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Panama and the Criminalization of the Global Finance System

By Sharmini Peries - Michael Hudson
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Sharmini Peries: Within a week the 11 million documents called the Panama papers, published by the International Consortium of Investigative Journalists, has become a household name. The documents are connected to the Panama law firm Mossack Fonesca that helped establish offshore accounts for some of the wealthiest and most powerful leaders to launder money and evade taxes.

On Tuesday the police in Panama raided the Mossack Fonseca law firm to search for more documents linked to illicit activities. But what are they expecting to find, since we have already known for some time now that offshore accounts are being used to evade taxes by the banking sector, essentially white-collar crooks, at institutions such as Credit Suisse and others? But who is really behind the creation of these mechanisms and loopholes for tax evasion?

Economist Michael Hudson says Panama was created as a tax haven by certain sectors of our economy for this purpose. Hudson is a distinguished research professor of economics at the University of Missouri, Kansas City, and he's a former balance of payments economist for Chase Manhattan bank. He is the author of many books, and the latest among them is Killing the Host: How Financial Parasites and Debt Bondage Destroy the Global Economy.

Michael, let's begin with a short history of the creation of Panama and how it was bought from Colombia by the United States, and its relevance today vis-a-vis the Panama papers.

HUDSON: Well, Panama was basically carved off from Colombia in order to have a canal. It was created very much like Liberia. It's not really a country in the sense that a country has its own currency and its own tax system. Panama uses U.S. dollars. So does Liberia.

The real story didn't come out in the Panama papers. Reporters naturally focused on criminal people laundering money. But Panama wasn't designed to launder money. It was designed to launder earnings – mainly by the oil and the gas industries, and the mining industry.

Panama and Liberia were long noted as having “flags of convenience.” Oil tankers and mineral ships would register themselves under the flags of Panama or Liberia, or some other country that used the U.S. dollar, not its own local currency.

I first found out about this about 40 years ago, when I was doing a study of the balance of payments of the oil industry. I went to Standard Oil, whose treasurer walked me through their balance sheet. I said, I can't figure out whether Standard Oil and the other oil companies make their money at the producing end of oil, or at the distributing end of refining and selling it. And he said, “We make our earnings right here in New York, in the Treasurer's office.” I asked what he meant He explained: “We sell the oil that we buy from Saudi Arabia or the Near East at very low prices to the tanker company that's registered in Panama or Liberia.” They don't have an income tax in their country, because they're not a real country. The oil companies then sell the crude oil to downstream distributors in the United States or Europe – at a very, very high markup.

The markup is so high that there's no room for profit to be made at all in refineries or gas stations selling the oil. So the oil companies don't pay the tax collector in Europe anything. They don't pay the American government an income tax either. All their earnings are reported as being made in the tankers, which are registered in countries that don't tax income.

I told him that I had looked at the balance-of-payments reports from the Federal Reserve and the *Treasury Bulletin*. I see here's Europe, here's Latin America, here's Africa and Asia. I can't find where the profit remittances are.

He told me to look at the very last line on the right hand of the country tables. It's called "International." I asked whether all these countries in Europe and elsewhere were international. He explained to me that "International" was a special category for what was really part of the United States abroad. They're the offshore banking centers – Panama, Liberia, *et cetera*.

So I found out that basically Panama, and hence Panamanian companies, were set up initially to register oil tankers and mineral ships in order to give the appearance of taking all of their profits on the transporting the oil, or the copper or other minerals, from third world countries to the United States and Europe.

The United States went along with this. This made the oil industry tax exempt really since the 1920s. When the income tax was created in 1913 or 14, it was intended to capture economic rents. But the big rent extractors, oil and gas and minerals, got away with avoidance.

PERIES: Michael, you indicated in one of your articles that you were approached by a State Department operative in 1967. Tell us more about that experience.

HUDSON: It was from a former State Department person who had gone to work for Chase. The problem that America had in the 1960s was the Vietnam War. The entire balance-of-payments deficit of the United States in the 1950s and the '60s, right down to the early '70s, was military spending abroad. Either the dollar was going down or the United States had to sell gold. That's what finally led Nixon to take the dollar off gold in 1971. But for many years the United tried to fight against doing that.

So the State Department came to Chase, and said, we've got to figure out some way of getting enough dollars to offset the military deficit. They found the way to do it. It was to make the United States the new Switzerland of the world. I was asked to make a calculation of how much criminal capital there is in the world. How much the drug dealers made, how much the criminals all over made, how much the dictators secreted away. How much goes to Switzerland, and how can U.S. banks get this criminal money in the United States?

The end result was that the U.S. Government went to Chase and other banks and asked them to be good American citizens and make America safe for the criminals of the world, to safeguard their money to support the dollar in the process.

Earlier, Chase had been asked to create a bank in Saigon so that the army and other people wouldn't have to use French banks, which sent it back to France, where it ended up with General De Gaulle cashing it in for gold, Chase said, okay, we will help set up banks.

Other banks did this not to evade the law, not to break the law initially, but to be good citizens and attract crooked capital from all over the world. The same thing happened with the British West Indies – the Cayman Islands. They had declared their independence, but in order not to be a real country, in order to attract flight capital to England, they rejoined the empire as a colony so that they could serve as money laundering intermediaries. The idea was to have all of this money come to the United States or its ally Britain.

All this context can easily be traced. If you look at the money that goes into Panama and other offshore banking centers in the Caribbean, none of this money stays in Panama. It becomes “U.S. liabilities to Panama,” or other banking centers – mainly to U.S. bank branches in these regions.

PERIES: Michael, there is a question I want to ask you. Over the next few days there has been many questions raised about why there are not many Americans or even Canadians named in the leaked documents. Some speculate that this is because in the U.S. they don't need tax havens, because it is one. States such as Nevada, Wyoming, and South Dakota are considered the new Switzerland of tax evasion. Explain how the process works, because all this is interlinked.

HUDSON: You usually have not only one or two, but often three or four centers in a “veil of tiers.” The idea is not to put money into the United States directly. Imagine you’re a Russian kleptocrat, or a Ukrainian kleptocrat, and you want to take a billion dollars and keep it safe. You’re not going to put it directly into a Delaware corporation, or a Wyoming corporation. The money is going to *end up* there. But if you put it right in, then the U.S. Government and the bank would say, “Wait a minute. Here is the president of Ukraine with a billion dollars, right in our banking system.”

So what you have to do is launder the money. Likewise with the Colombian drug cartel. They’re not going to put the Colombian drug cartel balance in a Delaware bank under their name. It has to go through a lot of stages. The money goes out of the Ukraine and out of Russia into Latvia, primarily via the banks of Riga. I’ve met with individuals in Riga, Americans who provide the service of setting up maybe 30 companies for the money launderer. They will send the money, say, to the British West Indies. From the British West Indies it’ll go to Panama. And then it’ll go from Panama, already being concealed, to end up in a Delaware corporation at the end of the line.

You can look in the balance-of-payments statistics and you can find liabilities of bank branches in Panama or the British West Indies or whoever, owed to the U.S. head office. You can look and see how much American stock, how many American bonds, how many American bank deposits all come from these islands. The magnitude is so enormous that this is what has been supporting the dollar.

Congress is right behind this. In the 1960s it recognized that basically, criminals are the most liquid people in the world. They don’t want to tie down their money and property, because property can be seen, it’s visible. Finance in the balance of payments reports is called “Invisibles.” If you’re a criminal, you want to have your finance invisible in order to keep it safe. And the safest investment is U.S. Treasury bonds.

So there was an argument in Congress in the 1960s: Do we want to have 15% tax withholding on the Treasury bonds, especially to foreigners? It was pointed out that most foreigners who hold Treasury bonds actually are criminals. So Congress said, we need criminal money. We are not going to withhold criminal taxes. We’re going to make crime tax-free. We’re going to tax American industry, we’re going to tax American labor, but not foreign criminals, because we need their money. So we’re not going to withhold what they hold through their fiduciary accounts in Delaware, which was the main at that time, or New York, or London branches of

U.S. banks. The London branches of U.S. banks were the single major depositors and source of revenue of growth in the 1960s for Chase, Citibank and others. They were called eurodollars. The eurodollars flowing into these branches were very largely from drug dealing and arms dealing, and third world dictators in Africa and other places.

So under U.S. pressure, the international banking system was set up to facilitate the money laundering of drug capital. The reason the Americans and the Canadians were not particularly noteworthy in the law firm's records is the Panamanian law firm's records was that its role was to set up money laundering for foreigners, to conceal their means of getting money. But the oil industry doesn't conceal it. The oil industry declares all of the income it gets, and the mining industry declares all the income that it gets from the Panamanian shipping companies, from the Liberian shipping companies. But because Panama and Liberia don't have an income tax, there's no tax liability for this. It's stolen fair and square from the tax collector, just like California Senator Hayakawa said America had stolen Panama fair and square from Colombia.

PERIES: Wow. The big question here in all of these discussions and leaks is what are the solutions to this problem, and is it attainable at all?

HUDSON: Well, the solution is to tax companies on their worldwide earnings. If you know that a U.S. company like Standard Oil, Exxon now, makes X billion dollars earnings, you simply rule that it doesn't matter whether you declare these in Panama or the United States. We're going to treat the income that you declare from your Panamanian shipping company as if it is earned in the United States, and we're going to tax it at the U.S. rate.

However, this explains why there's not going to be a solution to money laundering. If you would solve the money laundering problem and tax companies and their worldwide earnings, you would tax Apple on all the income that it makes tax exempt in Ireland by using Ireland as a tax avoidance center, you would take on the largest vested interests in the United States – oil, gas and monopolies.

I don't think any politician is strong enough to attract campaign contributions from these main contributors and at the same time really push to tax them. They're going to go after the little guy who is trying to walk through the loopholes that the oil industry created a century ago. But it's hard to go after the little guy and the small tax evaders without catching the big fish. And the big fish are the biggest corporations in the United States.

That's why the problem is not going to be solved. It won't be solved largely because the United States wants to support the dollar by attracting all of this crooked money, just like England wants to support sterling by making itself the flight capital center for all of the biggest criminals in the world, from the Russian kleptocrats to African dictators and Asian money launderers.

The whole financial system basically has been criminalized in the process of being militarized, to subsidize the fact that countries like the United States and Britain have heavy military budgets. This is how they finance their military budget – with money laundering by the world's criminal class. The byproduct is to leave the largest companies tax exempt, from Apple to Exxon, right down the line.

