

CESJ Editor's Note (11/11/08): The proposed level of tax exemptions under the Capital Homestead Act has been increased since this article was published in 2005. The exemptions from federal taxes allowed for a family of four, for example, have been raised to the first \$100,000 of family income (previously \$30,000), keeping more money in their pockets to pay for living expenses including their health coverage and education. See <http://www.cesj.org/socialsecurity/projections-cha.htm>.

taxanalysts

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Capital Homesteading for Every Citizen: Reforming the Tax System

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The following tax reform plan is excerpted from *Capital Homesteading for Every Citizen: A Just Free Market Solution for Saving Social Security*, published by Economic Justice Media (2004). For more information on the book and CESJ, go to <http://www.cesj.org>. For a glossary of the terms used in this article, go to <http://www.cesj.org/definitions/glossary.html>.

While the President's Advisory Panel on Federal Tax Reform will soon release its recommendations for revising the federal tax system, the tax reform debate obviously will continue. *Tax Notes* therefore will continue to publish tax reform proposals prepared by think tanks, interest groups, and other organizations. If your organization would like its tax reform plan published in *Tax Notes*, please e-mail it to us at taxnotes@tax.org.

For earlier articles in this series, see *Tax Notes*, May 2, 2005, p. 645; May 9, 2005, p. 767; and May 16, 2005, p. 915.

Few Americans today would label the U.S. tax system as either simple or fair. Many Americans believe that tax breaks are mainly benefiting the extremely wealthy. While the top 5% of Americans account for more than half of all personal income tax revenues, through advantageous arrangements wealthy taxpayers frequently are able to avoid paying anything but a token amount of taxes on their capital incomes. The payroll tax and sales and excise taxes take a much bigger share of disposable income from middle and low income Americans than from wealthy Americans, according to the Institute on Taxation and Economic Policy.¹

Meanwhile, our current approach to taxation continues to be justified under the erroneous assumption that

¹E.J. Dionne, Jr., "Low-Income Taxpayers: New Meat for the Right," *The Washington Post*, November 26, 2002, p. A29.

there is no other way than through supply-side tax incentives to stimulate new investments and create jobs.²

When business corporations, voluntary associations, or any other specialized social inventions become socially dysfunctional and create, rather than solve, problems for society, government is the instrument through which we overcome the problem, directly or through a restructuring of our institutions and laws. It is not in the nature of government to leave social vacuums unfilled.

Today, as a result of the maldistribution of ownership and income, we have reached a point where government itself is suffering from an acute case of functional overload. Public redistribution and efforts to control the economy have placed responsibilities on government that go far beyond its originally conceived and more normal functions of enforcing contracts, protecting property, suppressing violence and other-wise maintaining a just and peaceful society.

The mere shifting of centralized governmental activities to state and local levels totally ignores the underlying defects within our economic system that have engendered and exacerbated the growing wealth, income and power gap. Reorganization of the federal bureaucracy is a similarly futile palliative.

Capital Homesteading offers a solution, not an excuse for perpetuating or ignoring structural flaws in our major economic institutions. Behind Capital Homesteading is a philosophy of taxation³ and a carefully conceived strategy to remove gradually the tax system's present bias against property and property accumulations, on the one

²Under the current United States tax code, capital gains are given favorable treatment under the assumption that past savings are required to form new capital. Absent the speculative influence of the stock exchanges, capital gains are, in large measure, generated by corporations retaining earnings to finance new investment. This, in theory, increases the value per share which, when the shares are sold, generates a short- or long-term capital gain. This gain can then be used to finance additional new capital. To encourage new capital formation, and presumably create jobs for nonowning workers, capital gains are traditionally given favorable tax treatment, either a lower tax or no tax. Since the rich, by definition, control the vast majority of directly held corporate equity and thus the source of capital gains, favorable tax treatment of this source of income generates substantial tax breaks for the wealthy, thus exacerbating the wealth gap and the rigid stratification of society into a small minority of capital owners and a large majority of capital-less workers.

³The serious reader will find the justification and tax philosophy behind these Capital Homesteading reforms described in detail in the article, "Beyond ESOP: Steps Toward Tax Justice," by Norman G. Kurland, 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.

hand, and, at some point, to reduce the government's use of the tax system as an income redistribution mechanism, on the other.

The Purpose of Taxation

Any rebuilding of today's overly complex, inherently unjust tax system must start with the simple question, "Why do we have a tax system?" From the standpoint of Capital Homesteading, the answer is simple: to yield the revenue to pay the costs of a limited government, without damaging the incentives for maximum production of wealth and the broadest distribution of capital ownership. From this point, a whole new set of conclusions follow:

The bias in the present tax laws against property accumulations and property incomes should be removed. The bias in favor of redistribution, as a practical matter, must be more gradually phased out, as redistribution of income is supplanted with an effective program of redistributing future ownership opportunities. The tax system and federal laws generally should be restructured to encourage the creation, accumulation and the maintenance of property, its widespread distribution among all households, and the maximum generation of new wealth and improved technology within the free enterprise system.

Government should announce a target goal for the economy of a minimum floor of capital self-sufficiency for every household to achieve within the next thirty years. A national ownership plan, including new tax laws, would be launched to reach that goal, similar to the manner in which government assisted Americans in the building of our agricultural base through the Homestead Act of 1862.

The 160-acre ceiling made sense in distributing shares of our necessarily finite land frontier. The amounts that could be accumulated under the proposed Capital Homestead program, however, are limited only by our talent, our knowhow, our technological potential, and our ability to mobilize all our resources in building a new and more productive industrial frontier during the next several decades. Hence, in today's world, a target floor is more appropriate than a ceiling as the focus of government initiatives under a national ownership program.

An effective tax system would offer incentives for the enterprise system itself, as the principal source of wealth production, to become a more direct and efficient distributor of mass purchasing power for all consumers in the economy.

As the need for income redistribution and governmental intervention within the private sector lessens to an irreducible minimum, the functions and costs of government should drop progressively, eventually to the tolerable levels projected by the founding fathers. Instead of constricting private initiatives and production, as under today's tax laws, government under a soundly conceived national ownership strategy, would become the catalyst for stimulating expanded production of a more competitive free enterprise system.

Since the wealth necessary to cover the costs of government are products of private labor and private capital, taxes should be viewed as charges to consumers for essential services not available through the private

sector. Unlike other services, however, the buyer of public services is compelled to buy and the government will remain the sole seller, at least until these same services can be satisfactorily provided through the competitive enterprise system. This seemingly minor change in emphasis could open up some new ideas for privatizing (democratizing) government services and new opportunities for creative businessmen.

Direct or Indirect Taxation

Any tax blunts incentives, but a direct income tax on individuals is the least damaging, and, at the same time, places before the electorate the cost of government. User fees for government services, like camping fees and grazing fees, are also legitimate direct taxes. But sales taxes, value added taxes, payroll taxes, most excise taxes, and other indirect taxes are not just or economically sound methods for covering government spending, since they mask the spending patterns of public servants and elected officials from close taxpayer scrutiny and direct accountability.

Indirect taxes (including Social Security and unemployment taxes) also add to the costs of goods, thus shifting taxes to the consumer, reducing the competitiveness of U. S. enterprises and also our growth within the global marketplace. Taxes on property discourage new construction, improvements, and maintenance. But taxes on corporations are the most counterproductive of all forms of indirect taxes. The corporation income tax damages the corporation, an invention of man that is indispensable to the maximum production of wealth. To the extent return on investment is reduced, growth is stifled and the investment will go elsewhere.

But there is a more serious adverse and unjust effect of present corporation income tax laws flowing from the wide array of incentives the tax system now offers to the financing of industrial growth without the issuance of new equity instruments. The nondeductibility of dividends encourage the use of retained earnings or conventional borrowings for financial growth. (This is reinforced by tax subsidies, investment tax credits, tax exclusions and other loopholes to encourage investments in ways which make the rich richer.) By perpetuating exclusionary patterns of corporate finance, the corporation tax minimizes opportunities for all households to share in the growth opportunities of the economy.

Rates of Taxation

A growing number of tax scholars have argued that the case for progressive or graduated rates of taxation is uneasy at best.⁴ If redistribution of income (in contrast to redistribution of future ownership opportunities) is a form of direct discrimination against property, a progressive income tax is inherently an unjust tax, assuming one accepts the Kelso-Adler, rather than the Marx-Engels, version of economic justice.

But what about the poor? No more effective aid can be provided the poor than allowing them to share in the new job and ownership opportunities within a healthy

⁴Walter Blum and Harry Kalven, *The Uneasy Case for Progressive Income Taxation*, University of Chicago, 1953.

and growing private economy. The problem of those still too poor to share in the cost of government can be handled through tax exemptions or direct vouchers, or perhaps even the kind of negative income tax advocated by Nobel prize winner Milton Friedman.

Yet responsible citizenship is best served when everyone pays some direct tax. In an economy productive enough to provide a high standard of living for all households, which would be the long-range goal of economic decision makers, the cost of government would be minimal. Since government benefits should be equally accessible to each member of society, absolute justice would demand an equal per capita charge on all individuals, without regard to their income levels. But this, of course, is impractical at this stage of our economic history.

A more realistic and just tax today would be a flat or proportionate rate imposed on all directly earned and so-called "unearned" incomes above a poverty-level income for all taxpayers. A single tax rate would be administratively more efficient than a progressive or graduated tax. Ideally, the flat tax on individuals would cover all government expenditures each year, including welfare, defense, interest on the Federal debt, social security obligations, unemployment and all other current spending not covered by user fees. It could also cover the cost of health insurance premiums under universal minimum health care coverage, including health vouchers for the poor.

This will allow for the gradual or immediate elimination of regressive payroll taxes on workers and companies, making the economy more competitive. And it would help make government vastly more accountable and transparent to the electorate. If tied into a vigorous national growth and expanded ownership strategy, one could easily imagine future candidates for public office actually competing for votes on the basis of who could offer the best government services at the lowest flat rate. Each year's single direct tax rate could be adjusted up or down to provide sufficient revenues to avoid budget deficits and pay off government debt over time.

Under a progressive or graduated tax, on the other hand, political irresponsibility and waste is more easily tolerated. Many voters believe that the cost of increased government spending can be shifted to a tiny fraction of high-income individuals or fat cat corporations, and overlook the dangers of "printing press money" where there are sizable budget deficits. A flat tax would help raise the levels of economic sophistication of the taxpayers.

Another shortcoming of a progressive or graduated tax is that tax evasion and the search for tax loopholes by wealthy taxpayers increase as tax rates increase. And when inflation forces workers into higher tax brackets, pressures for additional pay increases add more fuel to the inflationary fires.

Resources tend to be misallocated under a progressive or graduated tax. Economic decisions become increasingly made, not on their economic merit, but on tax considerations. Thus, high tax brackets stifle growth and incentives to innovate and increase production, making all of society the poorer and less competitive.

Earned or Unearned Income

Under the Kelso-Adler theory of economic justice, the earnings from one's property in the means of production are morally indistinguishable from the earnings produced by one's skill or brainpower. Since they are both rewards directly related to their contributions to production, they should be taxed alike. And discrimination against property discourages investment and reduces society's overall productive capacity.

Karl Marx considered profits as income stolen from labor. Our tax laws that discriminate against property incomes reflect the same bias. But if capital is recognized as a producer of wealth, then capital incomes (whether distributed or undistributed) are legitimately earned by those who share property rights in that capital, the same as those paid for their skills and ingenuity.

The most serious problem with laws that discriminate against property incomes is that they hurt the poor more than they do the rich. Access to the full, undiluted stream of earnings from capital is a prerequisite for the financing on credit of broadened ownership opportunities and for more widespread distribution of profits as second incomes among today's nonowning citizens, including civil servants, many professionals, teachers, the military and the unemployable.

The only form of income that can properly be classified as unearned is that which is truly gratuitous and wholly unrelated to the production of marketable goods and services. Examples of unearned income, which should be included for direct taxation (once poverty-level incomes are exceeded) at the same rate as earned incomes, are: welfare checks, unemployment checks, social security checks, food stamps, gifts and bequests, gambling gains, and other gains not immediately converted into tax-free or tax-deferred individual capital accumulations, as described below.

Individual Capital Accumulations

As discussed previously, building capital self-sufficiency into every American household will not take place overnight. But once we establish a specific minimal level or floor for individual asset accumulations as a ten- or twenty-year goal to strive toward, it allows everyone to focus on the importance of property and the need to remove all institutional barriers to the broader distribution of ownership opportunities as expeditiously as possible. The floor of capital accumulations per household should represent the industrial equivalent of the 160 acres of frontier land that the federal government made available to its propertyless citizens under the Homestead Act of 1862. Thus the tax laws should be reconstructed to encourage the tax-free (or at least tax-deferred) accumulation of a "Capital Homestead" for all Americans over their working careers, consisting of a growing number of equity shares in the economy's expanding industrial frontier.

A tax-qualified CHA could be set up in the name of each individual, from birth, at a local bank to serve as his or her tax-free accumulator of capital. Shares acquired through ESOPs, CSOPs and CICs could be rolled over

into one's CHA account tax-free,⁵ as well as income-producing property acquired through tax-free gifts and bequests. Each individual's total acquisitions would continue to accumulate in a tax-free manner until the federally established capital self-sufficiency floor was reached. Thereafter, future accumulations would lose these tax privileges and become taxed at the current flat rate, thus discouraging grossly excessive, monopolistic accumulations of capital in the future. Upon death or when all or part of the assets are sold to increase consumption incomes, such tax-deferred assets would be taxed at the flat rate then prevailing. Fairness in the distribution of future ownership opportunities would mainly be controlled through the traditional IRS tax-qualification controls over discriminatory allocations and, more importantly, through the Federal Reserve Board's control over credit extended by commercial bank lenders to ESOPs, CSOPs, CICs and CHAs to foster growth of the private sector economy.

Under H.R. 462, the proposed Accelerated Capital Formation Act introduced in 1975 by Ways and Means Committee member Rep. Bill Frenzel (R-MN), this tax-free floor was set at \$500,000. Whatever the target amount, it should be set at a level that both fosters initiative and a desire for income independence for its owner, and it could be adjusted to rise with cost-of-living increases. To encourage the continued accumulation and retention of income-producing investments, and to discourage squandering, all tax-qualified accumulation trusts would be required to pay out all property incomes on a regular basis as second incomes to the owners, subject to direct personal income taxes.

The rationale behind permitting tax-free accumulations below excessively large wealth concentrations follows the principle that new capital formation and widespread capital accumulations should be encouraged, both for promoting economic democracy and for raising the standard of living for all citizens. Taxes on property slow down the capital creation and accumulation process. On the other hand, a direct tax on the incomes from already accumulated capital assets is simpler to understand, less harmful to investment and the care of property, and easier for tax authorities to administer.

Government Debt and Government Deficits

Since tax policy affects the size of the government's debt and government deficits in general, a few comments on the wisdom of debt and deficit spending policies are in order.

Under the influence of Keynesian economic concepts, the objective of many tax decisions since the early part of the 20th Century has been to cure inflation and unemployment. Keynes assumed the continuance of historic patterns of extreme maldistribution of capital ownership, and sought merely to fine-tune that malstructured

economy through the bureaucratic manipulation of government tax, spending, interest, and money-creation machinery. Structural reforms to our corporate ownership patterns were not part of Keynes' approach to the problems of unemployment and inflation.

In the Capital Homesteading strategy, however, the structural void left by Keynes is met head-on. Capital Homesteading would attack inflation and unemployment at the roots. The main thrust of this approach is to super-stimulate expanded rates of private sector capital investment, financed so as to broaden the base of equity owners in society.

The credit financing of corporate expansion must meet rigid standards of feasibility and must be repaid as a self-liquidating investment. New dollars flow directly into new productive capacity. In sharp contrast, government debt seldom, if ever, finances any production increases. Rather, it goes into nonproductive spending, war, and even into waste of human talent and natural resources. Government debt is therefore inherently inflationary. Even worse, when government spending is not matched with current tax revenues, the inflationary impact worsens. Funds must either be borrowed (thus diverting those same funds from productive investment in the private sector) or simply issued as printing press money.

From a standpoint of economic justice, government deficits make no sense at all. They cause inflation and are therefore a pernicious form of hidden tax on the public, most painful to the poorest members of society. A just tax system would work toward the elimination of future inflationary budget deficits and to curb further increases in the already bloated government debt. Better yet, a concerted effort should be made to begin to repay this debt.

Inheritance Policy

Under a national ownership strategy, inheritance policy should be restructured to discourage excessive concentrations of wealth and, in order to promote individual initiative and capital self-sufficiency, to encourage the broadest possible distribution of income-producing assets. Gift and estate taxes therefore should not be imposed on the donor or his estate (including assets accumulated within proposed Capital Homestead vehicles). Rather, taxation should be based on the size of the recipient's total accumulations after receiving the gift or bequest. If the value of the recipient's asset accumulations remain below the floor of capital self-sufficiency described above, no tax would be imposed on the newly acquired assets. Above that floor, a reasonable generational asset transfer tax (or a flat rate tax on "excess" Capital Homestead accumulations) would be paid.

Avoidance of Generational Asset Transfer Taxes

Above the targeted homestead accumulation floor, a generational asset transfer tax or the flat rate tax would be imposed on each new owner to discourage future excess concentrations of wealth and economic power when assets transfer from one generation to the next. This would replace the existing estate and gift tax systems. The generational asset transfer tax and flat rate tax could

⁵In 1984, Congress allowed for an analogous tax-deferred rollover of ESOP assets into an Individual Retirement Account or other qualified deferred compensation plan which a participant received in one lump sum. This was liberalized in 1992 to include incremental distributions rolled over into another qualified plan.

be avoided by distributing excess accumulations to others, including family members, friends, and employees, as long as their personal accumulations remain below the floor.

Integration of Personal and Corporate Income Taxes

The double tax penalty now imposed on corporate profits is becoming widely accepted as an unjust form of tax discrimination that should be eliminated. Some reformers are proposing to mitigate this problem through a highly complicated and arbitrary compromise that not only avoids the problem but worsens it. Instead of eliminating the double tax directly at the corporate level, they would permit a partial deduction for dividend payouts to the corporation and a redistribution oriented partial tax credit for shareholders. Hence, it neither restores private property in corporate equity nor does it promote expanded distribution of equity issuances. It merely makes the top 1% who own the majority of directly-owned outstanding corporate shares even richer.

Tax reform under Capital Homesteading would attack this problem directly with elegant simplicity. It would recognize that property and profits are inseparable and therefore all corporate net earnings, whether distributed or retained by the corporation, would be treated as earned by its owners and therefore should be taxable at the personal level, on the same basis as any other direct income. Under this alternative, the corporation would be treated for tax purposes like a partnership, with its business expenses (including depreciation and research and development) attributed and deductible at the enterprise level and all capital incomes attributed individually according to each owner's proprietary stake in the business. To encourage more equity financing of corporate growth, higher dividend payouts must be encouraged and alternative low-cost credit sources for financing must be made available to expanding and viable new enterprises.

Capital Gains Taxation

How to tax capital gains is a continuing source of much of the complexity and confusion that now plague our tax laws. How would a property-oriented Capital Homestead policy handle this problem?

First, it would restructure the tax laws to encourage investment and discourage speculation. At least for non-wealthy individuals it would add disincentives to gambling in high-risk securities and the commodities market. Tax laws would be designed to facilitate the acquisition, accumulation and retention by today's capital-deficient Americans of long-term investments, held mainly for their potential of yielding high, steady, and relatively secure second incomes to supplement their paychecks and retirement checks in the future.

As under present law, to the extent capital gains income results from short-term purchases and sales of commodities and securities, realized capital gains should be treated like any other kind of direct personal income. Such capital gains are no different than the purchase and sale of any other goods for a profit, or for that matter, gambling gains.

Capital gains from long-term holdings deserve different treatment, however, under a national strategy to broaden the base of capital ownership. As recommended above, to the extent that investments are accumulated within a tax-qualified vehicle, the gains should be permitted to increase tax-free or tax-deferred, until the individual affected reaches a targeted floor of capital self-sufficiency. Above that level capital gains would be subject to normal taxation after indexing for inflation.

If all of the proposals recommended here were adopted, the capital gains problem would gradually disappear. Much of the appreciation in the values of corporate common stock can be traced to the retention by management of earnings for meeting their capital requirements. As dividend payouts increase (encouraged by tax-deductibility of dividends at the corporate level) and as new sources of equity financing become readily available through the discount mechanism of the Federal Reserve System, the value of individual shares would tend to stabilize over time and be based on current and projected dividend yields per share. Hence, long-term capital gains would be less a source of future government revenues.

To some extent, long-term capital gains result, not from the increased productive value of the underlying assets, but from a gradual debasement of the American currency. Inflation-inducing government economic policies can be blamed for these artificial increases in profits and capital values. Except where prices increase from natural shortages, government should assume total responsibility for inflationary increases in the value of investments. Therefore capital gains taxation should always be inflation indexed to see if any gains in value actually exist.

State and Local Tax Systems

Today, a heavy portion of local revenues come from the taxation of property, thus discouraging investment and improvement of industry and residential property in their areas. Sales taxes also increase price levels, encourage tax evasion by local merchants, discourage trade, and generally can cause one area to become less attractive than another. Since high production, high incomes, and a higher quality of life rest on the quality of the structures, industrial equipment and facilities, and technology available to the residents of an area, it should be obvious that taxes on local property are counterproductive and should be gradually supplanted with a universal system of state and local taxation based upon the direct incomes of its residents from whatever sources.

Thus federal tax policy should create additional incentives for state and local taxing authorities to gradually shift to direct flat rate income taxes at the individual level, for the same reasons outlined above. To simplify tax collections, the state and local rates could be set at a percentage of the federal taxable incomes of residents of the area. Another advantage of this approach is that all areas of the country would become tax-neutral for investment purposes, thus increasing the nation's overall efficiency in the allocation of our manpower and other resources.

Tax Simplification

Although corporate income tax returns would still be important for disclosure purposes and for corporations unwilling to pay out their earnings fully to their stockholders, most of the tax revenues would flow from the expanded personal tax base. The personal income tax return and the tax system itself would, as a result, be enormously simplified and easier to understand. A simple one-page personal income tax return would be well-received by the American taxpayer.

Most personal deductions and tax credits could be eliminated under a flat-rate tax system, restoring the neutrality of the tax system over people's consumption choices. Personal exemptions, however, could be raised to the poverty level, so that the poorest families only would pay no taxes, including payroll taxes. But by filling-in a simple annual income tax return, a poor family could qualify for a negative or reverse income tax (or refund) as proposed by the conservative economist Milton Friedman.

Detailed Tax Reforms for Implementing Capital Homesteading

Sound tax policy recognizes that government does not produce wealth, and that every subsidy originates with those whose productive labor and capital actually produce marketable goods and services. It also recognizes that wealth is produced most efficiently within competing privately owned enterprises vying to satisfy private consumer demand, with every buyer voting with his or her own money to reflect a choice among available goods and services.

How then could the tax system be restructured to achieve responsible, sustainable and fair fiscal policy, while encouraging the objectives of Capital Homesteading?

1. Replace the graduated tax on personal income above the poverty level with a single flat rate on income from all sources, whether "earned" or "un-earned," including employment and property incomes, interest, dividends, inflation-indexed gains from sales and exchanges of property, unemployment compensation and welfare, social security and pension incomes, winnings from gambling, gifts and bequests [that are not reinvested or exempted by the "Capital Homestead Exemption" described below], etc.⁶

2. Exempt all household incomes of the genuinely poor by excluding from the flat rate tax all incomes

⁶Note the radical departure of this "poor man's flat tax 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 flat 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 come from a flat tax.

below \$10,000 per adult household member and \$5,000 per dependent child.

3. 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 protect the property rights of current owners;

- (b) All incomes channeled by businesses or individuals into dividend and patronage distributions or into the financing of business growth or transfers of equity ownership through employee stock ownership plans (ESOPs), Capital Homestead Accounts (CHAs), community investment corporations (CICs), pension plans, Keogh plans, or other IRS-"qualified" expanded ownership investment vehicles, but in no case where such amounts cause the accumulations of individual beneficiaries to exceed the "Capital Homestead Exemption" described in paragraph (13) below. These "savings" could be treated as tax deductible by either the businesses or individuals that make them; and

- (c) charitable contributions, with appropriate limitations to encourage expanded capital ownership and discourage monopolistic accumulations and control overproductive assets;

4. Eliminate:

- (a) the tax penalty on married couples;

- (b) tax credits;

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

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

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

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

5. 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.

6. Convert Individual Retirement Accounts (IRAs) into Capital Homestead Accounts (CHAs) as a mechanism for enabling all individuals to accumulate income-producing assets on a tax-deferred and/or exempt basis and permit CHAs, like employee stock ownership plans, to be used for acquiring corporate shares on credit secured and repaid with dividends deductible at the corporate level. Gifts or bequests to CHAs, ESOPs, and other

ownership-expanding vehicles could be made tax-deductible for income and estate tax purposes, as they are today for tax-free foundations.

7. 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.

8. Only allow exemption of capital gains from taxable personal income, to the extent that:

(a) 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; and

(b) 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. CHA, ESOP, etc.) but not exceeding the "Capital Homestead Exemption" listed in paragraph (12) below.

9. Avoid double and triple taxation by maintaining a tax on corporate net earnings but allowing corporations to avoid taxes on earnings they (a) pay out as dividends, cash productivity bonuses, ESOP and profit sharing contributions, purchases or debt service payments on replacement assets, patronage refunds, etc.; or (b) retain for research and development or (c) use for working capital.

10. Allow ordinary business expenses, like wages, to remain deductible at the corporate level 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 on all corporate shares, thus permitting stockholders to purchase newly issued corporate shares with profits deductible both from corporate as well as personal earnings. In the alternative, employees through ESOPs, and other shareholders through CHAs, CSOPs, CICs, etc., could use these tax-deductible dividends to repay loans for the acquisition of larger blocks of stock on a leveraged basis.⁷

(c) Increasing the ceiling on 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.

11. Liberalize depreciation rules by allowing full first-year deductions on all purchases of replacement assets (to maintain existing levels of capital productiveness, profits and property rights of existing owners).

12. Allow the tax advantages of a leveraged ESOP to be extended to all taxpayers through IRS-qualified Capital Homestead Accounts (CHAs), to utility customers under consumer stock ownership plans (CSOPs), and to citizen-shareholders of State and local Community Investment Corporations (CICs) for developing local land and natural resources.

13. Integrate with the Social Security System a tax-deferred "Capital Homestead Exemption" to encourage every man, woman, and child to accumulate through Capital Homestead Accounts, ESOP rollovers, Keogh Plans, IRAs, gifts, bequests, savings, etc., a personal life-time estate of wealth-producing assets, tax-sheltered up to \$750,000, including up to \$250,000 for one's equity in his primary residence. This reform would be targeted to provide all Americans with growing property incomes and direct ownership participation in the competitive free enterprise system. Such an estate would provide the same degree of income self-sufficiency and economic security for a family as the 160 acres of productive farmland granted under the original Homestead Acts.

14. Eliminate all contribution limits on "savings" through CHAs, ESOPs, IRAs, Keogh Plans, etc., until individual accumulations exceed the proposed Capital Homestead Exemption.

15. Provide an existing owner with a tax-deferred 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 by the seller 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.)

16. Permit an ESOP, CHA, CIC, or other ownership-expanding mechanism 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.

17. 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 designated urban and rural areas combined with widespread participation among residents in the

⁷The tax-favored payout of corporate dividends advocated here *should not be labeled "tax subsidies,"* any more than deductible wage costs are "subsidies" to employers. Tax-deductible profit distributions under Capital Homesteading 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.

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ownership, profits, and appreciated real estate values that would otherwise flow exclusively to outside land speculators.

18. Absorb the annual cost of the Social Security System entirely within the single flat rate income 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 eventually reduced as they are replaced by Capital Homesteading incomes.