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Michael Hudson: America's Deceptive 2012 Fiscal Cliff, Part II – The Financial War Against the Economy at Large

By Michael Hudson, a research professor of Economics at University of Missouri, Kansas City, and a research associate at the Levy Economics Institute of Bard College. His latest book is "The Bubble and Beyond."

Today's economic warfare is not the kind waged a century ago between labor and its industrial employers. Finance has moved to capture the economy at large, industry and mining, public infrastructure (via privatization) and now even the educational system. (At over $1 trillion, U.S. student loan debt came to exceed credit-card debt in 2012.) The weapon in this financial warfare is no larger military force. The tactic is to load economies (governments, companies and families) with debt, siphon off their income as debt service and then foreclose when debtors lack the means to pay. Indebting government gives creditors a lever to pry away land, public infrastructure and other property in the public domain. Indebting companies enables creditors to seize employee pension savings. And indebting labor means that it no longer is necessary to hire strikebreakers to attack union organizers and strikers.

Workers have become so deeply indebted on their home mortgages, credit cards and other bank debt that they fear to strike or even to complain about working conditions. Losing work means missing payments on their monthly bills, enabling banks to jack up interest rates to levels that used to be deemed usurious. So debt peonage and unemployment loom on top of the wage slavery that was the main focus of class warfare a century ago. And to cap matters, credit-card bank lobbyists have rewritten the bankruptcy laws to curtail debtor rights, and the referees appointed to adjudicate disputes brought by debtors and consumers are subject to veto from the banks and businesses that are mainly responsible for inflicting injury.

The aim of financial warfare is not merely to acquire land, natural resources and key infrastructure rents as in military warfare; it is to centralize creditor control over society. In contrast to the promise of democratic reform nurturing a middle class a century ago, we are witnessing a regression to a world of special privilege in which one must inherit wealth in order to avoid debt and job dependency.

The emerging financial oligarchy seeks to shift taxes off banks and their major customers (real estate, natural resources and monopolies) onto labor. Given the need to win voter acquiescence, this aim is best achieved by rolling back everyone's taxes. The easiest way to do this is to shrink government spending, headed by Social Security, Medicare and Medicaid. Yet these are the programs that enjoy the strongest voter support. This fact has inspired what may be called the Big Lie of our epoch: the pretense that governments can only create money to pay the financial sector, and that the beneficiaries of social programs should be entirely responsible for paying for Social Security, Medicare and Medicaid, not the wealthy. This Big Lie is used to reverse the concept of progressive taxation, turning the tax system into a ploy of the financial sector to levy tribute on the economy at large.

Financial lobbyists quickly discovered that the easiest ploy to shift the cost of social programs onto labor is to conceal new taxes as user fees, using the proceeds to cut taxes for the elite 1%. This fiscal sleight-of-hand was the aim of the 1983 Greenspan Commission. It confused people into thinking that government budgets are like family budgets, concealing the fact that governments can finance their spending by creating their own money. They do not have to borrow, or even to tax (at least, not tax mainly the 99%).

The Greenspan tax shift played on the fact that most people see the need to save for their own retirement. The carefully crafted and well-subsidized deception at work is that Social Security requires a similar pre-funding – by raising wage withholding. The trick is to convince wage earners it is fair to tax them more to pay for government social spending, yet not also to ask the banking sector to pay similar a user fee to pre-save for the next time it itself will need bailouts to cover its losses. Also asymmetrical is the fact that nobody suggests that the government set up a fund to pay for future wars, so that future adventures such as Iraq or Afghanistan will not "run a deficit" to burden the budget. So the first deception is to treat only Social Security and medical care as user fees. The second is to aggravate matters by insisting that such fees be paid long in advance, by pre-saving.

There is no inherent need to single out any particular area of public spending as causing a budget deficit if it is not pre-funded. It is a travesty of progressive tax policy to only oblige workers whose wages are less than (at present) $105,000 to pay this FICA wage withholding, exempting higher earnings, capital gains, rental income and profits. The raison d'être for taxing the 99% for Social Security and Medicare is simply to avoid taxing wealth, by falling on low wage income at a much higher rate than that of the wealthy. This is not how the original U.S. income tax was created at its inception in 1913. During its early years only the wealthiest 1% of the population had to file a return. There were few loopholes, and capital gains were taxed at the same rate as earned income.

The government's seashore insurance program, for instance, recently incurred a $1 trillion liability to rebuild the private beaches and homes that Hurricane Sandy washed out. Why should this insurance subsidy at below-commercial rates for the wealthy minority who live in this scenic high-risk property be treated as normal spending, but not Social Security? Why save in advance by a special wage tax to pay for these programs that benefit the general population, but not levy a similar "user fee" tax to pay for flood insurance for beachfront homes or war? And while we are at it, why not save another $13 trillion in advance to pay for the next bailout of Wall Street when debt deflation causes another crisis to drain the budget?

But on whom should we levy these taxes? To impose user fees for the beachfront reconstruction would require a tax falling mainly on the wealthy owners of such properties. Their dominant role in funding the election campaigns of the Congressmen and Senators who draw up the tax code suggests why they are able to avoid prepaying for the cost of rebuilding their seashore property. Such taxation is only for wage earners on their retirement income, not the 1% on their own vacation and retirement homes.

By not raising taxes on the wealthy or using the central bank to monetize spending on anything except bailing out the banks and subsidizing the financial sector, the government follows a pro-creditor policy. Tax favoritism for the wealthy deepens the budget deficit, forcing governments to borrow more. Paying interest on this debt diverts revenue from being spent on goods and services. This fiscal austerity shrinks markets, reducing tax revenue to the brink of default. This enables bondholders to treat the government in the same way that banks treat a bankrupt family, forcing the debtor to sell off assets – in this case the public domain as if it were the family silver, as Britain's Prime Minister Harold MacMillan characterized Margaret Thatcher's privatization sell-offs.

In an Orwellian doublethink twist this privatization is done in the name of free markets, despite being imposed by global financial institutions whose administrators are not democratically elected. The International Monetary Fund (IMF), European Central Bank (ECB) and EU bureaucracy treat governments like banks treat homeowners unable to pay their mortgage: by foreclosing. Greece, for example, has been told to start selling off—prime tourist sites, ports, islands, offshore gas rights, water and sewer systems, roads and other property.

Sovereign governments are, in principle, free of such pressure. That is what makes them sovereign. They are not obliged to settle public debts and budget deficits by asset selloffs. They do not need to borrow more domestic currency; they can create it. This self-financing keeps the national patrimony in public hands rather than turning assets over to private buyers, or having to borrow from banks and bondholders.

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