"Deficit Terrorism" and Economic Warfare

All the Perks are going to Wall Street, while Main Street slips into Debt Slavery

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Wall Street banks have been saved from bankruptcy by governments that are now going bankrupt themselves; but the banks are not returning the favor. Instead, they are engaged in a class war, insisting that the squeezed middle class be even further squeezed to balance over-stressed government budgets. All the perks are going to Wall Street, while Main Street slips into debt slavery. Wall Street needs to be made to pay its fair share, but how?

The financial reform bill agreed to on June 25 may have carved out some protections for consumers, but for Goldman Sachs and the derivatives lobby, the bill was a clear win, leaving the Wall Street gambling business intact. In a June 25 Newsweek article titled "Financial Reform Makes Biggest Banks Stronger," Michael Hirsh wrote that the bill "effectively anoints the existing banking elite. The bill makes it likely that they will be the future giants of banking as well."

The federal government and Federal Reserve have advanced literally trillions of dollars to save the big Wall Street players, to the point where the government's own credit rating is in jeopardy; but Wall Street has not had to pay for the cleanup. Instead, the states and the citizens have been left to pick up the tab. On June 17, Time featured an article by David von Drehle titled "Inside the Dire Financial State of the States," reporting that most states are now facing persistent budget shortfalls of a sort not seen since the 1930s. Unlike the Wall Street banks, which can borrow at the phenomenally low fed funds rate of .2% and plow that money back into speculation, states don't have ready access to credit lines. They have to borrow through bond issues, and many states are so close to bankruptcy that their municipal bond ratings are collapsing. Worse, states are not legally allowed to default. Unlike the federal government, which can go into debt indefinitely, states must balance their budgets; and they cannot issue their own currencies. That puts them in the same position as Greece and other debt-strapped European Union countries, which are forbidden under EU rules either to issue their own currencies or to borrow from their own central banks.

States, of course, don't even have their own state-owned banks, with one exception — North Dakota . North Dakota is also the only state now sporting a budget surplus, and it has the lowest unemployment and mortgage delinquency rates in the country. As von Drehle observes, "It's a swell time to be North Dakota ."

But most states are dealing with serious, chronic defaults, putting them in the same debt trap as Greece : they are being forced to lay off workers, sell public assets, and look for ways to squeeze more taxes out of an already over-taxed populace. And their situation is slated to get worse, since the federal government's stimulus package will soon be cut, along with assistance to the states.

The federal government is not only leaving the states high and dry but is threatening to impose even more taxes on their beleaguered citizens. Paul Volcker, former Federal Reserve Chairman and current White House economic adviser, said in April that Congress needs to consider a Value Added Tax (VAT) – a tax on various stages of production of consumer goods. A VAT of 17.5% is now imposed in Britain , and 20% is being proposed; while some EU countries already have a VAT as high as 25%. In Europe, at least the citizens get something for their money, including federally-funded health care; but that is not likely to happen in the U.S., where even a "public option" in health care is no longer on the agenda. The VAT hits the lower and middle classes particularly hard, since they spend most of their incomes on consumables. The rich, on the other hand, put much of their money into speculative trades, and those sales are not currently taxed.

Business Cycle or Class War?

Ismael Hossein-Zadehi, who teaches economics at Drake University in Iowa , calls the whole economic crisis a class war. What is being billed as public debt began as the private debt of financial speculators who offloaded it onto the public. The governments that bailed out these insolvent speculators then became insolvent themselves; but the bailed-out banks, rather than lending a helping hand in return, have demanded their pound of flesh, with payment in full. The perpetrators are blaming the victims and insisting on "fiscal responsibility." Wall Street bankers are dictating the terms of repayment for debts they themselves incurred.

"Fiscal responsibility" means cutting spending, something that is inherently deflationary during a recession, as seen in the disastrous Depression-era policies of President Herbert Hoover. Not that it was solely a Republican error. In 1937, President Franklin Roosevelt also cut public spending, tipping the economy back into recession. Spending cuts cause tax revenues to shrink, which results in more spending cuts. Contrary to what we have been told, national governments are not like households. They do not have to balance their budgets and "live within their means," because they have the means to increase the money supply. They not only have the means, but they must engage in public spending when the private economy is shrinking, in order to keep the wheels of the economy turning. Virtually all money now originates as bank-created credit or debt; and today the money supply has been shrinking at a rate not seen since the 1930s, because the banking crisis has made credit harder and harder to get.

Instead of "reflating" the collapsed economy, however, national governments are insisting on "fiscal responsibility;" and the responsibility is all being put on the states and the laboring and producing classes. The financial speculators who caused the debacle are largely getting off scot free. They not only pay no tax on the purchase and sale of their "financial products," but they pay very little in the way of income taxes. Goldman Sachs paid an effective income tax rate of only 1% in 2008. Prof. Hossein-Zadehi writes:

> "It is increasingly becoming clear that the working majority around the world face a common enemy: an unproductive financial oligarchy that, like parasites, sucks the economic blood out of the working people, simply by trading and/or betting on claims of ownership. . . . The real question is when the working people and other victims of the unjust debt burden will grasp the gravity of this challenge, and rise to the critical task of breaking free from the shackles of debt and depression."

Working people don't rise to the task because they have been propagandized into believing that "fiscal austerity" is something that needs to be done in order to save their children from an even worse fate. What actually needs to happen in a deflationary collapse is to spend more money into the system, not pull it back out by paying off the federal debt; but the money needs to go into the real economy – into factories, farms, businesses, housing, transportation, sustainable energy systems, health care, education. Instead, the stimulus money has been hijacked, diverted into cleaning up the toxic balance sheets of the financial gamblers who propelled the economy into its perilous dive.

Evening Up the Score

While Congress caters to the banks, the states have been left to fend for themselves. Where is the money to come from to pull off the impossible feat of balancing their budgets? Bleeding a VAT tax out of an already-anemic working class is more likely to kill the patient than to alleviate the disease. "Unlike EU countries, where the VAT is the largest single source of tax revenue," notes Professor Randall G. Holcombe in a recent study, "the states of the United States already tax the VAT tax base with their sales taxes." This doubling down on the same base would not only reduce the amount of money states are able to raise, but it would seriously hinder VAT's role as a money generator. By 2030, says Prof. Holcombe, this effect would have offset any increase in government revenue from the VAT.

A more viable and more equitable solution would be to tap into the only major market left on the planet that is not now subject to a sales tax – the "financial products" that are the stock in trade of the robust financial sector itself. A financial transaction tax on speculative trading is sometimes called a "Tobin tax," after the man who first proposed it, Nobel laureate economist James Tobin. The revenue potential of a Tobin tax is huge. The Bank for International Settlements reported in 2008 that total annual derivatives trades were $1.14 quadrillion (a quadrillion is a thousand trillion). That figure was probably low, since over-the-counter trades are unreported and their magnitude is unknown. A mere 1% tax on $1 quadrillion in trades would generate $10 trillion annually in public funds. That is only for derivatives. There are also stocks, bonds and other financial trades to throw in the mix; and more than half of this trading occurs in the United States .

A Tobin tax would not generate these huge sums year after year, because it would largely kill the computerized high-frequency program trades that now compose 70% of stock market purchases. But that is a worthy end in itself. The sudden, thousand-point drop in the Dow Industrial Average on May 6 showed the world how vulnerable the stock market is to manipulation by these sophisticated market gamblers. The whole high-frequency trading business needs to be stopped, in order to protect legitimate investors using the stock market for the purposes for which it was designed: to raise capital for businesses. As Mark Cuban observed in a May 9 article titled "What Business Is Wall Street In?":

> "Creating capital for business has to be less than 1pct of the volume on Wall Street in any given period. . . . My 2 cents is that it is important for this country to push Wall Street back to the business of creating capital for business. Whether it's through a use of taxes on trades, or changing the capital gains tax structure so that there is no capital gains tax on any shares of stock (private or public company) held for 5 years or more, and no tax on dividends paid to shareholders who have held stock in the company for more than 5 years. However we need to do it, we need to get the smart money on Wall Street back to thinking about ways to use their capital to help start and grow companies. That is what will create jobs. That is where we will find the next big

> thing that will accelerate the world economy. It won't come from traders trying to hack the financial system for a few pennies per trade."

Besides protecting legitimate savers and investors by exempting stock held five years or more, they could be exempted from a Tobin tax on total stock purchases of under $1 million per year. That would make the tax literally a millionaire's tax — and a small one at that, at only 1% per trade.

At the G20 summit in Toronto last weekend, a financial transaction tax was discussed and supported by France and Germany but was opposed by the U.S. and Canada , although nothing binding was resolved. However, the states do not have to wait for the federal government or the G20 to act. They could levy a Tobin tax themselves. Objection might be made that the Wall Street speculators would take their revenues and go elsewhere, but big banks and brokerages have branches in every major city in every state. They are hardly likely to pack up their tents and leave lucrative centers of business. Nor can it be argued that we should cater to the pirates who are looting our stock markets because they are paying us a nice bribe, because they aren't even paying a bribe. Financial trades do not currently generate tax revenues.

Two Green Party candidates for governor, Laura Wells in California and Rich Whitney in Illinois, have included a state-imposed Tobin tax in their platforms. Both are also campaigning for state-owned banks in their states, on the model of the Bank of North Dakota. People around the world look to the United States for boldness and innovation, and California and Illinois are two of the hardest hit states in the nation. If those states manage to turn their economies around, they could establish a model for economic sovereignty globally.

Ellen Brown developed her research skills as an attorney practicing civil litigation in Los Angeles . In Web of Debt, her latest of eleven books, she turns those skills to an analysis of the Federal Reserve and "the money trust." She shows how this private cartel has usurped the power to create money from the people themselves, and how we the people can get it back. Her websites are www.webofdebt.com, www.ellenbrown.com, and www.public-banking.com.
