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The Man Who Would Make Everybody Richer

EVEN in an age that venerates heresy, the iconoclastic philosophy of Louis Orth Kelso outrages many a professional economist. "A crackpot theory," argues Money Expert Milton Friedman. "Instead of saying that labor is exploited, Kelso says that capital is exploited. It's Marx stood on its head." Replies Kelso: "Damn right—and what's wrong with that?"

Kelso, 56, a highly successful San Francisco corporate lawyer, author and sometime economist, insists that economic ideologists as diverse as Karl Marx and John Maynard Keynes have been wrong. They have overstressed one factor—the role of labor—in the production of industrial wealth. Kelso holds that "the second factor," capital, is increasingly more important than labor because both technology and modern management aim at saving labor.

The U.S. economic system is in trouble, Kelso insists, because 5% of the population owns the capital—money, securities, land and tools—that produces about 90% of the wealth. This means that the rich grow richer while the bulk of U.S. workers are denied an opportunity to obtain a worthwhile share of the nation's abundance. What Kelso wants to do is turn 80 million workers into capitalists through a complex maneuver that would enable almost everybody to buy blue-chip stocks with borrowed money and ultimately enjoy a "second income" from the dividends.

The Closed Frontier. Kelso's idea has elicited increasing debate lately among bankers, corporate executives and officials of several governments. Venturesome companies have used some of his methods to shift ownership to their employees. Early this year, Alberta, Canada's historic haven for economic experimenters, began a formal study of Kelso's entire doctrine. Last week, as he has for more than a decade, Kelso hopped across the U.S. expounding the merits of his "universal capitalism." In Chicago, he met with a group of insurance men. In Washington, he dined with five Republican Congressmen, two Administration aides and Elliot Richardson, the incoming Secretary of Health, Education and Welfare. At week's end Kelso flew to Stanford University to give a lecture to executives of 13 California companies.

The Denver-born son of a poverty-plagued musician, Kelso developed his theories partly from his own struggle to make a living. He went to work when he was in the ninth grade and drove a dynamite truck to earn his way through the University of Colorado, from which he holds degrees in both finance and law. He grew interested in economics, he says, "by brooding about the absurdity of the Depression." While stationed in the Canal Zone as a Navy intelligence officer during World War II, he wrote a 600-page manuscript propounding his views. It lay in a closet for 15 years, until Philosopher Mortimer Adler, intrigued by a conversation with Kelso, asked to read it. Adler was so fascinated that he collaborated with Kelso on *The Capitalist Manifesto*, published in 1958; it has since sold 50,000 copies. To further his reform cause, Kelso later started in Washington the Institute for the Study of Economic Systems. Last year he gave the institute $52,000 from the six-figure income that he draws as senior partner in Kelso, Cotton, Seligman & Ray, one of San Francisco's ten largest law firms.

In his latest book, *Two-Factor Theory: the Economics of Reality* (co-authored by Patricia Hetter), Kelso maintains that the American system is "coming apart" because of its "defective financial and economic framework." One of his most potent arguments is historical. Until the close of the frontier, even the poorest laborer could acquire capital virtually free, in the form of land. "That opportunity motivated the building of the most powerful economy on earth," declares Kelso. Now that the free land is gone, he contends, the U.S. seems to have forgotten that "property is the only power capable of protecting the individual's political freedoms and rights."

ROBERT ISAACS

KELSO LECTURING AT STANFORD
Dividends and drawbacks.

Homesteading with Stocks. Kelso calls for a kind of Homestead Act that would make stock, rather than land, available to people who lack the cash or credit to buy it. He envisages creation of a federal agency to insure "capital diffusion loans," much as the Federal Housing Administration insures mortgage loans. He would empower banks to borrow funds directly from the Federal Reserve for such lending.

The plan might begin by helping the poor and unemployed. An eligible borrower would go to a bank and obtain, for example, $4,000 a year for five years (or $20,000 all together) to buy stock in corporations. The bank, protected against loss by the Government insurance, would put the money in escrow; a trust officer would buy a diversified portfolio of dividend-paying shares. Kelso figures that the stocks would ultimately pay for themselves through dividends. Thus the borrower could pay off the loan, then own the stocks outright and enjoy a dividend income from $20,000 of capital.

Raising the Dividends. At present, a $20,000 portfolio of high-grade stocks generally pays about $1,000 a year, or 5% in dividends. But Kelsonian economics calls for a return of at least 20%, or $4,000 a year—a level that Kelso figures could take 5,000,000 families off the welfare rolls in five years. To increase the dividend payout, Kelso would gradually abolish corporate income taxes and require companies to distribute all of their earnings to stockholders. Kelso maintains that the Government's revenue loss would be temporary and bearable. One reason is that rising personal-income-tax collections would greatly offset the gradual decline in corporate tax take. He also foresees a decline in Government expenditures for welfare and "make-work" activities—subsidies for uneconomic farms, dubious construction and military projects—that, by his estimate, now occupy one-third of the U.S. labor force.

The benefits of the plan would spread to middle-class workers in two ways. First, Kelso estimates, the funds for capital investment through increased stock sales would support economic expansion at hitherto undreamed-of rates of perhaps 15% or 20% a year, creating a great demand for labor. Second, companies would be tempted to adopt Kelso's plan voluntarily, partly because of a quirk in tax laws. For example, if Beneficial Paper Co., with 1,000 employees, wanted $20 million to build a factory, it would issue $20 million worth of new common stock. An employee-owned trust, set up somewhat like existing pension and profit-sharing trusts, would buy the shares with money borrowed from a bank. Here the tax quirk comes into play: the company could agree to make tax-deductible contributions to the trust to enable it to repay the loan; if the company itself borrowed the money from the bank, the loan would have to be repaid in after-tax dollars.

Without corporate income taxes, the dividends from the employee trust's investment ought to average $4,000,000 a year, says Kelso, enabling the trust to repay the loan in five years. After that,

each of Beneficial Paper's 1,000 employees would not only own $20,000 worth of stock but would also have a second income of $4,000 a year.

Some companies have already set up tax-sheltered trusts that allow their workers to become stockholders on credit. When the employees of San Francisco-based First California Co. found that the investment banking firm was for sale, they converted their profit-sharing plan into a stock bonus trust. The trust used its cash, plus a borrowed $1,000,000, to buy F.C.C.'s common shares, pledging the assets of the company to secure the loan. Within 2½ years, the trust repaid the loan out of company profits. In similar fashion, employees used a Kelso-devised fund to buy Peninsula Newspapers, Inc., of Palo Alto, Calif.

Unbottling the Genie. Like any adventurous idea, Kelso's plan has drawbacks. Critics argue that even if Congress could be persuaded to change the necessary laws—a big if—his second-income plan would merely be a substitute for today's Government redistribution of wealth through taxes, welfare, give-aways and make-work programs. Another difficulty is that Kelso concentrates on the manufacturing sector of the economy, noting that greater capital investment would lead to more productivity. But he tends to play down the rising importance of the economy's service sector, in which productivity growth is slow and cannot be rapidly expanded by capital investments.

Present stockholders might logically object that issuance of so many new shares to finance plant expansion would dilute their equity in corporations. Kelso notes, however, that stockholders' proportional share in the old assets of a company would remain the same; only the new wealth created by expansion would be spread widely among the new shareholders. To be sure, if Kelso's plan were widely adopted, the stock market might lose its lure as a casino. Reason: investors would have much less incentive to gamble on rising stock prices and much more inducement to invest for steady income. Kelso expects that his plan would smooth the gyrations of stock prices. Even in a bear market, he argues, the public's appetite for new shares would hardly diminish because investors would not be risking their own savings to acquire stock. And he figures that people who own stock as a source of second incomes would be apt to retain it as long as corporations avoid large cuts in their dividends.

Despite the flaws, Executive Vice President Walter Hoadley of the Bank of America calls Kelsonian theory "a forward-looking concept designed to preserve our enterprise system." Kelso himself seems convinced that his time has come. "I let the genie out of the bottle, and it's not going back," he says. "What did the French College of Surgeons call Pasteur? A mere chemist. I think that I am the Pasteur of finance."