Explanatory Notes

What Capital Homesteading Would Mean to the Average American

Projected Tax-Sheltered Wealth Accumulations and Pre-Tax Income Under Capital Homesteading

The schedule showing the potential asset accumulation by a "Capital Homesteader" is based on a number of specific assumptions that are listed below. These assumptions proceed from a defined set of principles underlying the Capital Homestead Act, a macro-economic application of a justice-based, free market paradigm called "the Just Third Way." As understood within this new framework:

• Using the legal definition of money as "*anything* that can be accepted in settlement of a debt" (as opposed to merely government-issued currency and commercial and central bank demand deposits), the money supply is backed with loans made to finance private sector assets instead of government debt. All such loans would be collateralized with capital credit insurance and reinsurance instead of traditional forms of collateral, and would be non-recourse to the borrower.

• The money supply is consequently "elastic," expanding and contracting directly with the needs of the economy, instead of in response to political needs or the best guesses of officials as to the amount of money that is needed. Money is created when financially feasible capital projects are brought to a commercial bank for financing and a loan is made, and cancelled when the loan is repaid. Thus, instead of requiring that lending come out of existing or "past" savings, new capital formation can be (and under Capital Homesteading is) financed using "future" savings.

• The role of the Central Bank changes from monetizing government debt to meet political needs, to monetizing private sector assets to meet economic needs. In practical terms, the Central Bank would no longer first create money, which inflates the price level as holders of money seek out existing investments. The Central Bank would, instead, only create money in response to qualified loans made for financially feasible investments previously vetted as sound by commercial banks and capital credit insurance providers, thereby avoiding both inflation and deflation.

• To promote economic justice and efficiency in the monetary system, full production, full ownership, a stable currency, sustainable growth, productiveness of land, natural resources, technology, infrastructure, and economic institutions, the Central Bank would only rediscount productive loans that promote full ownership.

Assumptions

1. Accumulation Beginning at Birth. Each citizen would become eligible at birth, or "Age 0," to begin receiving an annual capital credit allocation, *i.e.*, the right to obtain credit and have a commercial bank create money for the purchase of newly issued qualified Capital Homesteading Shares.

2. One-Time Discount Rate (Assumes Immediate Rediscounting at Central Bank). The money for Capital Homesteading is created *after* a financially feasible sound capital investment is properly vetted and new equity shares issued. Since the new money is based on the concept of "pure credit" money that is totally free of "past savings" of the rich or many small savers, the loan will be interest-free. Instead, a commercial bank imposes a service fee in the form of a discount off the face value of the loan. The borrower receives a portion of the loan proceeds, while the bank is repaid the full amount. This links all new money creation directly to an increase in marketable goods and services in the amount of the present value of the newly financed growth assets that will produce the marketable goods and services, thereby avoiding both inflation and deflation.

3. One-Time Initial Risk (Capital Credit Insurance) Premium. Currently, a commercial bank sets its discount rate so as to include a "risk premium" set by the experience that bank and others have had with a particular class of borrower and the collateral offered. When capital credit insurance and reinsurance replaces traditional forms of collateral, this risk premium can be separated from the discount rate and used to make a premium payment on an insurance policy, pooled with other premiums to cover the risk that the borrower may default on the loan.

In their paper, "The Equity Premium Revisited," Bradford Cornell, Robert Arnott and Max Moroz (as reported in www.cxoadvisory.com, the website of the CX Advisory Group, accessed November 14, 2013), concluded that "evidence from the most credible models of the historical U.S. equity risk premium converge to an annual value in the range 4% to 4.5% during 1872-1950 and 1951-2008." An equity risk premium of 4.5% was selected as being the most conservative. This is an average, and will vary according to the actual risk for a class of investment. It will be substantially lower for low-risk investment, and higher for high-risk investment. Some investments may be too risky to qualify for "pure credit" Capital Homestead financing, and will have to resort to existing accumulations of savings.

4. Annual Capital Credit Allocation. The amount of the annual capital credit allocation was conservatively estimated by taking slightly more than $2 trillion as the total amount of new capital formed in both the public and the private sector in recent slow growth years, and dividing it equally among the estimated total U.S. population.

5. Term of Acquisition Loan in Full Years. The loan term was calculated to ensure that the estimated annual debt service would not exceed projected annual income generated by the shares purchased with the proceeds of the loan.

6. Pre-Tax ROI. Target after-tax ROI ("Return On Investment") has historically been between 9-12% for a conservative mutual fund. Given the tax deduction of dividends at the corporate level (as with ESOPs under current law), the companies issuing shares would escape from paying the *cir*. 35% federal corporate tax rate as well as state corporate income taxes. This translates into 14-18.50% ROI. ROI of 15% was chosen as most conservative.

Calculations from Assumptions

7. Commercial Bank Discount Amount. This is the dollar amount of the 2% commercial bank discount rate. It is not necessary to consider the Central Bank rediscount rate, as this does not concern the Capital Homesteader, being a separate transaction between the commercial bank and the Central Bank.

8. Capital Credit Insurance Premium Amount. This is the dollar amount of the 4.5% risk premium.

9. Cash Available to Homesteader Each Year to Purchase New Shares. This is the dollar amount that each Capital Homesteader would have available for the purchase of newly issued equity shares.

10. Annual Earnings Per Loan. This is the amount of dividends that would be received by the Capital Homesteader, assuming that dividends are tax-deductible at the corporate level and all earnings are paid out in the form of dividends, first tax-sheltered along with the shares in a CHA or ESOP trust and taxable to the Capital Homesteader when distributed.

11. Payback Period (In Years). This is the total amount of each individual loan divided by the amount of debt service for a single loan. This indicates the number of years needed to repay the loan in full.

12. Annual Payment of Principal per Loan. This is the total amount of the loan to be repaid divided by the term of the loan.

Capital Homesteading Wealth Accumulation Projections

A. Age. This is the age of the Capital Homesteader, beginning at birth, or "Age 0."

B. Homestead Accumulation. This is the total amount that the Capital Homesteader will have in a Capital Homestead Account at that age.

C. Annual Earnings. This is the "Homestead Accumulation" multiplied times the "ROI" to give the annual income received by the Homesteader.

D. Debt Service Payment. This is the amount to be paid each year on the acquisition loans. At first, the payments consist of the full stream of income until the loan is repaid, at which point the Capital Homesteader will enjoy the full stream of income from the assets purchased with that loan to use for consumption. This amount has been capped at the amount of the annual capital credit allocation to ensure that the amount applied to debt service in any one year does not exceed the actual debt incurred in that year in order to prevent the diversion of consumption income into reinvestment.

E. Acquisition Debt Balance. This is the outstanding debt that the Capital Homestead has during any one year.

F. Annual Net Income. This is the total amount received by the Capital Homesteader after making all debt service payments.

G. Aggregate Dividends. This is the amount received by the Capital Homesteader in dividends, assuming full payout of dividends that are tax-deductible at the corporate level.