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THE COMING CURRENCY CARTEL COLLAPSE

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Why is there a demand for bitcoin? The short answer is that many do not trust government-issued and controlled currency – and such concerns are not unreasonable.

Three government-issued currencies dominate both foreign exchange trading and the holding of reserves: the U.S. dollar, the euro and the Japanese yen. The dollar accounts for almost 50 percent of trading, and the euro and yen combined for another 25 percent.

And all three are in deep trouble because the governments behind them have unsustainable debt burdens, as well as tax and regulatory structures that make the currencies less and less attractive to those who wish to hold or do business in them.

Alan Greenspan and other knowledgeable economists are arguing that the U.S. has been significantly underestimating the size of its national debt. The former chairman of the National Economic Council under President George W. Bush, Lawrence Lindsey, has recently said the national debt is closer to 300 percent of GDP when the unfunded liabilities for social security and Medicare are included. Others even have much higher estimates.

The euro is based on the fiction that its members will run deficits no greater than 3 percent of GDP. Of its big economies, only Germany is in decent fiscal shape, while France, Italy and Spain continue to accumulate debt at unsustainable rates. Japan is a debt basket case, with explicit debt well over 200 percent of GDP and a current deficit running at 6.9 percent of GDP. The Europeans and Japanese have the added burden of a slow demographic meltdown, further undermining the long-run faith in their currency.

Through increasingly foolish and destructive tax and regulatory policies, the Americans and Europeans have increased the incentives for businesses and investors to find alternatives for the dollar and the euro.

The U.S., by insisting that it tax the income of its citizens and residents regardless of where they live or have assets, is increasingly forced to extend its tax and financial regulatory laws into the sovereign space of other countries. This, quite understandably, builds resentment, undermines the rule of law, and reduces the desire by non-Americans to use U.S. dollars and U.S. financial institutions.

The new Foreign Account Tax Compliance Act regulations are the poster child for regulatory and tax self-destructiveness. The stated goal was to make sure that Americans (and other U.S. ‘‘taxpersons’’) were not avoiding U.S. income tax obligations. The ‘‘solution’’ was to require all non-U.S. financial firms who may have U.S. taxperson clients to report the information to the IRS.

So suddenly, non-American institutions are saddled with reporting to the IRS – and as these things take on a life of their own – increasingly every financial institution on the globe will be forced into reporting to every tax service in almost every country information about clients they may or may not have. Of course, none of this makes any sense from a cost-benefit perspective and is the antithesis of the concept of economic freedom or individual liberty.

There are a number of fatal flaws with the whole concept. One is: what is the definition of a financial institution? Not so simple. In the U.S., money laundering regulations and reporting requirements that were originally envisioned as applying to banks have been extended to car dealers, pawn shops, real estate brokers, etc.

Those seeking to evade reporting to government will look for any possible loophole, which, in turn, causes government to write more regulations to cover the newly found loophole. The result is there are so many regulations that the rule of law is beginning to collapse because no one or even any institution, including the government, can know what the law is.

Governments are increasingly demanding that individuals and businesses report all financial transactions to them. For instance, under the ‘‘Know Your Customer’’ regulations, financial institutions – as previously noted which are infinitely elastically defined – are supposed to know their customers, and their customers’ customers and so on.

If you are a customer of a financial institution and wish to withdraw some of your own money, that act is reported to the government above some threshold amount ($10,000). People know this, so they withdraw their own money more often in lesser amounts – which is now defined as “structuring,” which is also illegal. The former Speaker of the U.S. House of Representatives, Dennis Hastert, has been accused of ‘‘structuring.’’

Along with this, the U.S. and other governments have engaged in “asset forfeiture” which most often means that a government official seizes a private party’s assets on the suspicion that they might be involved in drug dealing, human trafficking, tax evasion or some other crime – even though they have not been convicted of any wrong doing.

Because the government is no longer protecting individual financial liberty but is engaged in a massive effort to destroy it, people of course are looking for ways to protect themselves against the government tyranny.

Suppose for the moment you no longer had to use the government monopoly money cartel nor government-regulated financial institutions to trade goods or services or to make investments. The current government money cartel can only exist if governments share tax and other financial information with each other. Small governments like Switzerland that have sound banking systems and a desirable currency are forced into the information sharing because they need to participate in the international financial clearing system, which, at the bottom line, is controlled by the U.S. Federal Reserve.

Many countries see the advantages of not being under the thumb of the Fed but have been powerless to do much about it.

The Chinese have made it clear that they are working to make their own currency a reserve currency, and the Chinese are big enough to begin to escape international financial reporting rules and the thumb of the Fed. The problem for the Chinese is their financial system is still mainly state-owned and controlled, and not well managed. This gives great pause to anyone who thinks that once the Chinese have sufficient financial power they will not abuse it in the way that European and American governments have.

Which brings us back to bitcoin and its competitors. People want anonymity with both their investments and their transactions. So the global brainpower and imagination is with those who can develop financial and monetary systems that both thwart and are hidden from increasingly oppressive, even democratically elected, governments.

Fortunately, most of the best and brightest do not choose government employment, and those who do tend not to gravitate towards the most oppressive and brain deadening parts like the tax collection agencies.

Government has the problem that it has to get all financial information on everything and everyone, or such information will increasingly flow through the loopholes or imperfections in the system – which always exist. As government currencies become less and less desirable because of the regulatory burdens associated with them and their increasingly structural unsoundness, creative private entrepreneurs will find ways to fill the gap. As more and more transactions and investments activities utilize private, anonymous, digital alternative monies, the government money cartels will be weakened until they are finally fully rejected as were the old communist currencies of Eastern Europe.

The transition is likely to be rough as governments become more and more oppressive to hold on to their dying monopoly – but as history has shown, such oppression is merely an unpleasant death spasm of the old order.

The former communist countries of Eastern Europe were able to recover from the financial collapse relatively quickly because the “black and gray” markets had grown to such an extent that they were able to provide most necessities. The old debts were inflated away, and new low-tax and fiscally responsible regimes quickly took over thus increasing living standards and liberty.

The experiments in private monies and financial regulatory workarounds should be applauded and encouraged, because they will be the safety net when the old tax and financial regulatory order in the U.S., Europe and Japan implodes.

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