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Tax Hostages?

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Do you believe the tax system should be used to punish people with unpopular views? One of old Soviet Union's actions that was most heavily and correctly criticized by human-rights activists both left and right was its confiscation of the wealth of those who chose to leave the U.S.S.R. The right to emigrate is considered by civilized people to be a basic human right.

Regretfully and embarrassingly, the U.S. Congress has just passed a law that places a higher tax burden (and in some cases wealth confiscation) on those who choose to permanently leave the United States, and may make some "tax hostages."

You may be thinking, so what, "it doesn't affect me and I don't care about those who leave my country." The reason you should care about how the government deals with such people is that wrong policies, if implemented, will undermine both investment and the rule of law in the United States, thus reducing employment and economic growth.

Some of the small number of Americans who renounce their citizenship and move elsewhere do so because they disagree with U.S. policies, and some do it to avoid what they consider unreasonable and excessive taxation. Others do it for very benign reasons, such as having married a foreign national and choosing to live in their spouse's country, not wanting to be double-taxed by the United States. And some, who had immigrated to the United States wish to retire to their original home country and again avoid double taxation by the U.S. government. (This occurs in jurisdictions where there is no tax treaty.)

People who choose to renounce their citizenship are often looked upon as traitors, both by those in totalitarian and authoritarian states, and unfortunately sometimes by those in democratic societies, even when their intentions are benign.

Many who immigrated to America over the last four centuries had some, or most of, their wealth in the old country taken from them in one form or another. This was rightly considered unjust. Yet, the descendants of many of those who suffered just voted to do something similar that differs only in degree, but not in kind or spirit.

Under the old law, tax exiles were required to file annual U.S. tax returns for 10 years after they had renounced their citizenship. They were also required to pay taxes on all

U.S.-source income, including estate and gift taxes. Many considered this law a basic infringement on human rights. (Note: Those who were never citizens and were not residents did not have to pay taxes on most U.S.-source income.)

This law affected very few people because low- and middle-income earners were exempted and clever people could legally and illegally get around it with relative ease. But, rather than get rid of the old, bad law, Congress decided to replace it with a worse law.

The new law will replace the current 10-year transition law. U.S. citizens will now be required to pay a tax immediately upon giving up their citizenship or "green card" status on their unrealized capital gains. This includes unrealized gains in a stock portfolio, real estate, art or other assets. Most foreign citizens are exempt from certain portfolio interest, dividends and capital-gains taxes; and American citizens normally only have to pay tax on realized gains. Hence, this new law clearly discriminates against those who choose no longer to be Americans, by taxing only them on unrealized gains.

People with insufficient cash to pay the tax on such unrealized capital gains, particularly those with illiquid assets, may face the choice of having the Internal Revenue Service seize their assets or become "tax hostages."

The apologists for Fidel Castro and Hugo Chavez will be able to point to this new U.S. law and ask why this is any different from the property takings by the aforementioned thugs? Yes, it is bit different, but behind it is the same mean-spiritedness, and disregard for property rights and the right to emigrate because of political beliefs. Such laws only make the United States look hypocritical to the rest of the world.

Yes, this law only affects relatively well-off people, many of whom could be charged with being unpatriotic. The reason everyone else should care is that once the principle and precedent is established that it is not wrong to discriminate against people because of their political beliefs, or former citizenship status, the fundamental concept of equality under the law has been undermined, which will also damage economic growth.

Laws like this are passed in Congress because some on the left think they may be able to get a few more tax dollars from "rich people," and some on the right think it is fine to punish people they believe to be unpatriotic. Both have forgotten that the purpose of government is to protect people and property and to ensure liberty.

Everyone would do well to remember the wise comments of the Scottish philosopher and economist Adam Smith when he wrote in 1755: "Little else is requisite to carry a state to the highest degree of opulence from the lowest barbarism, but peace, easy taxes, and a tolerable administration of justice, all the rest being brought about by the natural order of things."

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