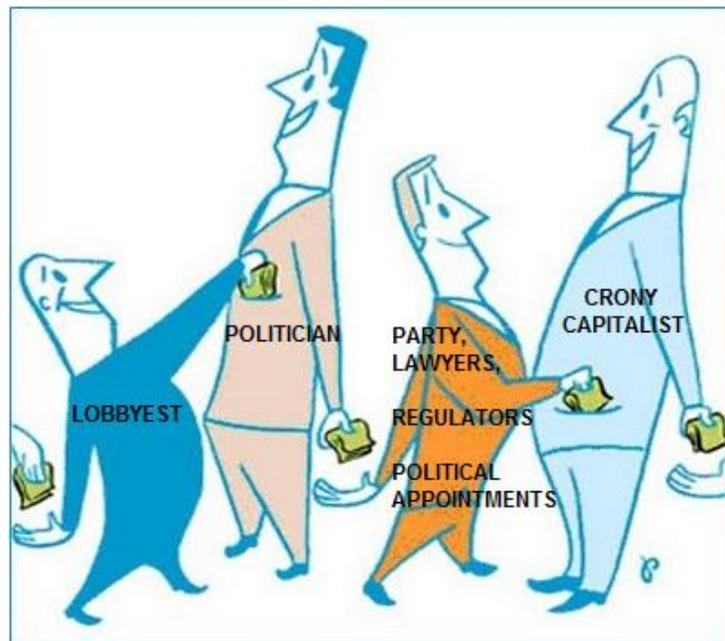


MACRO INSIGHTS

THE CRONY TRIBUTE SYSTEM

Lobbying, Influence Peddling & Campaign Contributions are Soooo Passé

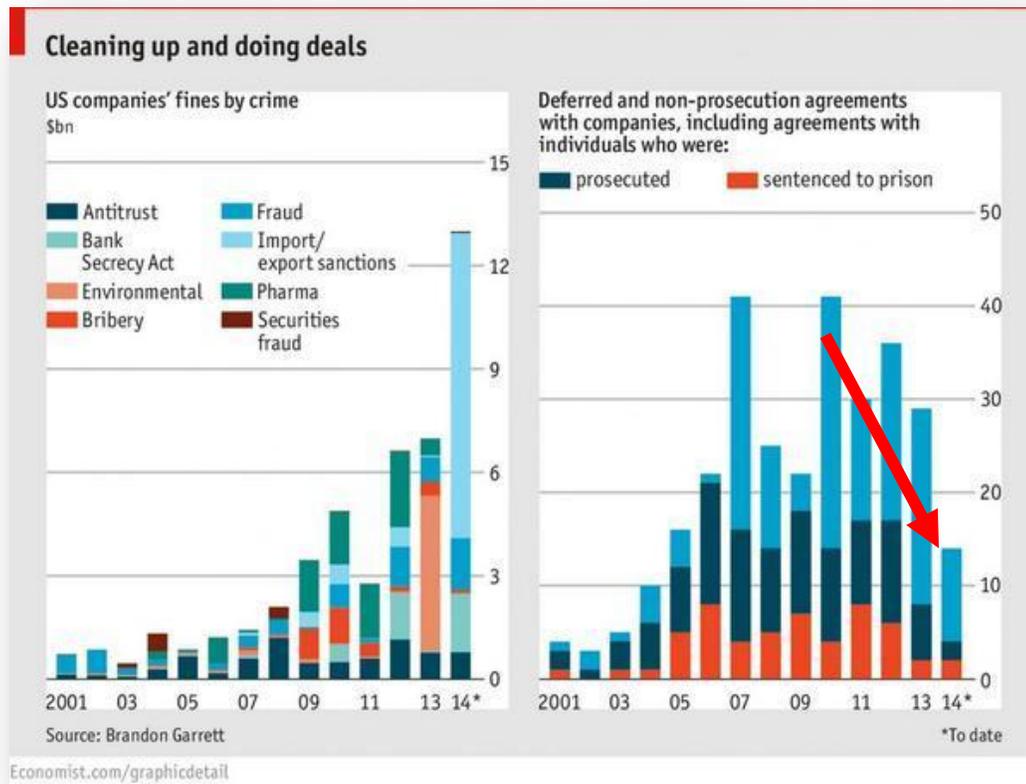


Gordon T Long
11/6/2014

THE CRONY TRIBUTE SYSTEM

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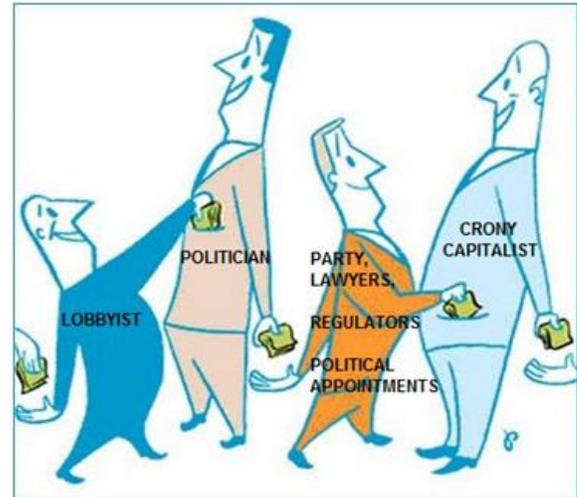


THE CRONY TRIBUTE SYSTEM

Lobbying, Influence Peddling & Campaign Contributions are Sooo Passé!

It isn't so much that they have stopped because in fact they have increased significantly. However, they have diminished in relative importance. Why? Because of the size of money now involved.

As one blatant example, the total settlements on mortgage penalties (at the root of the 2008 Financial Crisis) paid by the banks adds up to about \$106 Billion. About \$32 Billion of that may go to actually help borrowers. However, foreclosure actions totaled \$2.8 TRILLION! Bank penalties were less than 4% of the foreclosure actions. Bank profits on what has been found in court to have been a crime are miniscule in comparison to the size of profits earned!



Maybe even worse, no one went to jail, executive bonuses paid out for these activities were not "clawed back" and no one was even fired! This is because of the new Crony Tribute System.

To understand how the new Crony Tribute System works we need to understand its roots and evolution.

THE ROMAN TRIBUTE SYSTEM



A **tribute** (from [Latin](#) tributum, contribution) is wealth, often *in kind*, that one party gives to another as a sign of respect or, as was often the case in historical contexts, of submission or allegiance. Various ancient states exacted tribute from the rulers of land which the state conquered or otherwise threatened to conquer. In case of [alliances](#), lesser parties may pay tribute to more powerful parties as a sign of allegiance and often in order to finance projects that benefited both parties.

Words like "extortion", "bribery" and 'protection rackets' are unsophisticated applications of the Tribute System. They are heavy handed because power must be shown to exist to bring compliance. When power is understood to be in existence then the "respect" it holds conveys the importance of compliance.

In the Roman era countries and regional rulers paid tributes to Rome to avoid invasion, repressive tax increases, punitive fines, unfavorable laws and all manner of potential scams. By paying a tribute the Roman government would attempt to police this. The tribute was for protection against matters the payer felt they were unable to protect themselves against. Similarly the public merchants would pay tributes to political officials for preferential treatment or to stop themselves from being targeted for repressive regulations.

The Tribute was paid in the form of money or currency so as to continue to operate independently.

MAFIA'S ADOPTION

Why?

The Mafia adopted the Roman Tribute System because it was the only effective way of organizing and controlling members, who by their own personality wouldn't follow rules, conform nor be told what to do.

What is not fully appreciated is the core reason why they had to use this system. There is a scene in the "[Good Fellas](#)" movie that makes this clear.

The Role of the "Don"

The mobster Henry Hill played by Ray Liotta explains that the thing the FBI never understood was why the money flowed up to "Pauli", the Don played by Paul Cicero. It wasn't because they were told to do this.

"The Don was the police for those who couldn't go to the police."

Their power rested in managing an environment that allowed those below them to conduct their business **independently in a free and entrepreneurial fashion**.

It was out of respect. Respect for this power.

It operated on respect and only occasionally was punitive action required. In the mafia the Don couldn't send someone to jail but rather issued a "hit" to resolve any trespasses. An infraction got a life sentence in the truest form.

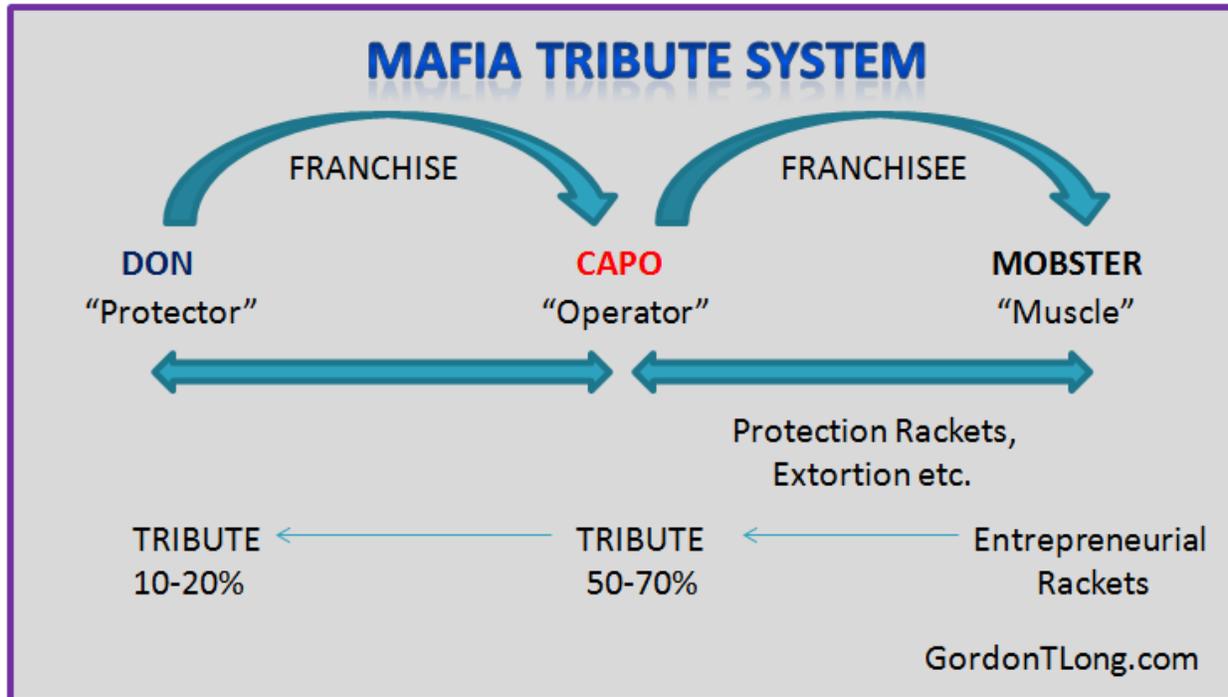
The whole system operated out of 'respect' with **unspoken and undocumented** understandings. There were no contracts or lawyers detailing any rules between members. They were both unnecessary and in fact dangerous for business.

It was their "Cosa Nostra".



Pauli the DON lays down the rules to a young "would-be" mobster

The payment to the Don was 15–20% or higher. It was decided on not by the DON but rather by the level of respect the underling had for the Don. The larger the tribute paid, the more of a “producer” you were and hence you received a higher level of recognition in which to operate. Too low a Tribute showed a lack of respect and the underling subsequently suffered the DON’s retribution so others would be more amenable.



The Tribute was paid in the form of money or currency so as to continue to operate independently.

THE US POLITICAL SYSTEM

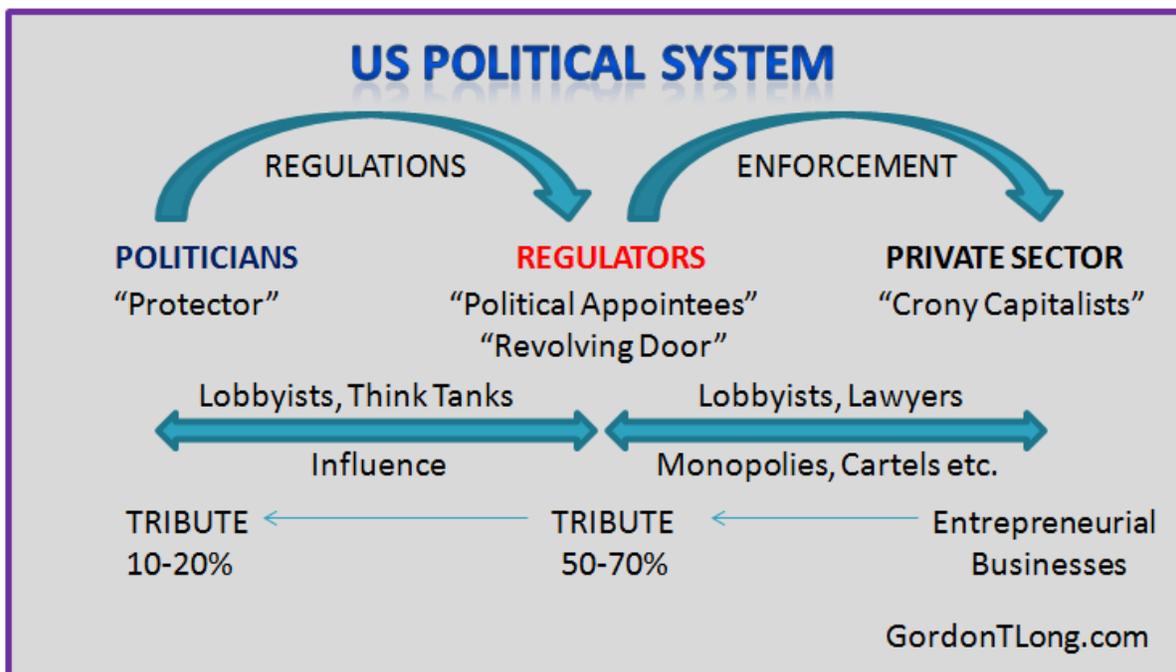
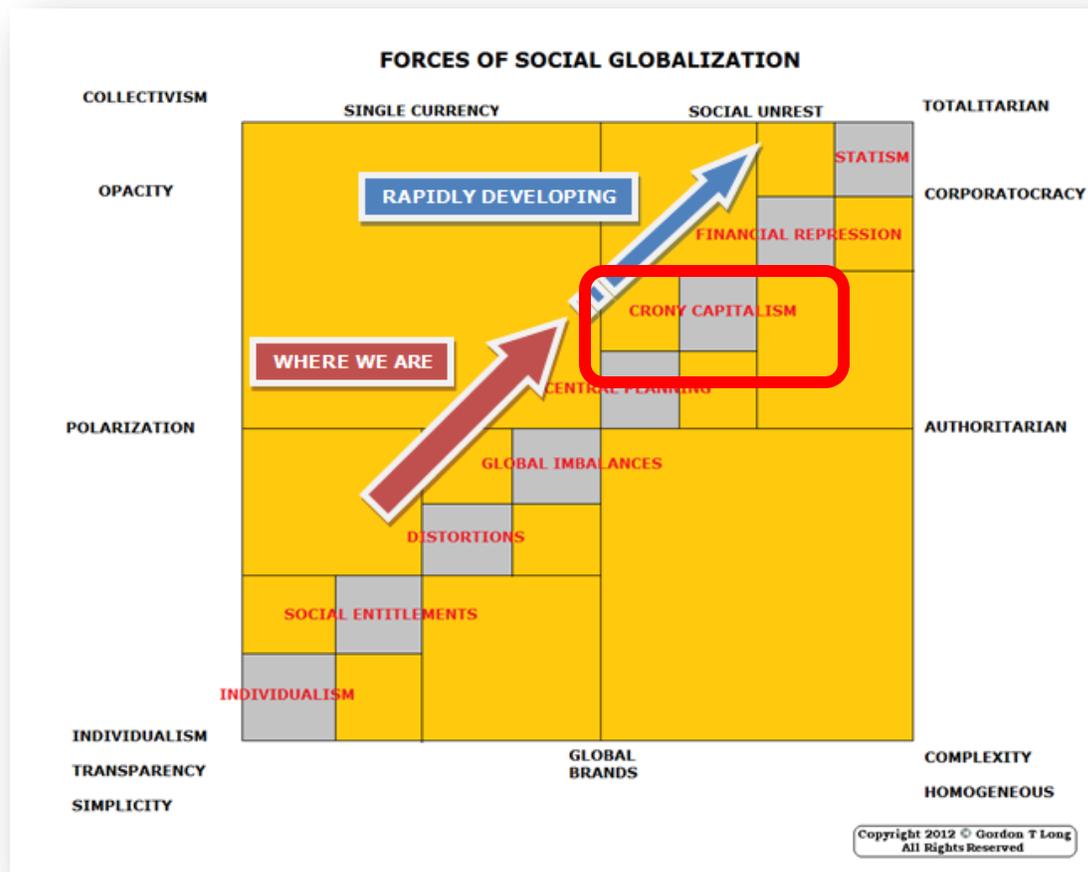
Let's contrast the Roman and Mafia "Tribute" System to the workings of the US Political System.

I have written extensively about the emerging Crony Capitalism in America. Most recently I produced three YouTube video's on the subject which I will refer you to rather than re-visiting this new capitalist mutation that comes with large government and increased central planning and control.

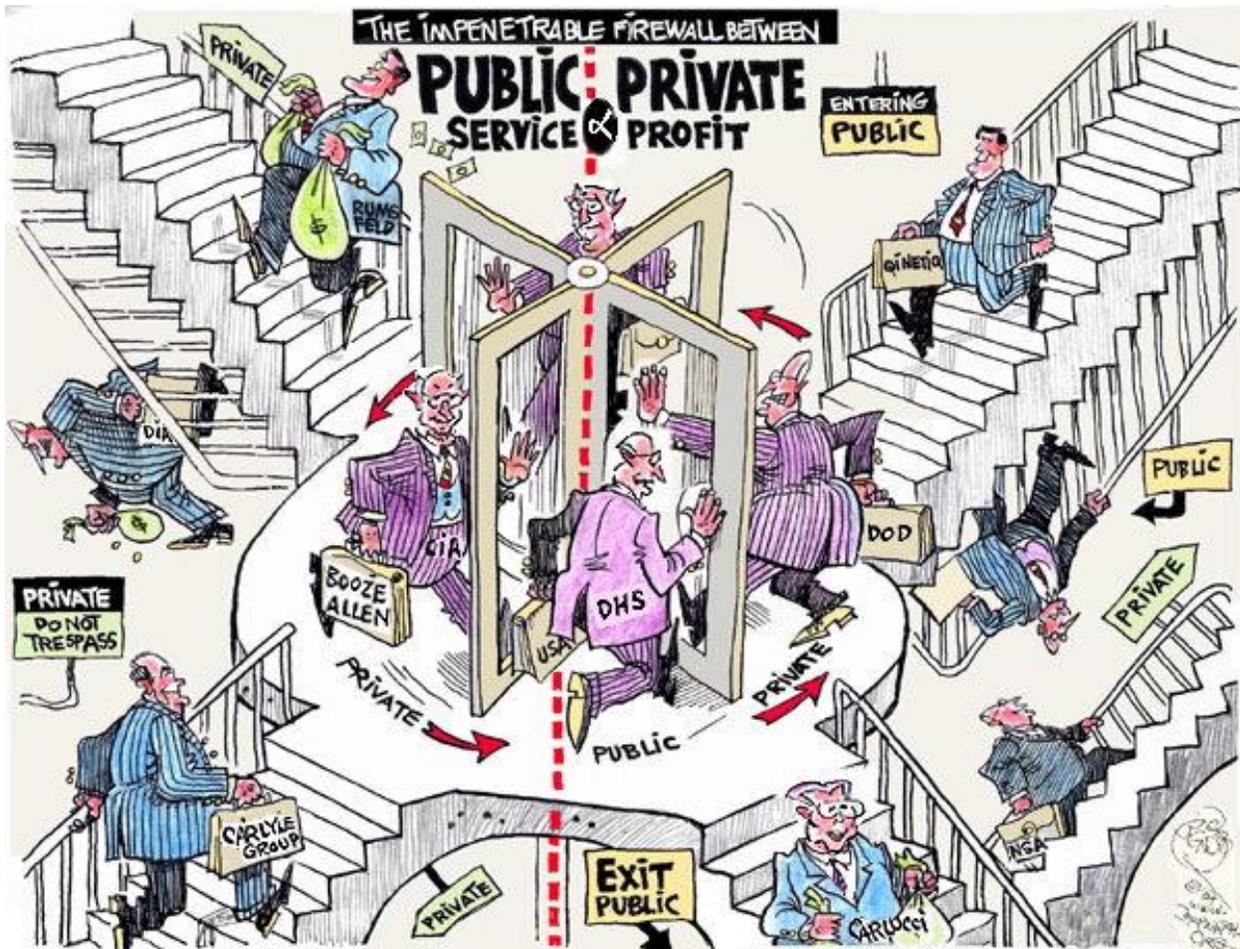
- 10 03 14 - Macro Analytics - [America's Terminal Political Dysfunction](#) - w/ Charles Hugh Smith
- 09 23 14 - Macro Analytics - [Cartels, Monopolies & Crony Capitalism](#) - w/ John Rubino
- 09 06 14 - Macro Analytics - [Why Crony Capitalism is Happening](#) - w/ Charles Hugh Smith

Similar to the MAFIA Tribute System it is mandatory that business dealing not be documented, openly discussed or communicated directly. The unspoken innuendo is paramount.

When this cannot be achieved, then lawyers and "client attorney privilege" must fill the gap. The current television series "[The Good Wife](#)" does a good job on a weekly basis of showing this carefully crafted interaction of lawyers, government enforcement and organized crime. It is a world of grey ruled by the letter of the law which can be argued and not intent, morality, ethics nor character. These characteristic are today secondary to income, profits and the exercise of political power.



Political Appointments & 'Revolving Doors'



In "[Who's Regulating the Regulators](#)", Veronique de Rugby writes:

Many people simply take it for granted that government regulation achieves its intended ends. National political debates often reflect this: Doe-eyed Democrats position themselves as the forthright champions of the little guy, selflessly tying unscrupulous businessmen to the mighty yoke of the regulatory state. On the other side, smooth, corporate Republicans appeal to our inner entrepreneurs, decrying the lost productivity and forgone trickled-down growth that would torture our nation's shackled conglomerates under the proposed new round of regulations.

Whether you're pro-regulation or anti-regulation in America depends more on affiliation than reality. For better or worse, **the truth is more insidious; regulators are often captured by the industry they regulate at the expense of everyone else.**

Even if a regulatory body is initially staffed by upright public servants, there are few (if any) ways to maintain a pure commitment to the agency mission.

John Rubino, my Co-Host on Macro Analytics refers to elected political positions as “extended job interviews”. To support his point [he compiled a list](#) of 418 senators and congressman from the 111th and 112th Congress ALONE that are now paid lobbyists. They are paid to influence laws, regulations and enforcement for those willing to pay. But it is even worse than this seems.

At the Federal level alone a new Presidential administration appoints more than 2000 people to top positions. The president usually receives nominations and suggestions from party officials, political allies, close advisers, academics, and business leaders on whom to appoint to bureaucratic offices. Sometimes the president appoints loyal political allies to key positions, particularly ambassadorships. This tradition is referred to as the ‘spoils system’ or simply patronage. Why would these people give up their careers? What possibly would be their motivations? The sheer numbers suggest there are likely many motivations both good and bad. These positions are Secretary, Under Secretary, Assistant-Under Secretary etc – powerful unelected positions.

Regulators & Enforcement

These same people are either in charge, involved in or appointed to most of the investigations conducted into suspected wrong doing.

Wall Street Insider and bestselling author, Michael Lewis [writes](#) “In an ever-more complex financial system that regulators must have explained to them by the financiers who create it, and the ever-more common practice among regulators of leaving their government jobs for much higher paying jobs at the very banks they were once meant to regulate. Wall Street's regulators are people who are paid by Wall Street to accept Wall Street's explanations of itself, and who have little ability to defend themselves from those explanations. Our financial regulatory system is obviously dysfunctional

... The Fed failed to regulate the banks because it did not encourage its employees to ask questions, to speak their minds or to point out problems. Just the opposite: The Fed encourages its employees to keep their heads down, to obey their managers and to appease the banks. That is, bank regulators



failed to do their jobs properly not because they lacked the tools but because they were discouraged from using them."

Capture & Collusion

Bloomberg's Megan McArdle in "[It's Normal for Regulators to Get Captured](#)" lays out that "regulatory capture" is normal - this is the process by which regulators who are put in place to tame the "wild beasts of business" instead become tools of the corporations they are trying to regulate, "especially large incumbents". She lists several reasons:

1. The regulated industry controls the information used by the regulator. Where do you get information about the banking business? From bankers.
2. The regulated industry cares more about regulations than anyone else. Regulatory bodies, like other organisms, shy away from negative stimuli.
3. The only place where a longtime regulator can get a new job is in the regulated industry. Everyone laments the revolving door.
4. It's hard to stay confrontational all the time. Regulators are people, too, and people are social animals. They want to be liked.
5. Lobbying.
6. Making a regulator's job easier. What's easier to regulate -- a few staid old incumbents that you know well or a zillion upstarts who don't know the rules, don't have a highly competent and extensive staff of compliance officers to deal with the regulators, keep changing what they do, forcing you to figure out what that means and come up with whole new sets of rules to cover the evolving marketplace and ... I don't really need to ask this question, do I? Over time, the interests of regulators and the interests of incumbents tend to converge upon keeping things nice and tidy by making sure that experienced players dominate the field.

The [secret Fed tapes](#) that were released by "[This American Life](#)" give hard details to this from whistleblower Carmen Segarra.



Taped Conversations Between Carmen Segarra & Goldman Sachs

REGULATORY CAPTURE & COLLUSION

47.5 Hours of Taped Proof the Financial Regulators are No Longer Regulating

The Wolves now guard the hen house - *The full ProPublica story [can be found here](#).*

Sad Tale of the New York Fed and Goldman Sachs Has a Simple Solution 09-27-14 **TheDailyBell** Corporate largeness inevitably generates government partnerships. This means that modern Western societies are mercantilist - run by a handful of individuals who circulate between the top posts of government and the leadership of private-sector multinationals. Within this context it is not surprising to find that the New York Fed is an ineffective regulator of the financial powerhouse Goldman Sachs. The process is called "regulatory capture".

1. Monopoly central banking concentrates decisions on the value and volume of money in the hands of a few.
2. Corporate personhood allows individuals running large companies to avoid responsibility for their actions.
3. I suppose I should add a third element into the mix ... patent law and copyright

The Secret Goldman Sachs Tapes 09-26-14 Michael Lewis Bloomberg

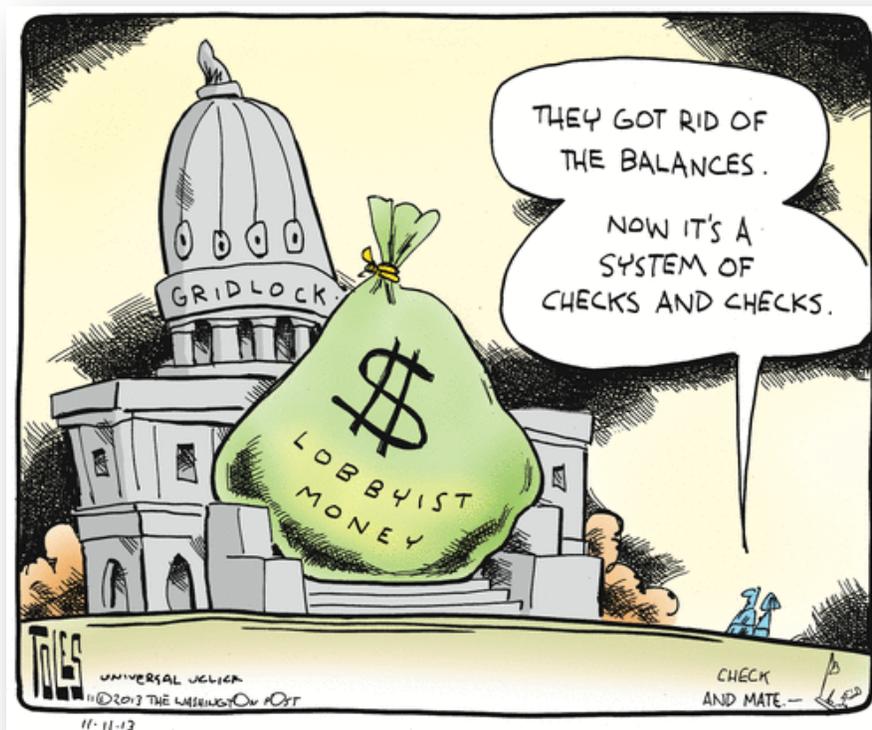
And for those who are time-constrained, and would rather just read the Cliff Notes (the ending should be known to everyone by now), here is Michael Lewis with an op-ed in [Bloomberg summarizing the banker-controlled farce the entire US system has devolved to](#): "The Secret Goldman Sachs Tapes"

Controlling the Rules of the Game

Judges are political appointees in the US legal system. They are normally selected by the party because of political bias. This has reached the level that for example most recently the Supreme Court [struck down limits on Federal Campaign contributions](#). Anyone currently watching the election campaigning for the upcoming November election can clearly see the affect of this in the volume and aggressiveness of media advertising by both politicians and political action committees. It is not only appalling but clearly shows that the Crony Capitalists have been given the green light to fully take over the US political system.

The ruling "may represent the latest step in an effort by a majority of the court to dismantle entirely the long-standing structure of campaign finance law erected to limit the undue influence of special interests on American politics," said Sen. John McCain (R-Ariz.), who sponsored the 2002 Bipartisan Campaign Finance Reform Act with then-Sen. Russell Feingold (D-Wis.).

The checks and balances in the US political system – whether the Legislative, Executive or Judicial have all been co-opted.



NO ONE GOES TO JAIL

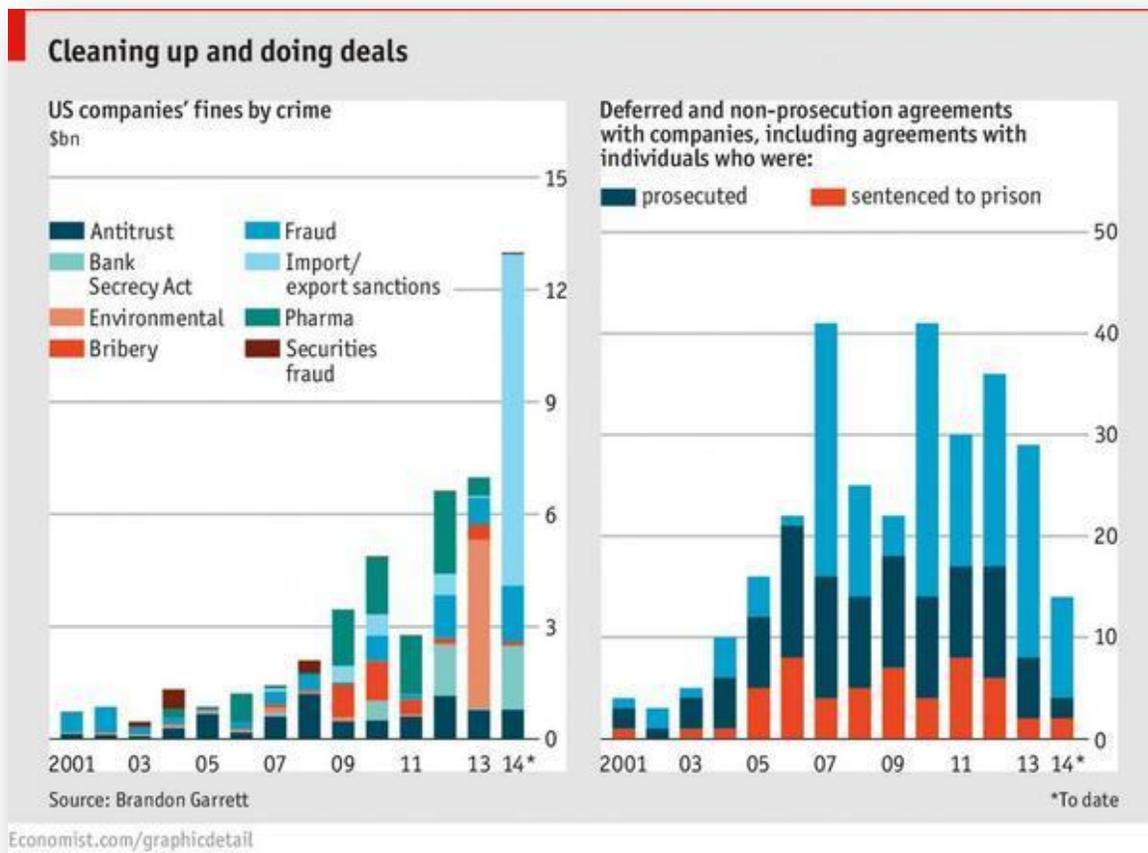
Everything we have discussed to this point is fundamentally about the ingredients that have allowed the new Crony Tribute System to flower.

Without these changes the perception of business leaders would not have changed to where today, breaking the law is a matter of making a business decision. What are the rewards and what are the risks?

When the PERSONAL risks and penalties are low then it is only a matter of dollar and cents.

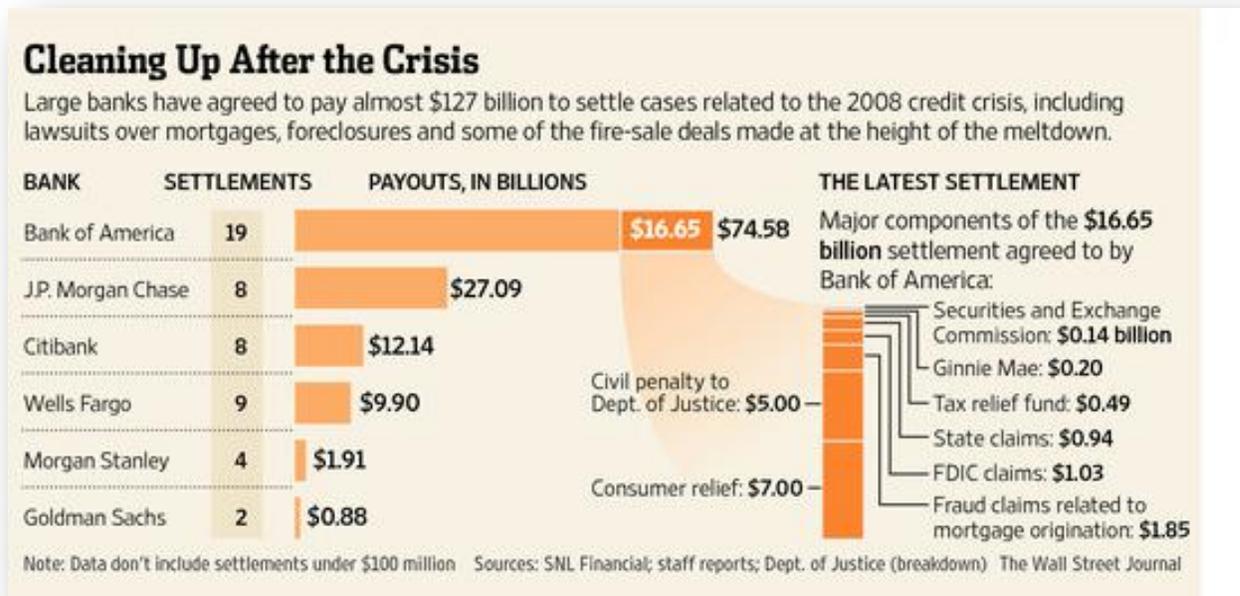
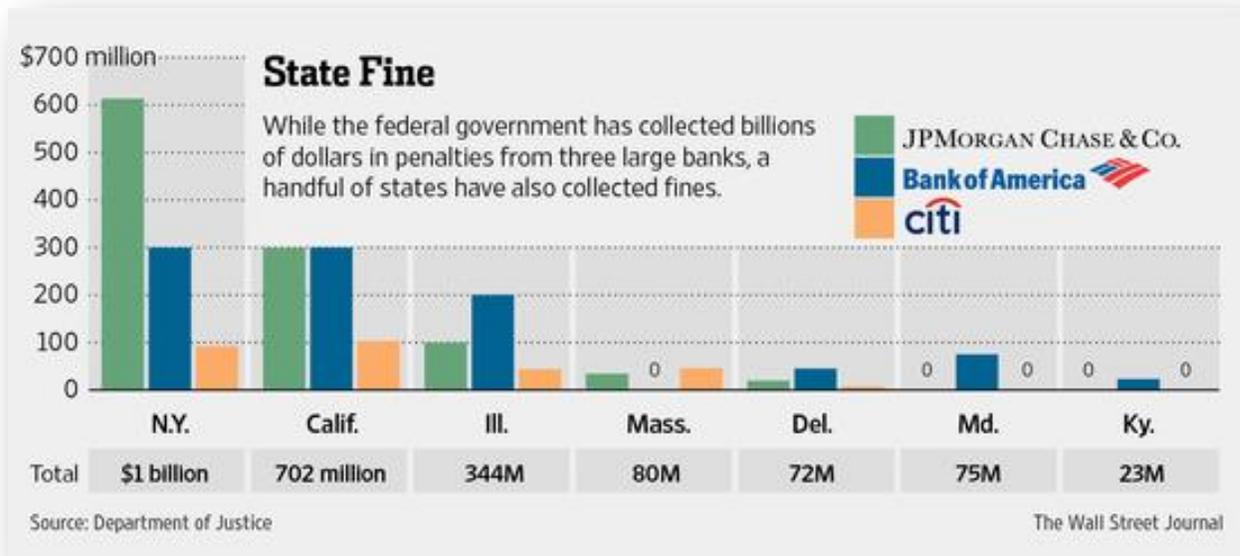
New Cost of Doing Business

The charts below illustrate the change that has occurred in America. White collar crimes are no longer punished by prison sentences but rather with fines and penalties which enrich the coffers of the government but do little to stop or change the behavior.

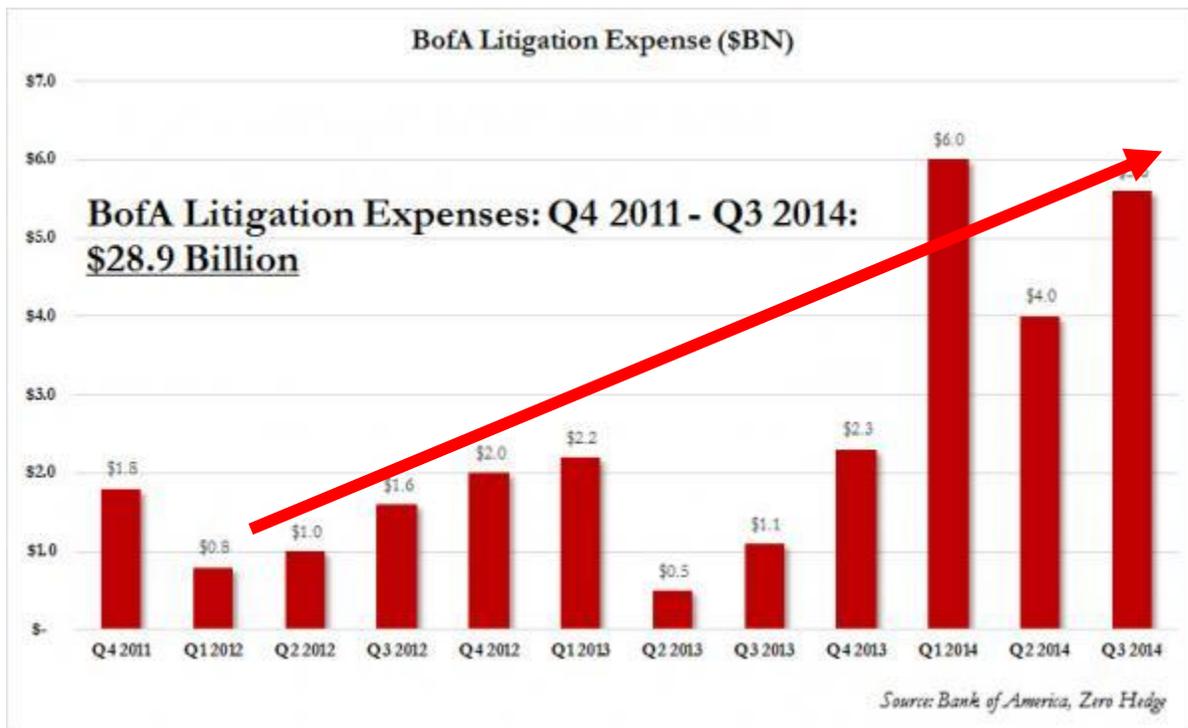


Why doesn't it change behavior? If the crime makes \$1B and you pay a fine of \$100B (10%) and no one goes to jail, why would you stop? It quickly becomes simply the cost of doing business.

The Government is now acting in a similar manner to a Mafia Don, allowing crimes to occur and then being paid in the form of a fine or penalty as a tribute for previously allowing business crimes to be conducted which were subsequently found to be illegal by those laws the Crony Capitalists were unable to have changed or to have influenced the actual enforcement actions.



In a recent research article: [For Bank Of America, Crime Is Now An Ordinary Course Of Business](#) the facts are clear that the direction is accelerating:



"Between Q4 2011 and Q3 2014 Bank of America produced "Net Income" of \$15.9 billion. However, the amount of added back "one-time, non-recurring" legal expenses is a stunning \$28.9 billion: **two of every three dollars, non-GAAP as they may be, comes from Bank of America engaging in criminal activity... and that's just the stuff it got caught for.**

So perhaps an even more relevant question than how long will the EPS "add back" bullshit continue, is how long will the regulators and enforcers allow Bank of America to exist as an organization for which two-thirds of its "ordinary course business" is, for lack of a better word, crime?"

Clearly Bank of America sees increased legal costs as being part of the business expense to achieve higher profits.

What we have here is one and the same as in the Roman and Mafia Tribute Systems.

The Tribute was paid in the form of money or currency so as to continue to operate independently.

Rackets: Rico Act versus Control Fraud

For years the FBI was supposedly unable to stop organized crime because it had no firm grounds for indictment. The advent of the use of the Rico Act changed all that. Today [according to law professor William K Black](#) the concept of "[control fraud](#)" is used in which a business or national executive uses the entity he or she controls as a "weapon" to commit fraud. Black was a central figure in exposing Congressional corruption during the [Savings and Loan Crisis](#). He took the notes during the [Keating Five](#) meeting that were later published in the press, and brought the event to national attention and a congressional investigation. Black is the author of, among others, *The Best Way to Rob a Bank is to Own One: How Corporate Executives and Politicians Looted the S&L Industry*. He testified before congress on Lehman Bros but no actions were taken once the media frenzy died down.

CONCLUSIONS

The 10-20% Tribute Level

It really isn't surprising that the growing fines are reaching the Tribute levels of 10-20% while incarceration shrinks. Cynically you could argue that a bankrupt government doesn't want to kill the only golden goose laying eggs. But this isn't the case. It is a matter of a changing culture and other pressures.

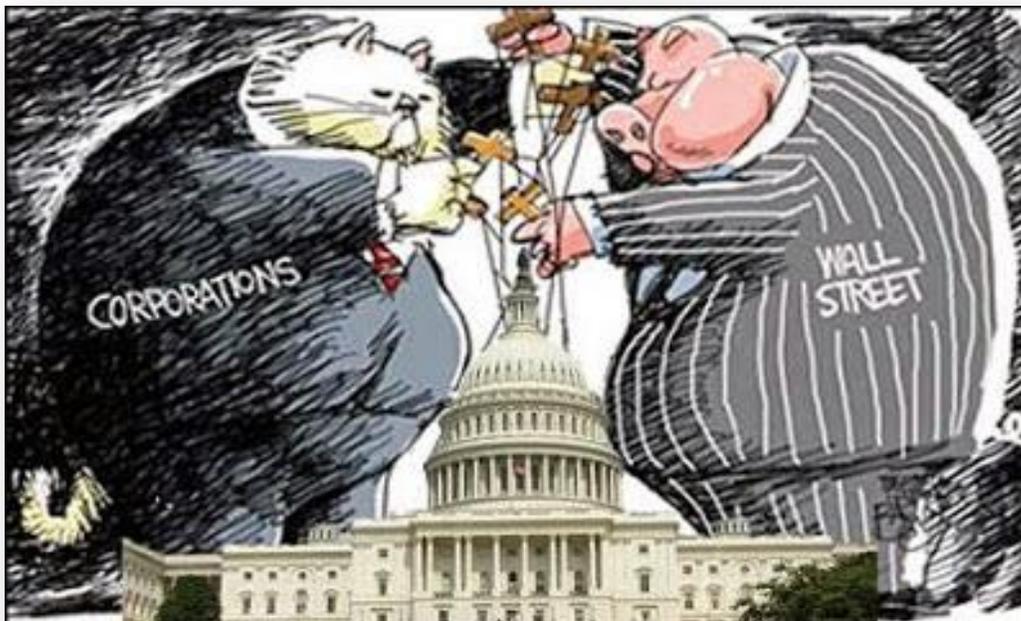
Cheaper than Capital Investment Risk

Corporations can no longer achieve 'top line' growth with aggregate demand shrinking and real disposable incomes being compressed. Bottom-Line growth is temporarily being achieved through financial engineering, stock buybacks and 'gearing' through off balance sheet contingent debt. However these approaches are reaching their limit.

Corporations are now being forced to increase margins not just through outsourcing, downsizing, right sizing, retirement & healthcare benefits removal and endless other costs savings methods, but to move towards market share capture. Margins improvements track very closely to market share improvements. The game is market share through any method that will deliver this. This was made obvious to the world recently when the world's largest brand manager, Proctor and Gamble, announced it would be dropping over 100 of its established brands. Few seem to have picked up on this dramatic development.

When the government becomes a larger piece of the economy it not only becomes a more important customer but the use of regulatory arbitrage and the influencing of regulations to gain a competitive advantage become the new competitive advantage for CEO's. Not to play the game aggressively will quickly cast you to the pile of the "has-been" corporations.

Today it is much less risky to play this game than to make major capital investments that may fail, be obsolete quickly, be uncompetitive etc.



My Co-Host Charles Hugh Smith [summarizes the fall-out](#) from the growing Crony Capitalism:

Everybody in the inner circle wins: the finance perps collect their millions in bonuses, the legislators collect their millions in campaign contributions, and the regulators (who managed to do nothing in the way of prevention) get to declare a toothless victory in announcing wrist-slap fines.

This cozy arrangement might seem benign, but it's actually deadly to democracy and the real economy. Let's call *crony capitalism* what it really is: Kryptonite to democracy and the real economy.

Concentrated wealth and State power form a self-reinforcing feedback loop that destroys democracy. The more profitable buying influence and the revolving door between corporations and regulators becomes, the more money the corporations have to spend on lobbying, which serves to further protect their profits. The more money political toadies collect, the more beholden they are to entrenched interests.

This feedback loop rewards crony capitalism and limits classical capitalism's key features: transparent markets and competition. An economy dominated by crony capitalism stagnates as competition is suppressed and government enriches those who are "more equal than others" (to borrow a phrase from Orwell).

Money that might have once been invested in research and development is now devoted to bribing politicians, lawsuits defending corporate turf and wrist-slap fines/Tribute to the State that enables and protects crony skimming operations.

When the machinery of governance is ruled by the highest bidders, democracy is dead.

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