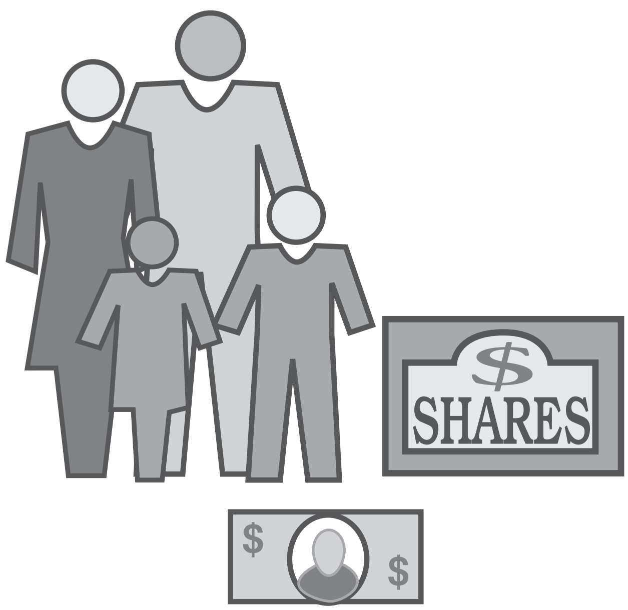
# THE CAPITAL HOMESTEAD ACT:
## NATIONAL INFRASTRUCTURAL REFORMS TO MAKE EVERY CITIZEN A SHAREHOLDER




by Norman G. Kurland

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# THE CAPITAL HOMESTEAD ACT:

## National Infrastructural Reforms To Make Every Citizen A Shareholder

*[Updated August 1999 from a paper prepared by Norman G. Kurland, President of the Center for Economic and Social Justice, at the request of the Chief Economist of the National Security Council, May 10, 1982.]*

### A New Vision for America's Future

In a July 1974 speech to the Young Americans for Freedom, then-Governor Ronald Reagan called for one of the most revolutionary policy reforms in the past century:

> "Over one hundred years ago, Abraham Lincoln signed the Homestead Act. There was a wide distribution of land and they didn't confiscate anyone's already owned land. They did not take from those who owned and give to others who did not own. ***We need an Industrial Homestead Act. . . .***"
>
> "[I]t is time to accelerate economic growth and production and at the same time broaden the ownership of productive capital. The American dream has always been to have a piece of the action."

In his February 1975 radio broadcast, Mr. Reagan hinted at the global implications of such an expanded ownership strategy when he commented:

> "Could there be a better answer to . . . Karl Marx than millions of workers individually sharing in the ownership of the means of production?"

Since 1973, Congress has passed over 20 laws encouraging employee stock ownership plans (ESOPs) and over 10,000 companies are gradually spreading equity ownership among their more than 10 million workers. In 1976 the Joint Economic Committee of Congress declared broadened ownership of new capital as a major new economic policy.[1]

Political support for the ESOP has come from both parties and from all across the ideological spectrum. The first champion of the ESOP was former Sen. Russell Long, for many years the powerful chairman of the Senate Finance Committee. Others who

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[1] For an understanding of the moral philosophy, compelling systems logic, and principles underlying this goal, the reader should turn to the many books and writings of Louis O. Kelso, father of the ESOP and binary economics, and the publications of the Center for Economic and Social Justice, especially *Curing World Poverty: The New Role of Property,* John H. Miller, ed., Social Justice Review: St. Louis, 1994. See also *Binary Economics: The New Paradigm* by Robert Ashford and Rodney Shakespeare, University Press of America: Lanham, Maryland, 1999.

have spoken out in favor of the ESOP concept include such diverse personalities as President Ronald Reagan, Senators Richard Lugar and Christopher Dodd, former Senators Gary Hart, Paul Fannin and Paul Laxalt, Representatives Benny Thompson, Charles Rangel, Phil Crane, and Dana Rohrabacher, and former Representatives Bill Frenzel, Jack Kemp, Mike Espy, Michael Barnes, and Parren Mitchell. President Clinton reportedly expressed his support for the ESOP at a cabinet meeting. While some academics and labor spokesmen have voiced skepticism, citing a few cases where ESOPs were abused, even this resistance is diminishing.

If expanded capital ownership is an idea whose time has finally arrived, what's holding it back?

One answer is, it still lacks a comprehensive strategy to lift remaining institutional barriers to free enterprise growth. Such impediments have been erected over the last century because we neglected to link private sector growth with a more just distribution of future ownership opportunities. This is especially true in our capital credit policies.

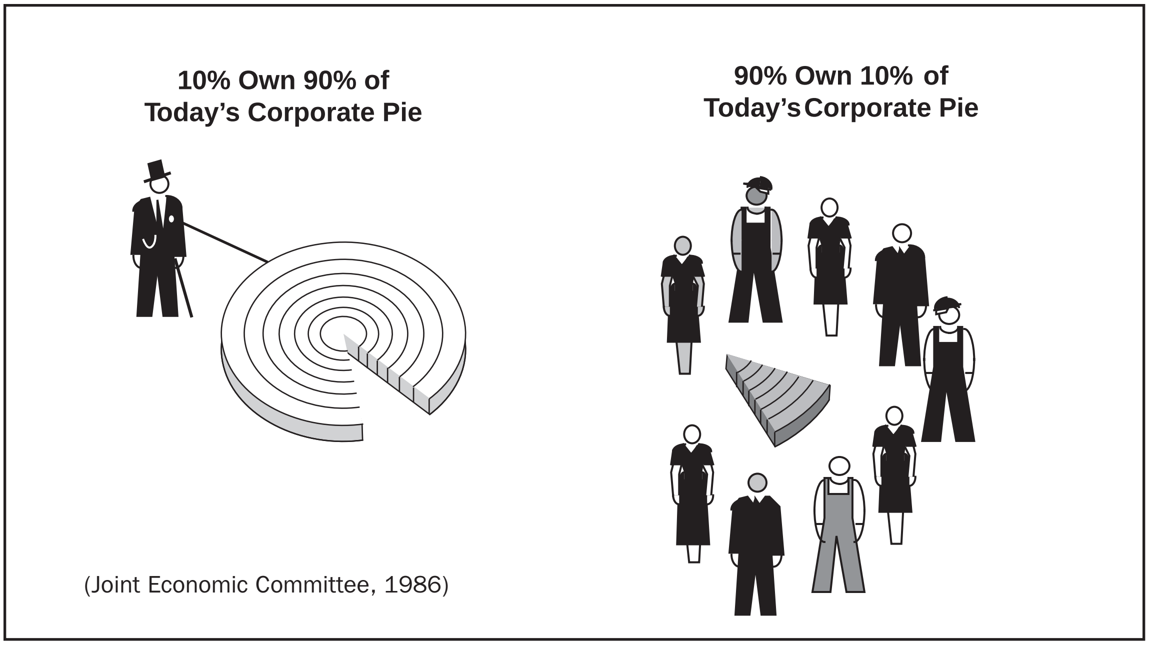
The second answer is that when our economic decision-makers reform our laws to encourage supply-side growth, they fail, unfortunately, to encourage a direct linkage between new incentives for that growth and expanded ownership and profit sharing opportunities.

This is why the $450 billion in tax incentives for new plant and equipment in the Economic Recovery Act of 1981 were labeled a "trickle-down" version of supply-side economics. And this explains today's widening gap between rich and non-rich Americans and the rising anxiety about the downsizing of America. Had the direct beneficiaries of those tax incentives been the workers, President Reagan's business tax reforms would have enjoyed a much broader base of voter support.

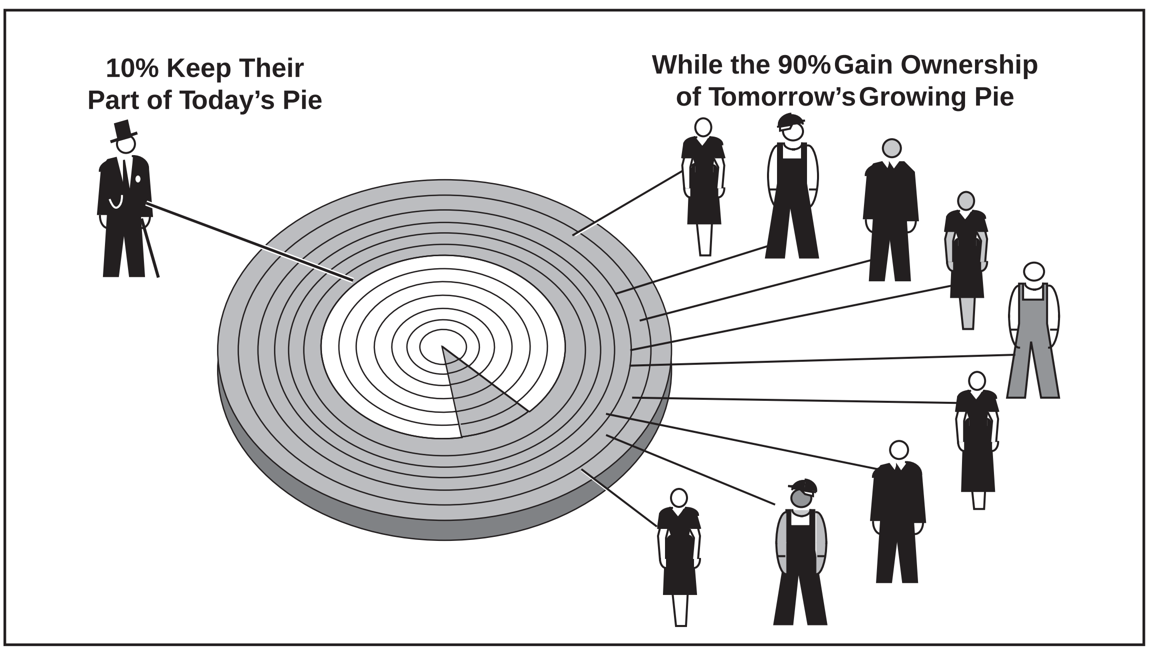
If we are to rebuild the free enterprise system—from the ground up—we must insure that more and more citizens have a viable private property stake in the virtually limitless technological frontier. It is clear, we need a Space Age counterpart to Lincoln's sweeping Homestead Act—a ***Capital*** Homestead Act[2].

[2] In 1995, after many years of discussion over the best name for this sweeping economic program, it was decided that the word "capital" best described the new form of productive "homestead," while shedding the smokestack connotations of the word "industrial." "Capital" also signifies the chosen site of the first prototype application for a Capital Homestead Initiative—a Super Empowerment Zone in the Nation's Capital of the U.S.A.

## WHO OWNS TODAY?




## WHO WILL OWN TOMORROW?



## I. AN OVERVIEW

The basic interdependent components of the Capital Homestead strategy are like the legs of a three-legged stool:

(1) **Democratization of productive credit,** by reforming monetary policy to conform to the goal of sustainable, market-oriented, non-inflationary growth. The new policies would aim at an immediate reduction in prime interest rates to 3% (without subsidies) for private-sector investment, through a two-tiered base for interest rate policy. Central banks would:

(a) Be restrained from further monetization of deficits or encouraging other forms of non-productive uses of credit (i.e., demand-side credit), which would then be forced to seek out already accumulated savings at market interest rates; and

(b) Use the Fed discount mechanism exclusively for discounting, at low discount charges but subject to a 100% reserve requirement, "eligible" industrial, agricultural and commercial paper financed through its member commercial banks. This reform would synchronize the supply of real money with real growth of the economy. It would provide an asset-backed currency reflected in more efficient instruments of production and keep basic economic decisions in local hands.

(2) **Simplification of tax systems,** centered around taxing incomes from all sources at a single rate (offering a universal yardstick for political hopefuls to compete against), as a direct means for:

(a) Balancing national budgets and restraining overall spending, including social security programs;

(b) Ending the use of the tax system to circumvent the appropriations process; and

(c) Eliminating double taxation of profits in ways that maximize greater savings and investments in new plant and equipment, plus removing other features that discourage expanded capital ownership.

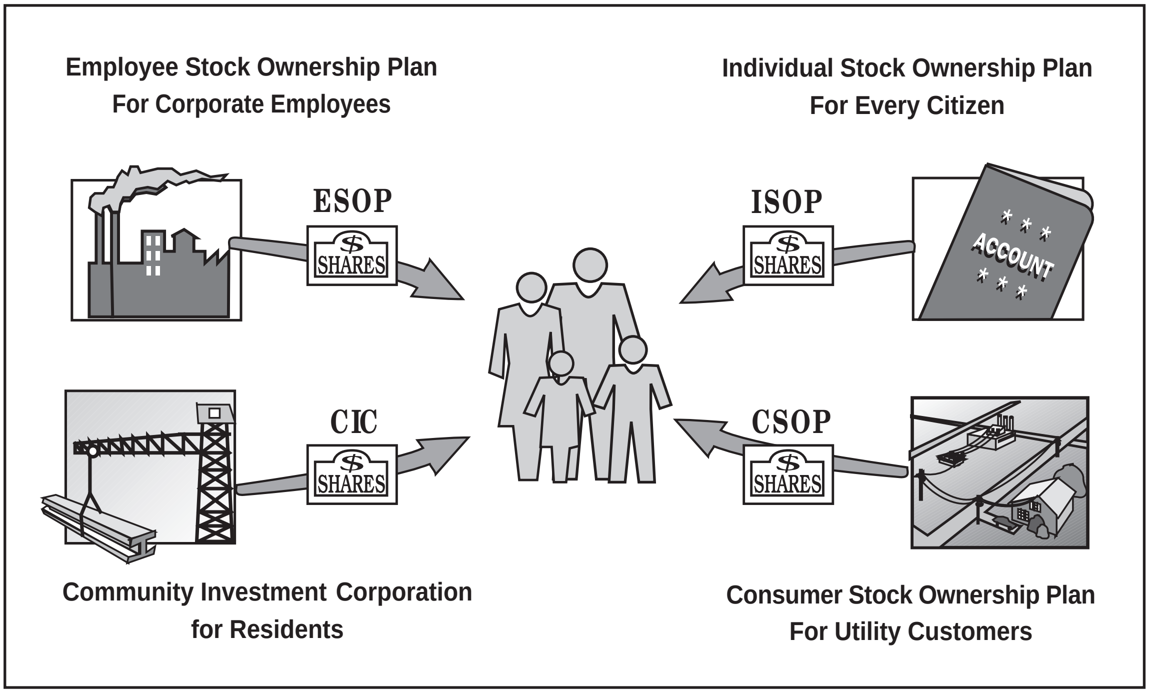
(3) **Linkage between all tax and monetary reforms to the goal of expanded capital ownership.** This would encourage all citizens to share directly in the equity growth and profits from our ever-expanding high-technology frontier and to insure the broadest possible base of direct beneficiaries (and thus political supporters) of all future tax and monetary reforms.

In contrast to social security, this strategy would create for every voter a "Capital Homestead Exemption" for accumulating over his or her working lifetime a personal estate that would be exempt from income, capital gains, gift, estate and other taxes, a modern equivalent of the 160 acres of land that government made accessible to American pioneers.

Citizens would accumulate their Capital Homestead shares in many ways, including such "credit democratization" vehicles as: Employee Stock Ownership Plans

(ESOPs); Consumer Stock Ownership Plans (CSOPs); Individual Stock Ownership Plans (ISOPs); and Community Investment Corporations (CICs). These high-powered financing vehicles would link the new monetary and tax incentives for productivity growth under the Capital Homestead Act, with an ever-expanding base of citizen-shareholders.

CAPITAL HOMESTEADING—4 VEHICLES




## II: DESIGN PRINCIPLES AND GUIDELINES

To shift the Federal Government's role from today's income redistribution policies to the more limited and healthier role of encouraging "economic justice" through free enterprise growth, a Capital Homestead Act should begin establishing:

**Positive Policies for Private Sector Growth.** Re-create the conditions that resulted from the first Homestead Act of 1862: Full employment, declining prices--and a broad distribution of property ownership.

**National Ownership Goals and Targets.** Set a realistic long-term target, based on the nation's industrial growth potential, to achieve a minimum Capital Homestead Stake for every American family, perhaps $100,000 over the next 20 years.

**Saving the Social Security System.** Keep existing promises and reduce the growing burden on the Social Security System, by enabling every American to accumulate (through inheritances, gifts, ESOPs, IRAs, community investment corporations and other expanded ownership vehicles sheltered from taxes under the "Capital Homestead Exemption") sufficient wealth-producing assets to provide each person with an adequate and secure taxable income from property, independent of Social Security benefits and incomes from other sources.

**Capital Homestead Exemption.** Establish a personal "Capital Homestead Exemption" (perhaps $500,000 per individual), thus providing every American an opportunity to accumulate over his or her working lifetime an income-producing, space-age equivalent of the 160 acres of land offered to landless Americans under the original Homestead programs, free from capital gains, inheritance, and gift taxes.

**Planning for Maximum Growth, with a Balanced Budget and Zero Inflation Rate.** Implement a peace-time counterpart of World War II's War Industrialization Board to bring together America's finest minds and prime movers to recommend ways to unharness maximum rates of sustainable private sector growth to achieve a balanced Federal budget and a zero inflation rate under the Capital Homestead Act, including reasonable national ownership targets and priorities.

**Anti-Monopoly Reforms.** Link all economic reforms to methods that discourage privileged access to or monopolistic accumulations of private property ownership of the means of production. Enforce anti-trust laws by providing access to capital credit to broadly owned new competitors to enhance and sustain market-oriented growth.

**Democratization of Federal Reserve Credit.** Reform Federal Reserve monetary policy (especially by reactivating the Fed's power to discount "eligible" commercial, industrial, and agricultural paper) to bring about a two-tiered, non-subsidized interest rate structure within member banks of the Fed. This reform would encourage more widespread individual access to lower-cost bank credit for ownership-expanding private-sector productivity growth, while allowing savers to receive market interest rates for non-productive or ownership-concentrating uses of credit, including government deficits.

**Liquidity for Local Banks.** Require the Fed to supply sufficient money and credit through local banks to meet the liquidity and broadened ownership needs of an expanding economy. Such "Fed facilitated" loans would be subject to appropriate feasibility standards administered by the banks and limited only by the goal of maintaining a stable value for the dollar.

**Capital Credit Insurance to Overcome the Collateralization Barrier of the Non-Rich.** Promote the availability of private sector capital credit insurance as a substitute for collateral to cover the risk of default on "eligible" Capital Homesteading loans for expanding share ownership among workers and other capital-deficient citizens, similar to the role played by home mortgage insurance for broadening home ownership in America.

**Stabilized Value of Currency**. Create a stable currency backed by productive private sector assets rather than non-productive public sector debt. Terminate use of the Fed's money-creating powers to support foreign currencies or to buy and sell Treasury securities, thus forcing governments to borrow directly from savers in the open markets.

**A Tax System More Accountable to Taxpayers.** Radically simplify the existing Federal tax system in ways that automatically balance the budget and make Congress more directly accountable and responsive to all taxpayers.

**Removal of Tax Obstacles to Broadened Ownership**. Eliminate tax provisions that unjustly discriminate against or discourage property accumulations and investment incomes, especially for poor and non-rich families.

**Pro-Competition Policies.** Remove economic bottlenecks to effective market competition so that just prices, just wages and just profits can be controlled by the laws of supply and demand, rather than by central planners, by fiat or regulation, by government-sanctioned monopolies, or by other coercive pressures.

**A Market-Driven Wage and Price System.** Gradually eliminate rigid, artificially-protected wage and price levels and other restrictions on free trade, which afford special privileges to some industries, businesses and workers at the expense of American and foreign customers of U.S. products. Selectively target duties on foreign products produced in violation of just market principles.

**More Just Social Contract for Workers.** Focus top priority during the next decade on developing a more just "social contract" for persons employed in the private sector, geared to maximum ownership incentives, so that instead of inflationary "wage system" increases, all employees can begin to earn their future gains increasingly through production bonuses, equity accumulations, and profit earnings linked to their personal efforts and to the productivity and success of their work team and the enterprise for which they work.

**Restoration of Property Rights in Corporate Equity.** Restore the original rights of "private property" to all owners of corporate equity, particularly with respect to the right to profits and in the sharing of control over corporate policies, while still safeguarding the traditional functions of professional managers.

**More Harmonious Industrial Relations.** Promote the right of non-management employees to form democratic trade unions and other voluntary associations for negotiating and advancing their economic interests, including their ownership rights, vis-à-vis management.

**Expanding Equity Opportunities for Farm Families.** Preserve farm families as the basic unit for maintaining self-sufficiency in meeting America's food supply, while discouraging the spread of ownership-concentrating conglomerate and foreign takeovers of prime agricultural lands. Equity sharing among dozens of farm families working together in large corporate agribusinesses would update the "family farm" concept.

**Phasing-out of Agricultural Subsidies.** Assist farmers who wish to associate together voluntarily in cooperatives and in enterprises jointly owned by farmers and workers, including integrated agribusinesses, for supplementing their farm incomes and reducing the need for subsidies.

**Incentives for Research and Development.** Encourage special ownership incentives for those engaged in research and development, especially in the search for new sources of energy and labor-saving technology.

**Conservation of Resources.** Develop new methods of conserving and re-cycling non-replenishable and limited natural resources that are vital to society's long-term survival, until suitable substitutes can be discovered and developed.

**Property Incomes for Public Servants.** Provide America's military, policemen and firemen, teachers, and other public employees with a growing and more direct equity stake in the free enterprise system, both as a supplement to their costly pension plans and so that they will better understand and defend the institution of private property.

**Downsizing of the Public Sector.** "People-ize" government-owned enterprises and services into competitive private sector companies, whenever feasible, by offering their employees (and customers in capital-intensive operations like TVA) opportunities to take over their ownership and control.

**Prototype Policy Reforms for Local and Foreign Governments.** Encourage State and local governments and other countries to promote widespread capital ownership as a basic pillar for building a sound market economy.

**Localized Free Enterprise Zones.** Launch several Capital Homesteading demonstrations, possibly in areas of high unemployment (like the Super Empowerment Zone proposed in 1996 for the District of Columbia) to evaluate ownership-broadening Federal Reserve reforms, innovative broadened ownership mechanisms and advanced concepts of worker participation in decision-making and self-management.

**Land and Natural Resources Owned by the People, Not Government.** Anything that can be owned by government, especially income-producing land and natural resources, can be and should be owned and controlled locally, broadly, and equitably by individual citizens and their families, not by government, or by a few owners, land speculators, or corporations with few or no local share owners.

**New Challenges for Multinationals.** Provide special encouragement to U.S.-based multinational corporations to become instruments of peace and a more just world economic order, by broadening access to their ownership base to all citizens of the world community, especially for exploiting the resources of the sea and other planets.

## III. BASIC VEHICLES FOR IMPLEMENTATION

Ownership is largely determined by access to capital credit. Just as society can structure its laws and institutions to concentrate ownership, society can reform its laws and institutions to decentralize ownership. Similarly, future corporate credit can be used to build more ownership into the same tiny group of present shareholders. Or access to corporate credit can become democratized to create new owners.

### The Employee Stock Ownership Plan

One powerful ownership-expanding technique, known as the Employee Stock Ownership Plan (ESOP) provides widespread access to capital credit to each employee in a company on a systematic basis. Technically, the ESOP uses a legal trust that is "qualified" under specific U.S. tax laws encouraging employee ownership.

Thus, while it is closely policed by the Internal Revenue Service and the Department of Labor to insure that the ownership plan operates in ways beneficial to employee-owners, the ESOP provides special tax privileges and incentives for the company, existing owners, and the employees.

Fortunately, the laws are extremely flexible, so that each plan can be tailored to fit the circumstances and needs of each enterprise, and deficiencies in the design of an ESOP can easily be corrected.

What is an ESOP? An ESOP may be designed to combine many elements into a single package. It is an employee benefit program. It is a tax-deferred means for workers to accumulate equity. It can be an incentive and productivity program for all employees. It can be a retirement program. It can be a new reward system, working best when a modest base salary is supplemented with cash bonuses and equity shares, linked to the proceeds of the operation. It can be a two-way accountability and communications system between management and non-management employees. It can be a means for workers to participate both as workers and as stock-holders in corporate direction. It can be an in-house tax-exempt stock exchange, for both new equity issuances and repurchase of outstanding shares. It can offer workers a source of current dividend incomes. An ESOP can be all of these and more; but one of its most unique features is that ***it is a basic innovation in corporate finance.***

An ESOP is the only tool in the world of investment finance that can create new owners and generate new sources of capital credit for corporate growth or transfers of ownership, while insulating these new owners from direct personal risk in the event of default and allowing repayment of the entire debt with pre-tax corporate dollars.

The leveraged ESOP operates in this way: it channels capital credit through a trust representing employees, from the ***same sources*** and subject to the ***same feasibility standards*** and corporate guarantees as direct loans to the corporation. The loan funds are used to buy stock for the workers, either from present owners or for financing expansion or modernization of the corporation. The loan to the trust is wholly secured by and repaid with future corporate earnings.

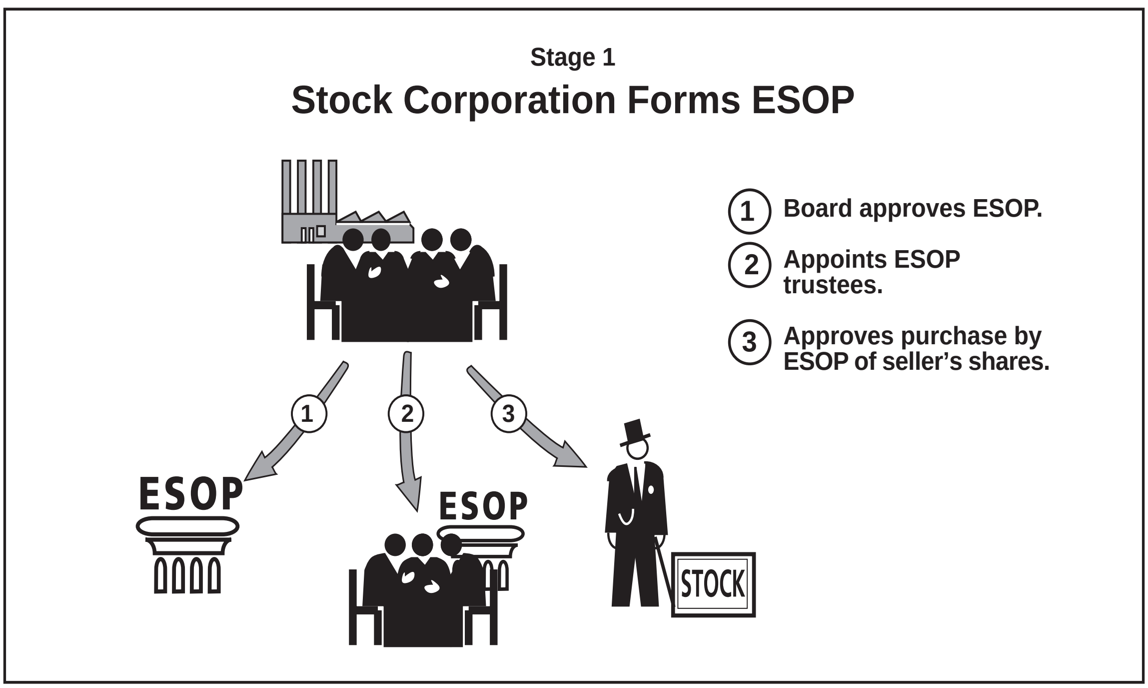
Normally, the workers make no cash outlay from payroll deductions or their savings, and none of their present savings is at risk. Shares of stock are allocated to the individual accounts of workers only as blocks of shares are "earned;" i.e., the company contributes cash out of future pre-tax profits to the trust. The cash, which is treated as a tax-deductible employee benefit, is used to repay the stock acquisition loan.

Whereas traditional uses of leveraged corporate credit work only for present owners, the ESOP uses corporate credit to convert its workers into stockholders. Thus, the magic of self-liquidating capital credit can be used to lift more individuals into an expanding ownership system.

A well-designed ESOP clarifies subtle distinctions between "ownership," "management," and "worker participation." Operationally under an ESOP, day-to-day control remains in the hands of professional managers who, under a carefully designed system of checks and balances, simply become accountable to a broader shareholder base, including other workers, and a more broadly representative board of directors.

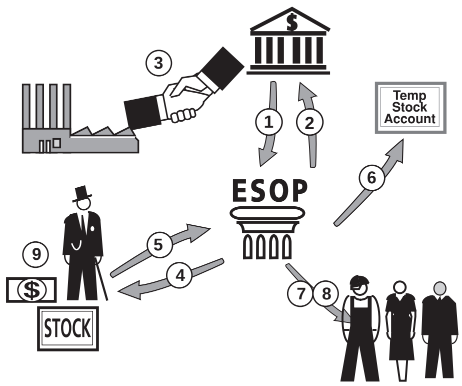
Employee stock ownership, therefore, involves a delicate balancing of the goal of efficiency with that of justice, and the goal of continuity of the firm with accountability of management to its new owners. It simply applies the genius of the republican form of government to the business world.

**These charts show how the ESOP is used to enable workers to buy existing shares:**



### Stage 2

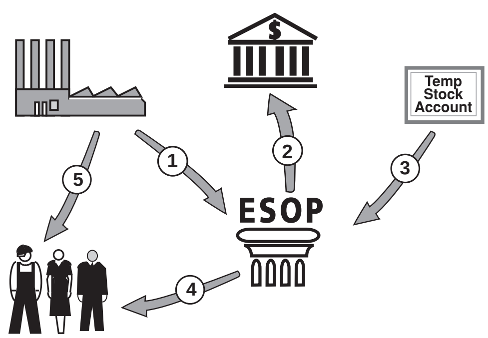
## Existing Stock Purchased with Loan to ESOP




1. Bank loans money to ESOP at reduced interest rates.
2. Trust signs note to bank.
3. Corporation guarantees to make contribution to ESOP to repay loans.
4. ESOP pays seller for shares.
5. Seller transfers shares to ESOP.
6. Shares pledged as collateral or held in suspense account.
7. ESOP accounts set up for each employee.
8. Credit purchase requires no cash or guaranty by employees.
9. Seller avoids capital gains taxes by buying new shares in another company.

### Stage 3

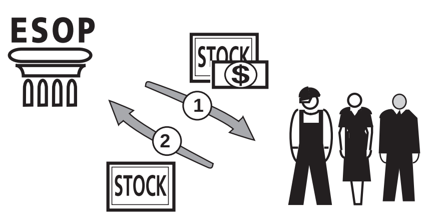
## Company Pays Out Profits for Repaying Buyout Loan, Bonuses, and Dividends as New Employee Benefits




1. Company makes annual contribution to ESOP for loan repayment (tax deductible).
2. ESOP pays annual principal and interest due on loan.
3. Shares released for annual allocations.
4. Released shares allocated and held in ESOP accounts of participants (non-taxable).
5. Distribution of monthly and annual cash bonuses and dividends, if available.

### Stage 4

## Distribution of Vested Shares Upon Retirement orTermination




1. Distribution of cash and ESOP shares (taxable).
2. Sale of distributed shares at appraised fair market value.

## ADVANTAGES OF ESOP

### For the Worker:

- Elevates the dignity and status of each worker to that of an owner.
- Diversifies workers' income beyond wages alone to include profit sharing bonuses, stock accumulations, dividend income and the participatory rights of a shareholder in the company.
- No taxes on the equity accumulations until shares are distributed from the ESOP trust, generally upon retirement.
- Provides workers as a group with access to productive credit for "leveraged" purchases of up to 100% of all shares of their company's equity, secured and repayable out of future profits.
- Job security cushioned during bad years by flexible ownership incentives linked to productivity and profits.
- Greater harmony and cooperation between management and nonmanagement workers.

### For the Seller:

- Leaves control of company in friendly hands.
- Rewards loyal workers who contributed to business success.
- Creates an in-house market for total or partial equity sales.
- Tax-exempt capital gains—tax incentives permit a tax-free investment rollover for owners who sell their shares of stock to an ESOP and use the proceeds to invest in other securities.*

  * Subject to favorable opinion of seller's tax advisors and counsel.

### For the Company:

- Discounted interest rates—lenders can reduce credit costs on loans to ESOPs which result in lower interest rates for capital growth and equity transfers.
- Easier debt service—lower interest plus the full deductibility of loan principal and interest repayments makes debt service easier.
- Positive cash flow—both tax savings and reduced interest costs produce added cash for the company.

### For the Lender:

- Lenders (banks, insurance companies and mutual funds) can charge lower interest costs on loans to ESOPs and gain added security from the ability of the ESOP to service its entire debt, principal and interest, on pre-tax corporate dollars.
- More harmonious labor-management relations further enhances security of debt repayment.

### For the Government:

- Reduced political pressures for subsidies, public sector payrolls and fiscal deficits.
- Expanded private sector productivity and a broader base of taxation from rising property and job incomes among workers.
- A broader political constituency against redistributive taxation and over-regulation of business.

## The Individual Stock Ownership Plan: A High-Powered IRA

Individual Retirement Accounts (IRAs) and Keogh Plans for the self-employed could be transformed into Individual Stock Ownership Plans (ISOPs). This would require amending tax and securities laws to provide each citizen with the same tax and credit treatment now provided to corporate employees through ESOPs. These tax-free accumulation devices could be structured to provide access to low-cost capital credit to all Americans through their local banks.

Thus, individuals, including those not employed in the private sector, could purchase on non-recourse credit a diversified portfolio of new SEC-qualified equity issuances, as an alternative method for financing the growth of American industry. Like the ESOP, this stock acquisition credit would be secured and repayable wholly with pre-tax corporate earnings, assuming that higher dividend payouts were encouraged by making them deductible as proposed below.

## The Consumer Stock Ownership Plan

Similarly, a Consumer Stock Ownership Plan (CSOP) could be structured for regular customers of such capital-intensive regulated enterprises as electric utilities, mass transit systems, cablevision systems, and other natural monopolies. Again, using low-cost capital credit, these companies would have new sources for financing their equity growth, while turning their customers into new stockholders.

The stock acquisition credit for CSOP participants would be repayable with their share of future profits, in the form of tax-deductible patronage bonuses and/or dividend payouts. After paying for the stock, dividends and patronage bonuses earned by the customers would help to offset their utility bills.

## The Community Investment Corporation

The Community Investment Corporation (CIC) grew out of a legal mechanism known as the "General Stock Ownership Corporation" (GSOC), which was added as Subchapter U of the Internal Revenue Code by the Revenue Act of 1978. As enacted, all citizens of a State could become stockholders of such massive projects as the Alaskan gas pipeline. Subchapter U proved so unwieldy that no State adopted a GSOC despite its many attractive ownership incentives

This mechanism, however, is extremely feasible if applied at a local community level, particularly if used as a real estate planning and development corporation, financed so that all present and future residents could become stockholders, as proposed below in connection with "super empowerment zones" initiatives (Paragraph 19, *"Specific Tax Reforms Recommended"*).

# IV. SPECIFIC RECOMMENDATIONS

## A. The Monetary Component

### The Logic of Corporate Finance: The Source of the Problem and the Key to Broadened Ownership of New Capital Formation

Self-liquidation is the logic of corporate finance. In general, newly formed industrial capital (improved land, new structures, advanced machines and tools) is never brought into existence unless the new investments will pay for themselves, generally 3 to 5 years as a rule of thumb. By projecting its future earnings or "future savings," as Simon Kuznets has pointed out in his book, *Capital in the American Economy: Its Formation and Financing,* a business will incorporate financing methods that will enable it to acquire the ownership of capital instruments before it has saved the funds to buy and pay for them. This is the purpose of finance. It is the meaning of "feasibility" in the investment world.

After the initial cost of investment is paid, of course, its equity resides wholly in its owners and is expected to earn additional profits for them indefinitely. (Through depreciation accounting, a company sets aside enough funds out of its gross earnings before net profits are even computed, thus preserving through physical maintenance and replacement the property rights of owners in already accumulated capital assets.)

Once feasibility is established, corporations become eligible to attract external credit from commercial banks. The funds may come from other people's savings or, as will be explained below, from expanded bank credit. In contrast to consumer credit, loans for investment purposes are secured by the general credit of the corporation itself and are non-recourse to the eventual equity owners of new capital.

In other words, the corporation is a "social tool" which affords legal insulation against personal liability to corporate stockholders in the event of default by the corporation on its loans or other obligations. This is its major function. It explains why society uses the corporations to produce most of our wealth. Stockholders benefit from corporate credit but at no personal risk to themselves or other investments.

Because the logic of corporate finance—self-liquidating credit—has never been extended to non-owners, it is self-evident why Karl Marx noted that "capital tends to breed capital," making the rich richer and keeping the workers propertyless throughout their lives.

Traditional methods of corporate finance—basically retained earnings and external credit—are the root cause of the highly concentrated ownership patterns in all free enterprise economies. Roughly 95 percent of all American households have little or no direct ownership stake in U.S. enterprises of any income significance. Access to direct equity participation, for those who can afford it, comes mainly from the public market in already outstanding securities, whose values are highly susceptible to manipulation by the rich and by large institutional investors.

Even worse, unless we develop alternative modes of corporate finance, today's ownership concentrations can only worsen. Virtually all future capital in the U.S.—at least $10 trillion needed for the next decade[3]—will become owned automatically by the same ownership class. The political climate for forceful redistribution and nationalization of our largest enterprises will correspondingly increase.

Since access to corporate credit determines whether the few or the many will share directly in the ownership of our corporate sector's growth potential, Capital Homestead reforms would promote innovative modes of corporate finance [described in Part III, *"Basic Vehicles for Implementation"*]. These vehicles would dramatically restructure future ownership opportunities within private sector corporations, while making new equity issuances more attractive as a source of expansion capital.

### "Pure Credit": An Untapped Source of Low-Interest Credit to Build Market Power into Consumers Based on Broadened Capital Ownership of New Capital

"Where will the money come from?" is a common reaction to those encountering the expanded ownership theories for the first time. After all, the U.S. economy needs roughly $10 trillion during the next decade and it does not appear, according to the projections made by the Chase Manhattan Bank and other observers, that Americans will be able to accumulate enough savings to purchase all that new capital.

The answer is "pure credit," or newly-created credit. "Pure credit" is a civilized society's ultimate weapon in the war against unjust concentrations of wealth and economic power. And it already exists in the hands of the Federal Reserve Board of Governors, waiting to be used for meeting our projected capital shortfalls and for democratizing the ownership base of the U.S. economy in the process.

Paper money, such as Federal Reserve Notes, is a "pure credit" instrument. Central bankers, such as the Board of Governors of the Fed, have the exclusive power to manufacture units of currency, which represent liabilities and promises made by the Fed. Properly issued, modern money is a lubricant (medium of exchange) for conducting transactions and is supposed to be a dependable yardstick for measuring economic values in the marketplace. Money facilitates credit transactions.

"Pure credit" is essentially based upon the legal concept of "promise" and the enforceability of contracts, two main ingredients of a free and orderly economy. Pure credit is nothing really more than the power of people (including legal associations of people, like corporations and the Fed itself), to contract freely with one another under a system of law which enables everyone affected by the contract to enforce their rights and claims over property under the contract.

It involves elements of volition as well as control. It is limited only to the extent that people, their associations, and government itself make promises they cannot keep. Since promise is the "glue" that holds any society together and determines how confi-

[3] According to the annual *Economic Report of the President*, new capital added in recent years in both the public sector and private sector, totals over $1 trillion annually in new plant and equipment, infrastructure and all forms of rentable space. This amounts to $4,000 per man, woman and child in America.

dently people view the future, the making and breaking of promises determines whether that society is strong or weak, orderly or disorderly, growing or disintegrating.

Credit by its very nature is a social phenomenon. Like the ballot, money and credit are "public goods," presumably accessible to all under equal conditions. Control over productive credit will determine in large measure the nature and quality of America's future industrial frontier as well as its future ownership distribution patterns.

Because credit is so essential to participation in a free enterprise market economy and to the acquisition of private property, ***a denial of access to credit amounts to a denial of one of the most fundamental of human rights,*** equality of access to the means to acquire and accumulate property.

Moreover, in a society where the ownership of productive capital is so crucial to freedom and human happiness, unjust discrimination among citizens as to who has access to capital credit constitutes as gross a violation of equal protection of the laws as discrimination in access to the ballot.

What Americans are beginning to discover is that such a violation of our fundamental constitutional rights is taking place daily on a systematic basis and the culprit is no less than our present Federal Reserve System. It manufactures capital credit which flows to the already rich, and ever more burdensome consumer credit to propertyless workers. Little wonder that there is increasing political sentiment in Washington to bring the Nation's central banker under greater public scrutiny and control.[4]

The way credit is used, the persons to whom it is made available, and the purposes for which it is used are proper subjects of governmental policy. The "social costs" of maintaining an efficient credit system and who will pay those costs can thus also be legitimate subjects of governmental regulation

In this light, the government can determine the appropriate Federal Reserve discount rate as a "service charge" for supplying new currency needed for expanding commercial bank credit to meet the growth needs of the economy.

When the "full faith and credit" of government stands behind the Nation's currency and the demand deposits in our commercial banking system, this involves "pure credit" in the ultimate sense. Government, by controlling the total volume of currency and commercial bank credit needed to facilitate economic transactions, controls the direction of private enterprise. Government also has the power to be "lender of last resort" under our Constitution, if that becomes necessary.

When the government abuses its money-creating powers, we have inflation and a breach of one of government's most important "promises" to its citizens, that the value of its currency will remain constant. And when government does not keep this basic promise to its people, all debts are jeopardized, property is arbitrarily redistributed to debtors from creditors, and all other promises that hold society together also become difficult to keep. "Trust" is gone.

Today, the Fed has no productive assets supporting the U.S. currency, only liabilities in the form of Treasury paper supporting liabilities in the form of paper currency.

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[4] William Greider, *Secrets of the Temple: How the Federal Reserve Runs the Country*, New York: Simon and Schuster, 1988.

The Fed prints money hoping that still unborn generations will be able to support wasteful government spending of the past. It is only a matter of time before this bubble bursts.

If it is the source of the problem, the Federal Reserve System—government's main instrumentality for controlling the costs and volume of "pure credit" extended through the commercial banking system—is also the source of the cure for inflation. It can play the central role in restructuring the future ownership patterns of the economy, while leaving the actual allocation of credit in the hands of commercial bankers.

In his book, *The Formation of Capital* (1935), Harold G. Moulton, former president of the Brookings Institute, laid the theoretical foundation for the "pure credit" monetary policies first developed by Louis Kelso and refined by this author.[5]

Moulton pointed out that ***economic growth did not depend exclusively on past accumulated savings,*** that there need not be a trade-off between expanded consumption and expanded investment. Growth could instead by based on transforming waste (in human and technological potential) into useful production, ***based on future saving and future profits.***

Moulton posed the question, "Where could funds be procured for capital purposes if consumption was expanding and savings declining?" Most economists assert there can be no growth without savings, unless we cut back on consumption. Moulton answered his own question:

> "From commercial bank credit expansion. Such expansion relieves the possibility of shortage in the 'money market' and enables business enterprises to assemble the labor and materials necessary for the construction of additional plant and equipment." (Page 107)

The real limits to expanded bank credit, Moulton added, were physical ones: unused capital resources and raw materials, an unemployed work force, unutilized plant capacity, and ready markets for new capital goods and new consumer goods.

His study of one of the fastest growth periods of U.S. economic history, 1865 to 1895, revealed that while bank reserve requirements remained relatively constant, the volume of commercial bank credit outstanding rose substantially but price levels actually declined for the period by about 65 percent. (Pages 87, 116)

Moulton also demonstrated that even in periods of great business activity, our productive energies are normally underutilized; there is always some slack in the system

The proponents of the "Phillips Curve" suggest that we cannot accelerate present growth rates without causing inflation. In fact, Fed Chairman Alan Greenspan has stated that growth in the U.S.—given current rates of productivity growth of 1.4% and growth in the workforce of 1.1%—should not exceed 2.5% annually.[6]

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[5] See "The Federal Reserve Discount Window," Norman G. Kurland, *Journal of Employee Ownership Law and Finance*, National Center for Employee Ownership, Oakland, CA, Winter 1998.

[6] See letter of April 4, 1995 from Alan Greenspan to Congressman Bennie Thompson (D-Mississippi) in response to Cong. Thompson's letter of March 24, 1995. Contained in *"The Federal Reserve Discount Window"* by Norman G. Kurland (cited above).

Citing historical evidence to the contrary, Moulton proves that we can have rapid growth without inflation. Indeed, during World War II the U.S. economy experienced 15% annual growth rates, despite the removal of 13 million able-bodied workers from the workforce to engage in a global two-front war.

And, on the opposite side of the coin (also to the chagrin of many economists), we can have rising prices alongside recession, as we recently experienced for the first time in 1974.

Moulton's conclusion is worth noting:

> "[T]he expansion of capital occurs only when the output of consumption goods is also expanding; and . . . this is made possible by the [simultaneous] expansion of credit for production purposes." (Page 118)

Unfortunately, Moulton failed to carry the connection between expanded bank credit and expanded capital creation to the next logical step forward: the expansion of the base of capital ownership and capital income distributions as a new, more direct, and more efficient source of mass buying power to absorb future outputs of final consumption goods. But Louis Kelso fortunately picked up where Moulton left off.

## The Discounting of "Eligible Paper": The Federal Reserve's Hidden Power to Stimulate Private Sector Productivity Increases and Broadened Ownership

Supplying funds to the money market and controlling the cost of these funds—the rediscount rate—has long been recognized as the orthodox instrument of monetary policy. In *"Lombard Street"* (1873), Walter Bagehot outlined the principles of central banking, arguing that the main function of the Bank of England was to serve as the lender of last resort, mainly by supplying liquidity to a capital-deficient economy through the flexible use of its rediscount powers.

The House Banking and Currency Committee, in its widely circulated publication, *"A Primer on Money "* (August 5, 1964) noted:

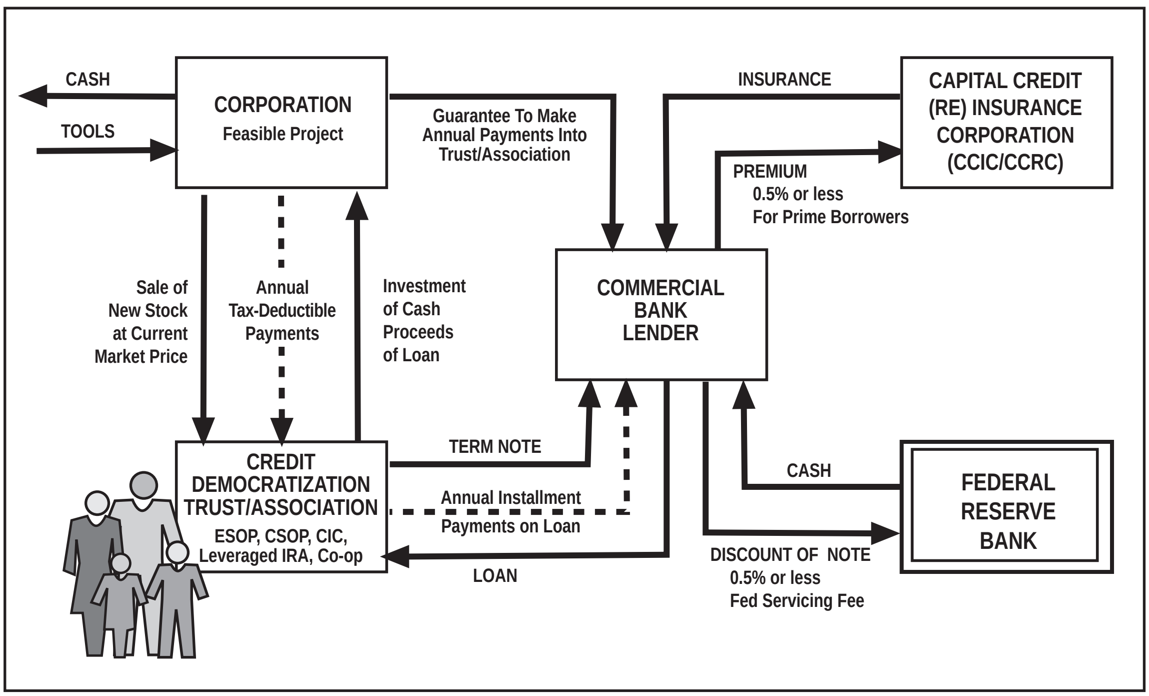
> "When the Federal Reserve Act was passed, Congress intended [the purchase of "eligible paper"] to be the main way that the Federal Reserve System would create bank reserves. . . . When this practice was followed, the banks in a particular area could obtain loanable funds in direct proportion to the community's needs for money. But in recent years, the Federal Reserve has purchased almost no eligible paper. . . ." (Page 42)

> "When the Federal Reserve System was set up in 1914 . . . the money supply was expected to grow with the needs of the economy. . . . It was hoped that by monetizing "eligible" short-term commercial paper, by providing liquidity to sound banks in periods of stress, and by restraining excessive credit expansion, the banking system could be guided automatically toward the provision of an adequate and stable money supply to meet the needs of industry and commerce. . . . The system's reserves would expand and contract via the discount window as cash and other needs made necessary. . . . To safeguard their liquidity and provide a base for expansion, the member banks... could obtain credit from the nearest Federal

> Reserve bank, usually by rediscounting their "eligible paper" at the bank—i.e., . . . selling to the Reserve Bank certain loan paper representing loans which the member bank had made to its own customers (the requirements for eligibility being defined by law). If necessary, the member banks might also obtain reserves by getting "advances" from the Federal Reserve bank. . . ." (Page 69)

The two-tiered interest rate policy was invented in 1974 by this author to resurrect the Fed's discount mechanism as the principal means for the democratization of productive credit, leading to accelerated rates of investment, broadened ownership, and an asset-backed currency.[7] [For a graphic description of "where the money will come from" for building an expanded ownership economy, see the diagram below, *"Creating Money for Capital Homesteading."*]

## CREATING MONEY FOR CAPITAL HOMESTEADING

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[7] See *"A New U.S. Monetary Policy for Fighting Inflation and Financing Growth of U.S. Productivity Through the Private Sector,"* Norman G. Kurland, Occasional Paper, Arlington, Va., August 2, 1974. Also see *"Kelsonian Monetary Policies for Fighting Inflation,"* Norman G. Kurland, a paper delivered to the Eastern Economics Association, panel on Kelsonian Economics, April 15, 1977; reprinted in Hearings on H.R. 3056, Small Business Employee Ownership Act, Subcommittee on Access to Equity Capital and Business Opportunities, Committee on Small Business, U.S. House of Representatives, May 8, 1979, pp. 15-29.)

## Recommended Monetary Reforms

The specific monetary reforms to accelerate private sector growth linked to expanded capital ownership are as follows:

1. Declare a moratorium on any future purchases by the Open Market Committee of the Federal Reserve System of U.S. Treasury bills, other public debt paper, including foreign currencies, thus forcing the U.S. Treasury to sell directly its paper on the open market and putting an end to further monetization of government deficits.

2. Simultaneously, the Fed should announce a ***two-tiered interest policy*** under which its discount rate would be set at 0.5% or less and its discount window would be exclusively available to member banks and members of the Farm Credit system for discounting "eligible" paper for feasible industrial, commercial, and agricultural projects. "Eligible" paper would be strictly limited to promissory notes and other private-sector productive credit instruments issued by IRS-qualified ESOPs, CICs, leveraged IRAs and CSOPs, production and marketing cooperatives, family farmers, sole proprietorships, or other IRS-qualified expanded ownership mechanisms for the purpose of financing growth or acquisition of productive (i.e., income-producing) capital assets. (Where feasible such credit should also be available to buy one's primary home.) All such credit would have to be supported by a business feasibility study reflecting the self-liquidating nature of the transaction. The loan paper would also be:

   (a) secured by the general credit of the enterprise as a going concern;

   (b) collateralized by equity instruments, accounts receivable, land and other hard assets involved in the transaction, plus the shares of stock acquired with the loan;

   (c) insured to cover the risk of default by commercially available credit insurance, through premiums paid by borrowers or lending banks;

   (d) designed to be repayable principally from the future pre-tax earnings of the enterprise guaranteeing the loan's repayment;

   (e) endorsed for negotiability by the commercial banks making the loans; and

   (f) endorsed by every collective bargaining unit representing employees of the enterprise guaranteeing the loans to its members.

3. Banks negotiating loan paper that is eligible for discount with the Fed would be free to allow market forces to determine the bank's mark-up for money, above the Fed's 0.5% discount rate ("Fed service charge"). Thus, commercial bank lenders could cover their administrative costs and profits, plus a premium to cover the anticipated risk of default on the specific investment being financed. Prime interest rates should drop to 3% or less under the two-tiered interest policy, without any tax subsidies.

4. All new currency issued by the Fed to meet the discount needs of its member banks under the Capital Homestead Act should be subject to a special 100% reserve requirement, thus creating a 100% asset-backed currency. (This new money would be supported by promissory notes backed by business guarantees of repayment; collateralized by the new equity issuances and new business assets financed under the Act; and reinforced by highly-motivated borrowers disciplined by ownership incentives.) This would simplify the policing role of the Fed and help guard against misuse or abuse of their discount privileges by the member banks.

5. The Fed should be specifically prohibited from purchasing or discounting paper representing any non-productive uses of credit (such as U.S. Treasury Notes, consumer loans, loans for speculating in commodities or securities, unfriendly leveraged acquisitions, local and State government debt, etc.) or other uses of credit that do not encourage broadened capital ownership and competitive markets. However, existing savings freed up by the lower tier of the new interest structure would remain available at market rates for consumer finance, speculation, and other non-productive uses of credit, as well as future public sector borrowings.

6. There are many options available to government in structuring accessibility to capital credit. For example, like the $10,000 home loans to World War II veterans, annual allotments of Capital Homestead Act credit could be extended to eligible individuals for investments of their choice, as long as local banks (subject to Federal feasibility criteria) determine the venture to be feasible and the loan repayable with future pre-tax earnings.

   Entrepreneurs, farmers, professionals and workers could then aggregate their credit through ESOPs of existing or new corporations; or they could acquire diversified holdings through special IRAs or pension plans designed to invest in SEC-registered new equity issuances, CICs, consumer stock ownership plans, etc.; or they could launch their own new ventures. Corporations and farms needing expansion capital would have new lower-cost sources for meeting their funding requirements.

7. A Capital Diffusion Insurance Corporation could be established, on a self-financing basis, similar to MGIC or FHA home mortgage insurance, to offer commercial insurance to bank lenders against the risk of default on Capital Homestead Act capital credit and to offer, for a premium paid by the new owners, some "down-side risk" portfolio insurance. These risks could be spread even further through a reinsurance facility established either by the private sector or by the public sector.

8. The amount of annual credit to be discounted each year by the Fed under the Capital Homestead Act could meet at least 50% of the $1 trillion added each year in new plant and equipment, new infrastruc-

> ture, and new rentable space by the U.S. private and public sectors.[8] (Today, almost none of this incremental growth is financed in ways that expand ownership to poor and middle-ioncome Americans.) Spreading access to ownership stakes in a $500 billion growth pie equally among America's 150 million registered voters, each U.S. voter could be allotted over $3,000 annually in Fed-discounted capital credit to invest in the capital growth of the U.S. economy.

In the alternative, such credit could be linked to relative employment incomes for incentive purposes and to encourage more honest disclosures for Federal tax purposes. (Thus, a voter earning $20,000 could get a low-cost capital loan of, say $10 per $100 of reported employment income, or $2,000. A "floor" could be set at $1,000 and a "ceiling" at an appropriate level geared to the balance of each year's annual U.S. productive capital to be financed through the Federal Reserve discount mechanism.)

Each year the credit allotted to each voter could be adjusted to the nation's projected capital requirements for that year. Higher allotments of low-cost production credit might have to be provided to farmers, in order to keep America's agricultural lands in private hands, particularly younger farmers, and to maintain present high levels of productivity in food production.

Logically, this reform could generate faster rates of growth than the artificially low growth limits of 2.5% annually imposed by Alan Greenspan, Chairman of the Federal Reserve System. Greenspan's arguments that faster rates of growth would trigger runaway inflation assumes a continued exclusion of middle-income and poor Americans from the means to share in growth profits.

Greenspan also assumes a continuation of the waste in human and technological potential inherent in today's Welfare State. The credit reforms and budget-balancing tax reforms in the Capital Homestead Act would convert this waste into marketable production, with income from new jobs and widespread sharing of growth profits to sustain higher rates of growth. Hence, America could easily reach the 5% growth rates called for by President Clinton and House Speaker Gingrich, without inflation.

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[8] The annual new capital formation in all sectors of the American economy, as of November 1992, consisted of:

| | |
|---|---|
| New plant and equipment | $565.4 billion |
| Non-residential construction | $126.2 billion |
| Public construction | $122.2 billion |
| Residential buildings | $193.3 billion |
| | **$1.007 trillion** |

Source: *Economic Report of the President,* January 1993 (Tables B-50 and B52).

## B. THE TAX COMPONENT

### Objectives of tax reform[9]

1. To make Congress more directly accountable and responsive to all taxpayers.
2. To improve structural restraints within the tax system on government growth and spending by creating a direct linkage between tax rates and budgetary changes.
3. To encourage savings and investment and otherwise favor growth in the competitive free enterprise system as the direct distributor of consumption incomes for American workers and retired citizens.
4. To reduce and gradually eliminate all redistribution features within the current tax system, including Social Security, except for income exemptions and an income "safety net" for the genuinely poor.
5. To simplify the overall tax system to improve taxpayer feedback and understanding and to make it less costly to administer.
6. To produce neutrality in the taxation of consumption incomes from all sources, and otherwise remove all distinctions between "earned" and "unearned" incomes.
7. To stimulate expanded opportunities for all Americans to acquire, accumulate, and receive incomes from direct equity participation in new and growing enterprises.
8. To abandon today's complicated mixture of tax penalties and discriminatory tax brackets, offset by special tax subsidies, credits and privileges affecting property, wealth accumulations, new productive investments, and so-called "unearned" income, and replacing these tax gimmicks with simple "escape hatches" designed to encourage expanded private sector investment and productivity incentives linked to broadened ownership participation.
9. To eliminate the inflationary impact of the tax system itself on the costs of American produced goods and services, and to remove artificial tax increases (e.g. "bracket creep," inventory adjustment profits) wholly due to inflation.
10. To integrate the corporation and personal income tax systems by:
    (a) eliminating the double and triple penalty tax on corporate profits;
    (b) encouraging fuller dividend payouts; and

[9] The serious reader will find the justification and tax philosophy behind these Capital Homestead Act reforms described in detail in this author's article, *"Beyond ESOP: Steps Toward Tax Justice,"* published in the April and July 1976 issues of *Tax Executive* and updated in chapter 8 of *Curing World Poverty: The New Role of Property,* John H. Miller, ed., Social Justice Review, St. Louis, 1994.

(c) attributing non-reinvested corporate earnings as incomes taxable to shareholders.

11. To eliminate:

    (a) the tax penalty on married couples;

    (b) personal deductions (except for tax deferrals and exemptions for savings and investments);

    (c) tax credits;

    (d) tax-free interest on public-sector financing;

    (e) tariffs on imported goods (except when used selectively to encourage just market competition);

    (f) tax shelters for speculative and non-productive investment;

    (g) all forms of indirect taxes not based on consumption incomes.

12. To eliminate the effect of inflation on gains from the sale or exchange of homes, farms and other productive assets.

13. To encourage home ownership as an investment by allowing deductions of mortgage payments on homes but treat "imputed rent" as a form of taxable consumption income.

14. To expand the use of Individual Retirement Accounts (IRAs) as a mechanism for enabling all individuals to accumulate income-producing assets on a tax-deferred and/or exempt basis and to give IRAs and other Capital Homesteading vehicles the same tax treatment as now enjoyed by employee stock ownership plans, for the purpose of acquiring corporate shares on credit secured and repaid with dividends deductible at the corporate level.

15. To relieve pressure on the Social Security System by establishing a lifetime personal "Capital Homestead Exemption" to enable every American to accumulate (through ESOPs, IRAs, and other Capital Homesteading vehicles) a capital estate of at least $500,000 worth of wealth-producing assets to provide them in their retirement years with taxable capital incomes to supplement incomes from other sources.

16. To move toward the deconcentration of capital ownership in private hands for future generations of Americans by replacing estate and gift taxes with a tax on the amount that the recipient does not keep in the form of an income-producing investment or on an amount in excess of the "Capital Homestead Exemption."

## Specific Tax Reforms Recommended[10]

1. Replace the regressive Social Security/Medicare tax and the graduated tax on personal income with a **single percentage tax on total income above the poverty level**,[11] whether "earned" or "unearned," including all incomes from work, interest, dividends, inflation-indexed gains, rentals, unemployment compensation, welfare, social security and pension incomes, gifts and inheritances (above the "Capital Homestead Exemption" described below), etc.

2. Allow the tax advantages of a leveraged ESOP to be extended to all taxpayers through IRS-qualified IRAs, to utility customers under consumer stock ownership plans (CSOPs), and to citizen-shareholders of regional and local Community Investment Corporations (CICs).

3. Integrate with the Social Security System a tax-exempt "Capital Homestead Exemption" to encourage every man, woman, and child to accumulate through ESOP rollovers, Keogh Plans, IRAs, gifts, bequests, savings, etc., a personal life-time estate of wealth-producing assets. This reform would be targeted to provide all Americans with growing property incomes and direct ownership participation in the competitive free enterprise system.

   To establish a long-range ownership target and to motivate working Americans to maximum rates of investment and productivity, this "minimum floor of capital self-sufficiency" should be set high, perhaps $500,000 worth of accumulated investments per American during his lifetime. Such an estate would provide the same degree of income self-sufficiency for a family as the 160 acres of productive farmland granted under the original Homestead Acts.

4. Eliminate all contribution limits on "savings" through ESOPs, IRAs, Keogh Plans, and other Capital Homesteading vehicles, until individual accumulations exceed the proposed Capital Homestead Exemption.

5. Absorb the annual cost of the Social Security System entirely within the single percentage tax imposed on all incomes above the poverty level. As expanded growth and expanded ownership provide noninflationary property incomes for retiring Americans, social security benefits can become stabilized and perhaps reduced eventually.

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[10] The tax-favored corporate payouts listed here ***should not be labeled "tax subsidies,"*** any more than deductible wage costs are "subsidies" to employers. Tax-deductible profit distributions, as proposed here, represent structural reform of the tax system. These tax deductions are designed to eliminate the unjust "double tax" penalty on corporate profits, by integrating the corporate income tax with the personal income tax, while exempting reasonable property accumulations to meet the Nation's income security goals.

[11] Note the radical departure of this "poor man's single percentage proposal" from the flat tax proposals of Steve Forbes, Jack Kemp and others: Their "make the rich richer" flat tax would exempt from taxation capital gains, dividends, interest, inheritances, and gifts, and insulate the rich from contributing from their property incomes to the regressive, pay-as-you-go Social Security and Medicare systems. Under our single percentage tax, the poverty-level worker and his employer would pay no Social Security or Medicare taxes, because all revenues to meet Social Security and Medicare promises would be funded by a single percentage tax from many incomes now escaping from this growing burden.

6. Move toward a balanced budget by adjusting the single percentage tax proposed in paragraph (1) to a single percentage rate that all taxpayers will pay on their non-exempt incomes anticipated for that year to cover all budgeted Federal expenditures for the same year and, when appropriate, gradually eliminate the government's debt. The single percentage tax can be adjusted from year to year, but its very existence will create a highly focused pressure on Congress to keep the single percentage as low as possible.

7. Eliminate all existing deductions and tax credits to businesses and individuals, except:

   (a) Ordinary and necessary business expenses, including full and immediate deductions for current expenditures or full debt service payments to replace existing productive assets and otherwise to maintain current levels of profitability and productivity.

   (b) All incomes channeled by businesses or individuals for financing growth or asset transfers into employee stock ownership plans (ESOPs), individual retirement plans (IRAs), pension plans, Keogh plans, or other IRS-"qualified" Capital Homesteading vehicles, but in no case where such amounts cause the accumulations of individual beneficiaries to exceed the $500,000 "Capital Homestead Exemption" described in paragraph (3) above. These "savings" could be treated as tax deductible by either the businesses or individuals that make them.

8. Allow the full deduction of the purchase price or the current mortgage payment (principal as well as interest) for the purchase of a taxpayer's principal home. However, to provide tax neutrality between renters and homeowners, add the "imputed rent" of each dwelling of a taxpayer to his annual taxable earnings.

9. Exempt all household incomes of the genuinely poor by excluding from the single percentage tax all incomes below $7,000 per household member.

10. Allow corporate dividends to be deductible at the corporate level to the extent they are paid out currently to stockholders or are used to repay loans for purchasing newly issued stock or stock ownership transfers through ESOPs, IRAs or similar "qualified" Capital Homesteading mechanisms.[12]

11. Tax all dividends and interest income at the personal level without exclusions to the extent the taxpayer's total income from all sources exceeds the exemption levels for the poor.

[12] This reform would necessarily reduce such exclusionary and ownership-concentrating sources of corporate finance as retained earnings and direct debt. However, the monetary reforms described above in Part IV.A would provide for a more than adequate substitute—"pure credit" for Capital Homesteading financing—in volumes limited only by the economy's real growth capacity.

12. Exempt all capital gains from taxable personal income only to the extent that:

    (a) The taxpayer's gains are reinvested within 60 days (or 18 months for a home) into income-generating investments held within an IRS-qualified capital accumulation mechanism (e.g. ESOP, IRA, etc.) but not exceeding the "Capital Homestead Exemption" listed in paragraph (3) below.

    (b) The taxpayer's spendable gains are equal to or less than the inflation-adjusted value of the assets during the period over which the assets were held before being sold.

13. Avoid double taxation by maintaining a tax on corporate net earnings but allow corporations to avoid taxes on earnings they pay out as dividends, cash productivity bonuses, ESOP and profit sharing contributions, purchases or debt service payments on replacement assets, etc.

14. Ordinary business expenses, like wages, would remain deductible as under present laws, while encouraging ownership expansion by allowing:

    (a) Full debt service deductions on credit to acquire replacement assets.

    (b) Full dividend deductibility, thus encouraging full dividend payouts while permitting stockholders to purchase newly issued corporate shares with profits deductible from corporate earnings. In the alternative, stockholders as well as employees through ESOPs could use these tax-deductible dividends to repay loans for the acquisition of larger blocks of stock on a leveraged basis.

    (c) Expanded use of tax-deductible contributions to a leveraged ESOP for financing new equity issuances representing growth capital of the company. This would effectively allow the current expensing of annual debt service payments for financing growth through the company's ESOP.

15. Depreciation rules would be liberalized by allowing full first-year deductions on all purchases of replacement assets (to maintain existing levels of productivity and profits).

16. Provide for the tax-free rollover of the proceeds from the sale to an ESOP of shares or assets of any enterprise, including shares trading in the open market, as long as the proceeds are reinvested in other productive assets within 18 months. This would encourage employee participation in ownership as well as provide a new source of equity financing for new and growing businesses. (This expands the present rollover provision for sale of shares to an ESOP to shareholders of publicly traded companies.)

17. Allow an ESOP to assume the estate tax liability for the value of employer stock transferred to an ESOP by the executor of an estate, provided the company guarantees payment of the tax over a seven year period.

18. Permit an ESOP to be treated as a charitable organization for income, gift, and estate tax purposes provided the donated stock is not allocated to the donor, family members of the donor or 25 percent shareholders.
19. Amend the Internal Revenue Code (following the precedent in the former Subchapter U for General Stock Ownership Corporations) to allow the use of Community Investment Corporations (CICs) for land planning, acquisition and development of "super empowerment zones" so as to encourage comprehensive, large-scale development of an area combined with widespread participation among residents in the ownership, profits, and appreciated real estate values that would otherwise flow exclusively to outside land speculators.

## C. OTHER POLICY REFORMS

### Fiscal Policy Reforms

By restructuring the Federal monetary and tax system to promote accelerated rates of private sector investment linked to expanded ownership, wasted people, hoarded resources and underutilized technology would be put back into full production. This would not only reduce Federal spending for welfare and unemployment and increase the earnings base for Federal tax revenues, but it would also begin to transform today's inherently inflationary "wage system" by linking labor's increased gains to rising productivity and profits.

Thus, many inflation-indexed costs would be eliminated, including the interest costs on the Federal debt. The proposed single percentage tax would also serve as a brake on runaway Federal spending.

### Social Security System Reforms

By generating higher job and investment incomes for all Americans and shifting to a single percentage tax for covering Social Security costs, the Capital Homestead Act would act as a "safety valve" on today's near-bankrupt system. Unlike the "pay-as-you-go" Social Security System, the Capital Homestead Act would help finance America's productive growth and remove an oppressive future burden on our young workers.

### Public and Private Retirement System Reforms

Instead of gaining a direct private property stake in our free enterprise system, civil servants at the State and local levels acquire through their pension plans an extremely remote and indirect ownership stake in the Nation's productive capital. The same holds for private pensions, which Peter Drucker has aptly described as "pension plan socialism." Such collective ownership of the means of production is hardly distinguishable from the way it was for the workers in the former Soviet Union.

As they now stand, these pension plans distort stock values, place enormous power in the hands of money managers, large institutional investors, stock brokers, day traders and other speculators, but do little to meet directly the financing needs of capital-starved industries. In fact, many vulnerable companies are threatened with bankruptcy because of their large and growing pension liabilities. And pension trustees have become willing allies for corporate raiders and unfriendly takeovers of major U.S. corporations, causing losses of millions of jobs in the process.

At the Federal level, whatever assets are held to pay for rising military and civilian pension benefits are mainly in Treasury paper, not in the productive assets the economy needs to generate taxable incomes. The Capital Homestead Act would create a piece of the action in America's growth frontier for all public and private employees covered by today's defective retirement systems.

### Privatizing Government Enterprises and Services

The Postal Service and the Air Traffic Control System are but two examples of enterprises that could probably be run more efficiently and more profitably if they were run as employee-owned operations. Waste, absenteeism, featherbedding, and resistance to automation are less tolerated by employee-owners than by those with no ownership stake in bottom-line profits.

The TVA could also be re-organized as a stock corporation owned by its employees and customers. So could mass transit systems if they had access to low-cost credit from local banks under the monetary reforms proposed under the Capital Homestead Act. In fact, even new local schools could be organized by parents and frustrated teachers as for-profit corporations if sufficient low-cost capital credit were available (reinforced by a voucher system) to enable them to enter into effective competition with the public school systems. The Scottsdale, Arizona Fire Department and San Francisco's garbage collectors work very well as employee-owned operations.

### Anti-Trust Reforms

A pro-competition approach to anti-trust problems involves a two-pronged approach: (1) where courts have ordered that a violator divest itself of a subsidiary or a division, the Federal Government should advocate ESOP financing as a remedy, so that the divested operation could operate independently as an employee-owned company, with the violator even providing some of the buyout credit; and (2) to prevent excessive concentration from occurring in the first place, potential competitors should be provided with access to sufficient low-cost capital credit, as proposed in the Capital Homestead Act, to enable them to meet economies of scale. In general, however, private monopolies never occur without some special privilege or power conferred on them by government.

### Super Empowerment Zones

Legislation supporting "free enterprise zones" offer a laboratory for converting economically depressed urban and rural areas into prototypes for free market policies linked to expanded ownership. So far, however, the ownership thrust has been muted to the point of virtual silence, offering critics another example to deride as "trickle-down" economics. By adding the ownership strategy outlined in paragraph #2 above under "Monetary Reforms" and paragraph #17 under "Tax Reforms," an enterprise zone would become a microcosm of a socially just market economy (a "Super Empowerment Zone") rebuilt from the bottom-up.[13]

## Environmental Protection Reforms

Another way of describing pollution is "resources out of place." Recapturing those resources and keeping them from harming innocent victims and other living things generally require expensive technology. Customers must be able to afford the additional costs involved, and the technology required to preserve the environment must be financed in the least expensive way. The Capital Homestead Act provides that financing and also enables the ultimate customers of corporate products to gain rising property incomes so that they can better afford the extra costs of a healthier environment.

A "special burden" tax on industrial polluters might also be considered to cover damages to victims and the environment and as an incentive to minimize pollution. This would pass on to customers the unavoidable costs of technological development, which inevitably is an imperfect process.

## Ownership Reforms for Land and Natural Resources

Land and natural resources should be owned by the people, not the government. Control over land and natural resources dictates the quality of how that land is used, and the extent to which finite natural resources can be transformed into new and ever more productive and efficient tools and technologies, including alternative sources of energy. In the past, ownership and control over land and natural resources have generally been monopolized, either in the hands of government, or a few landowners, speculators and giant corporations. In the future, to the maximum extent possible, new laws and institutions should be encouraged that ensure widespread local citizen and family participation in the ownership, control and profits of sustainable and environmentally-sound development of local and regional land and natural resources. (Special legal provisions restricting land use could be built into transfers of government-owned lands designated as wilderness areas or natural treasures.) At the minimum, all local land now owned by governments at all levels should be transferred free of charge to local and regional for-profit Community Investment Corporations ("CICs"). This would turn landless citizens and stakeholders into shareholders, with government retaining oversight responsibilities to guarantee economic justice, preserve irreplaceable wilderness areas, and safeguard fundamental human rights and the rights of future generations.

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[13] See *"Capital Homesteading for DC Citizens: A Federal Reserve Demonstration for Funding Economic Empowerment."* Norman G. Kurland. Occasional Paper, Arlington: Center for Economic and Social Justice, 1995.

## Multinationals and Foreign Assistance

American assistance to the developing countries could be vastly expanded, with reduced taxpayer support, if U.S.-based multinational corporations could be encouraged to link their investments overseas with the expanded ownership objectives called for under the Capital Homestead Act.

For example, through use of ESOP financing the multinationals would not only convert their foreign employees into capital owners, but in so doing would automatically be creating a broadened political constituency for a global common market based on free enterprise principles.

No troops or foreign aid could offer a more effective safeguard against future expropriations and nationalizations of U.S.-based companies around the world. This would also facilitate the transfer of U.S. know-how and technology in ways that would further peaceful growth and expanded U.S. markets.

## Law of the Seas Treaty

Through employee-owned subsidiaries of multinational corporations, the ocean beds could begin to be mined in ways that would simultaneously offer training, job and ownership opportunities to individuals from all parts of the world, thus enabling them to return home after 5-year tours of service as affluent individuals. The more efficient the operation, the faster affluence could be produced from the sea and injected into the developing economies. No international income redistribution scheme could conceivably do better.

## Capital Homestead Planning Commission

To refine the programs of the Capital Homestead Act and chart its future, the President should convene a task force of action-intellectuals and prime movers from the business, labor and political world. It could outline targets and priorities to guide the program and help in communicating it to the media and the general public. Some of its members could be appointed to an Capital Homestead Planning Commission to oversee and give continuing policy direction to the program.

## U.S. Office of Expanded Capital Ownership

The Act should provide for a small permanent staff to administer and evaluate the progress of the President's expanded ownership programs. It should be given equal status with the Office of Management and Budget, whose tasks should be greatly simplified if the Capital Homestead Act initiatives prove successful.

## CONCLUSION

As we stand at the threshhold of the Twenty-First Century, humanity is faced with a critical choice.

We can continue down the old paths, bound by the scarcity assumptions and theories of the past, where technology and global markets represent a boon to a fortunate few and a threat to the livelihoods of many.

Or, guided by the revolutionary insights of Louis Kelso, Buckminster Fuller, Martin Luther King, Jr., Russell Long, and other "post-scarcity" visionaries, we can travel a new path. Not bound by the finite borders of a land frontier, this new path leads to an advanced technology frontier limited only by human creativity and ingenuity. It is a path which seeks the unshackling of human potential of all persons globally and the lifting of the social barriers that make the rich richer and the poor and middle class increasingly vulnerable economically to technological progress.

Indeed, the most challenging problems facing society are not in science or technology. Rather, they can be traced to the growing gap between our technological environment and our social environment. The first environment we can see or feel; it changes with scientific discoveries and the invention of more efficient technologies. The second environment consists of "invisible structures" (i.e., laws, constitutions, and social institutions such as our monetary and tax system)—things we cannot see or feel.

It is in the design of these invisible structures that our relationship with technology is determined. How we design these social structures will determine who will control and profit from what Bucky Fuller called the "energy slaves" of advanced technology.

Since the Industrial Revolution, the faster technology has progressed, the faster most people have become separated from their technological environment and the means for earning a living. By blocking human beings from equal access to ownership incomes and power to control their own destinies, institutional barriers impede those individuals from working effectively with others for the common good. Therefore, everyone loses from this waste of human creativity.

To lift these social barriers requires correcting the faulty ideas and defective institutional structures of economic plutocracy upon which they rest. Ultimately, good ideas work in the long run and inferior ideas eventually create their own problems. But new ideas require people willing to step ahead of the crowd, willing to abandon their own ideas when they are wrong, willing to take risks, if necessary, for ideas that are right.

Creating new owners of new wealth is a good idea whose time has come. It will become a reality when it attracts the critical mass of new leaders and ordinary people who are ready to address the problems and injustices inherent in the economics of scarcity. It will take market-oriented populists with the bold vision and courage of America's pioneering ancestors, people who are willing to venture forward into the challenging new frontier that is waiting to be built in the Twenty-First Century. The world awaits these Space Age pioneers.

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