy's Audit Court, a budgetary watchdog, said the push had yielded modest results. People considered most at risk of dodging taxes get audited only once every 30 years on average, the court said, adding that those who undergo an audit typically return to illegal behavior after two years. The court also said tax authorities manage to collect only about half the evaded tax they unearth.

"The problem is Italians' way of thinking," said Stefano Simontacchi, managing partner at Milan law firm Bonelli, Erede and Pappalardo. "To change that we'd need 20 more years."

—Patricia Kowsmann in Lisbon, David Roman in Madrid and Nektaria Stamouli in Athens contributed to this article.