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An IBC Tax Strategy Part I

By L. Carlos Lara

It's been said that people would rather die than think. But I am going to see if I can incentivize you do just that by showing you a way to fund a large Infinite Banking Concept (IBC)-type life insurance policy, while using cashflows that are dedicated to paying your taxes. I should say upfront that this discussion will make sense immediately to business owners, but I hope that salaried individuals see relevance to their households as well. Now in order to provide this intriguing maneuver a fair disclosure, I will need to do it in two parts. In this first part, I will lay the groundwork, and then in next month's article I will provide some numerical illustrations to show exactly what I mean.

Let me be perfectly clear that my discussion *does not reduce your tax liability*. This is not about "finding a tax loophole." Rather, I am pointing out one option that people with large cashflows—such as business owners who annually make a large expenditure to the IRS—have, if they've been convinced that obtaining a well-funded IBC-type policy is a good idea.

As my remarks indicate, this idea isn't really about "paying taxes" per se; it would work for any recurring expenditure that is of a comparable size, year after year. I personally use this strategy for my own taxes, and that's why I'm choosing this particular approach to relay the idea.

As I said above, my discussion will resonate most with business owners.[1] There is an important reason for this. Business owners have a unique distinction that employees on a fixed income do not have. This main difference is the ability to create "windfalls" through either profits or from the sale of business assets. This can include the selling of the entire business itself as a final exit strategy at some time in the distant future. So if you are a business owner and operate an LLC or a corporation this idea is tailor made for you.

Before we go further, let me also stress that this is not to be construed as formal tax or investment advice. The ideas presented here are only thinking exercises. In fact, we recommend that you discuss these ideas with your own personal tax, investment or legal advisor. Who knows, you could be teaching them something they have never heard or thought of before and they might be very grateful to you for having shared it with them.

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Finally, this article assumes you are either an owner of a well funded dividend paying Whole Life insurance contract from a mutual or mutual holding company that has been properly designed according to Nelson Nash's *Infinite Banking Concept (IBC)*, or at the very least that you have studied the concept and are in discussions with someone from the Practitioner Finder—people who have passed our training course. (They can be found at: www.infinitebanking.org/finder.) This is an absolute requirement. The reason for this is because it is not possible to fully grasp the financial implications discussed here until one has become an owner of such an insurance contract and has been practicing IBC in their own life. So clearly the ideas discussed here are not for the novice.

If you are reading this and do not yet own one of these contracts don't let that disappoint you. You will still benefit from the various points being made in this article. I encourage you to read on and learn. You may well become motivated enough to actually get one of these important insurance policies to practice this strategy for yourself. Either way I will be sure to list several resources in the references section of this article that will help you continue your educational journey.

INSIDE THE IBC SPECIALLY DESIGNED POLICY CONTRACT

As every practicing owner of an IBC insurance policy knows, these are designed to facilitate use of the "living benefits" available to any policy owner, which allows the policy to be a financing instrument. However the death benefit is the core element of a life insurance policy, and understanding its value as an asset will be essential to my analysis. The financing function is made possible because the owner can take out policy loans with the surrender value of the policy serving as collateral; this is a legal right that is provided to all policy owners and is spelled out in the language of the insurance contract.[2]

If you should obtain such a loan this is what actually happens in layman's terms. The life insurance company is advancing you a loan, at a contractually specified rate of interest. Your policy continues to "grow" on its own strength, however, and in a sense that internal growth partially compensates for the interest on your policy loan. In addition to the guaranteed growth, a payment of an annual dividend is also made into the policy. Although the dividends are not guaranteed you should know that mutual companies have historically paid dividends virtually every year for as long as these companies have been in existence, except on a few isolated occasions. This historical evidence for many of these companies spans a period of over a hundred years, even right through the period of the Great Depression of the 1930s.

So long as the earnings do not exceed the cost basis in these policies the total of these two quantities (the guaranteed growth and dividends paid) are accumulated inside the policy tax-free. Consequently, their tax *equivalent* amounts (depending on the tax racket of the policy owner) help reflect their true earnings inside the policy. For example, an earned interest rate of 3% inside the policy (without adding the annual dividend) and with no federal or state income tax attributed to it, is equivalent to approximately 1.25% to 2% additional interest earned depending on the policy owner's tax bracket. When you add the tax equivalent dividend to this amount you get an even higher return. A tax equivalent calculator obtained from the Internet can help you analyze this.[3]

But I don't want you to merely look at the growth in the "cash value" of the policy, treating it as if it were a money-market account. No, remember that this is a *life insurance* policy. When these dividends are automatically reinvested they purchase additional, paid up death benefit coverage. In a sense this is generating equity in the policy as a result of this increase. This is an immensely important component that is immediately noticeable when reviewing a year-end annual report on these policies. A simple comparison of the increased death benefit against the cash values and the policy loans outstanding each year reflect this equity increase. In other words, the

result is an ever-increasing asset (the death benefit) that resembles a prime piece of property with a value that never declines. This higher death benefit is critically important at the death of the policy owner, especially in the case where there are numerous loans outstanding.

Interestingly, the increased death benefit each year caused by the reinvestment of the dividends in order to purchase more insurance actually forces the payment of an even larger dividend payment into the policy the following year. This happens on account of the policy's set trajectory to have the cash values ultimately equal the death benefit by the policy owner's 121st year. The beauty of all of this is that all of these moving money parts occur in clockwork precision like gears that shift by themselves. It is literally that mechanical. Yet these self-loading and self-firing actions within the policy produce impressive results.

Meanwhile the lent money to the policy owner is usable for any expenditure on a taxfree basis since it is borrowed money and not income. What the policy owner has given up in exchange for the use of this tax free money (until he repays the loan) is a collateral assignment in the cash values of the policy up to the amount of the indebtedness. When the policy owner repays the loan and the interest charge on it, the collateral held by the company is released and additional borrowing capacity for the policy owner is increased by exactly the same amount.

In a sense, you can think of your policy as chugging along, doing its own thing, while the life insurance company makes you a loan "on the side," with money it takes out of the general pool, not directly "out of your policy." Now to reiterate, they charge you an interest rate on this loan, just as they insist on earning a return on other investments they might make. But it's helpful to know exactly what the mechanics are of policy loans, and how they differ from (say) taking money out of your checking account or selling off a portion of your 401(k) in order to make a large purchase.

THE IDEAL WAREHOUSE FOR OUR WEALTH

One thing we should not overlook is that when you make your first premium payment to the mutual company you immediately become a partial owner of the company, a very important fact. (In contrast, a stock insurance company has stockholders, who may not be the same people as its policyholders.) At that exact point the company becomes totally responsible to pay your beneficiary the death benefit in your insurance contract if you should drop dead later that same day. But it also does something else. The insurance company now becomes responsible, and it guarantees this responsibility by the financial strength of the company, to distribute a portion of its profits to you in the form of dividends. This happens so long as you remain an owner of the company by continuing to make your premium payments.

The premium payments you make are always made payable to the insurance company in care of your name and policy number assigned to your contract. Those premiums as well as the millions of dollars in premiums made by other policy owners are invested by the company. It's noteworthy that these investments are mostly in loans to highly reputable institutions like the government and highly rated corporations. These investments earn an interest income that translates into company profits. The investment fund that is earning this interest income is often referred to as the *general pool* or investment portfolio of the company.

All monies sent to the insurance company by policyholders goes into this general pool. Even when you deposit additional money into your PUA Rider,[4] a feature of all specially designed IBC policies, you make your check payable to the company in care of your name and policy number associated with your contract It's exactly the same procedure that is used when making the premium payments, the only difference is that you direct the company as to the placement and posting of this money. In like manner, the same thing happens when you pay back a loan and its interest. This is why so many IBC practitioners feel as though the use of IBC with a dividend paying Whole-Life policy from a mutual company is like owning one's own private cash flow

system.

But what should really be coming into focus as you think through this is the idea of a *ledger* with your name on it as well as the policy contract number. Keep in mind that the actual money associated with your ledger is not there but safely housed in the investment portfolio (the general pool) of the company and is working for your benefit as an owner of the company. All this money must keep working if the company is to make a profit.

When you take out a policy loan it is taken out of that general pool of the company earmarked for loan investments. In other words, at your request the company is now making an investment in your loan as opposed to someone else's. As you can see this keeps the money working and is doing so for the benefit of all the owners of the company including you. But the company is actually granting the policy owner a loan from this general pool. Simultaneously, an assignment in the cash values of the policy owner's particular policy has been taken as collateral by the insurance company.

This action by the company is not only representative of good accounting that keeps the books straight, but at the same time it also allows for the enormous cash flow flexibility afforded the policy owner by having borrowed from his own system. This financing flexibility inherent in these specially designed policies, which we are about to identify, is what makes possible the strategy we are discussing.

THE BIG THREE COMPONENTS THAT MAKE ALL THE DIFFERENCE

The best way to see this important difference is to think comparatively as you study each of these three components carefully. Think about money borrowed from other sources and money paid to other sources that are different from the insurance contract system we are describing. Also think about what you may have to give up in exchange every time you take these actions with those outside sources. Think about commercial banks, finance companies, credit cards and even qualified plans. Think about shopping at your local Costco, the grocery store, the shopping mall and similar places where you don't borrow money at all—you just pay cash.

Now let's first look at these three components in the form of statements and then I will comment on each one where hopefully the impact of what I am revealing will become clear.

Number One—Access and Control Over Your Money: If you have cash value in your policy you have a contractual right to policy loans.

Number Two—Flexibility of Repayment Terms: You can pay back the policy loans on your own terms or even not at all if you wish.

Number Three—Uninterrupted Compounding Of Your Money: Whatever amount you borrow that same amount continues to earn money in the form of interest, dividends, and equity in your policy as long as you live and as long as your policy remains in force.

THE IMPORTANT ANALYSIS

With regards to the Number One Statement, this is a most powerful benefit. I have been a business consultant to corporations for forty years and have observed a noticeable business management pattern when it comes to borrowing money. If you only knew how many individuals, especially business owners, often have to borrow money from a bank or a credit card just to be able to pay their taxes, it might be easier for you to recognize how powerful this benefit really is. Banks and credit cards are not the best sources for borrowing money, yet needing to pay taxes on time is always a priority. In fact it is a downright necessity and yes, people will go into debt to pay them. This is because the consequences of not paying taxes can be quite severe.

But with a well-funded policy so long as you have unencumbered cash value in the policy the insurance company, by the language in its contract, is willing and ready to grant you a policy loan.[5] Furthermore, there are no credit checks, no extensive forms to fill out, no questions about what you are going to use the money for, or how you plan to pay it back when

requesting a policy loan. You just simply ask for the money and it's mailed to you or deposited directly into your account in about 3 to 5 business days, sometimes sooner.

As to why a policy owner has the absolute authority to repay the loan strictly on his own terms, as stated in point Number Two, the answer may surprise you, but it actually makes logical sense. Recall that when insurance companies invest policy owner premiums in very safe fixed income assets such as U.S. Treasuries or investment grade corporate bonds they are actually lending money to these institutions. These investments, as we said earlier, are loans.

But policy loans to a policy owner are a better (literally *risk free*) investment than bonds as far as the insurance company is concerned. They actually have more control over a policy loan than they do over bonds since they actually control and guarantee the cash value, which is the collateral. Since policy loans never exceed their cash values and unpaid principal amounts may be deducted from cash surrender or policy death proceeds, the safety of principal associated with policy loans is absolute, from the life insurance company's perspective.

For this reason the company is not at all worried about the repayment of the loan, even if the policy owner decided not to pay it back at all during his lifetime. If the policy owner cannot generate by his own merits the incentive to repay the loan in order to reopen his credit line for future borrowing, then at the policy owner's death, the company will simply subtract the loan from the death benefit.

This is why we stress that the increasing equity in the policy caused by the reinvestment of the dividends to purchase more death benefit secures the policy owner, as well as the beneficiary, from going in the hole or simply breaking even by having numerous outstanding loans. This is why the reinvestment of the dividends is a standard feature of a Whole-Life policy designed according to Nelson Nash's IBC especially during the borrowing years of a policy Finally there is point Number Three. You will be more than delighted to learn that when you take out a policy loan the actual amount of the loan never "comes out" of your cash value and so it never stops earning money. You have only given an assignment on that amount of money. Yes, you received the loan money from the company, but the amount received never came out of its tax-free earning capacity inside your policy. This loan money you received to pay your taxes is still earning portfolio interest, annual dividends, and purchasing additional death benefit with them, which continues to increase the equity in your policy. If you really think this through this is quite a remarkable accounting feature. To be sure, this isn't "free money," because you must pay the life insurance company contractual interest on the policy loan. But to repeat, the actual mechanics of the policy loan make it an operation "on the side," while your policy itself continues to chug along. (We are here neglecting the complication of "direct recognition" and "non-direct recognition," which more advanced readers will want to research to fully understand the impact of policy loans upon performance.)

By combining all of these important aspects of the insurance contract with a business owner's ability to create windfalls for purposes of repaying outstanding loans and you have the makings for an ideal system for creative cash flow strategies and management.

GETTING YOUR POLICY UP AND RUNNING

Suppose you've been following our podcast and reading the materials put out by the Nelson Nash Institute. You're convinced that having a well-funded IBC-type policy is an excellent component of any business or household financial plan. However, you hesitate to act because you think it would take too long to build up a policy that could really affect your situation.

Well, what I do in my own affairs might shed light on a strategy you could use to accelerate the process. Specifically, you can take cashflows that are already earmarked for paying your business taxes, and "detour" them through a correctly designed IBC policy. This would allow you to build up the infrastructure of a policy that has a much larger

capacity than you may have thought possible.

In Part II, I will use numerical illustrations to show exactly what I mean. Let me be clear: There is nothing magical going on here. We're not creating money out of nothing. But the special features of policy loan terms will allow you to put time on your side; you will be able to fund your policy with future windfalls in a way more convenient to the vagaries of your cashflow.

Also in Part II I will describe how business owners, using IBC and their corporate entities, can pre-plan their profits using bonuses and sale of assets in such a way that even better results can be achieved.

References

(For all those interested in learning more about IBC and the types of insurance contracts we are describing we recommend you listen to the many podcasts we have recorded regarding this subject, especially Episode 17, 18 & 19 at https://lara-murphy.com/podcast/ and while there visit the resources section of the website for additional information.)

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3. Tax Equivalent Calculator, Dinkytown.net, The Best Financial Calculators Anywhere, https://www.dinkytown.net/java/TaxEquivYield.html, January 19, 2017

4. Cash Value vs. Death Benefit In Life Insurance, Article by Robert P. Murphy, PhD., The Lara-Murphy Report, April 2014, https://s3.amazonaws.com/Greatest-HIts/Cash+Values+vs.+Death+Benefit+in+Life+Insurance.pdf

5. The Mechanics of Policy Loans, Article by Robert P. Murphy, PhD., The Lara-Murphy Report, November 2011,

https://s3.amazonaws.com/Greatest-HIts/The+Mechanics+of+Policy+Loans.pdf

6. Compound Interest Calculator, copyright moneychimp.com, http://www.moneychimp.com/calculator/compound_interest_calculator.htm

Thirty Third in a monthly series of Nelson Nash's personally written Becoming Your Own Banker © *lessons. We will continue these lessons until we have gone through the entire book.*

Part IV, Lesson 2 Equipment Financing

Content: Page 52, BECOMING YOUR OWN BANKER – The Infinite Banking Concept.

The young man observes, "That's like my wife shopping at Winn-Dixie Grocery when we own a grocery store, too. Can I do business at my store?" His insurance agent replies, "Yes, by all means! The insurance company must lend that cash value out in order to be able to pay the death benefit that it has promised – any you outrank all the possible places where they lend money! How much money do you need?"

"Every time I replace a truck, the dealership allows me a greater trade-in value, but the price of the new one I buy keeps going up, too. I seem to always keep financing about $52,600."

Turn to page 61 and note that, for the first four years of the policy, it is identical with the previous example on page 55. The insurance company has got to lend $157,373 somewhere, so there is no problem in lending him $52,600 since he outranks all possible borrowers. It is a fully secured loan as far as the insurance company is concerned.

The agent explains that he needs to start a repayment schedule and that the policy calls for 8% interest on the loan balance – but "we are not going to play that game – you are going to pay the same thing that you are paying the finance company on those 3 other trucks in your fleet, and that is $1,502 per month!"

You must realize that the policy owner can tell him, "Stick it in your ear – this is my money and I can pay anything I want to – or maybe I'm not going to pay anything at all." If the owner comes up with that

sort of nonsense, the agent needs to take him back to the grocery store example in Part I and explain "the can of peas one more time." If he doesn't understand that story, then the agent needs to take him back to the First National Bank of Midland, TX and explain the error of the directors of that bank one more time. If he still doesn't understand, then the agent needs to draw a line through his name and forget him because he is either a thief or he is unteachable! Neither is a good business associate.

Let's assume that he is a good student and understands that whatever he pays in interest is going to his policy being managed by the "gophers" at the insurance company. Anything over the 8% loan interest requirement will be going to increase the capital in his policy and provide more money for the insurance company to put to work in his behalf. It is just like the example of the extra 2 cents for the can of peas that the grocer required his captive customers to pay in Part I.

And so, at the beginning of the fifth year he makes a policy loan of $52,600 and trades in an old truck, making sure to make a loan repayment of $18,000 – the same thing he had been paying a finance company for the old one. This transaction shows up on the illustration as (-$34,600) in the Net Annual Outlay column. If it takes you a minute to understand this cash flow, then take all the time you need. It must be understood. At the end of the eighth year he has repaid the loan plus interest back to his policy. He repeats the process every four years.

Now, look at the cash value at age 65 – it is $1,988,254. Compare this with the yield in the previous example where the insurance company managed it all on his behalf ($1,517,320). He has an increase of $470,934 by financing the truck through his own banking system. His cash flow in both examples is the same. It is all a matter of where the interest he is paying goes – to the finance company or to his policy.

Note that his retirement income has increased to $125,000 per year. Assuming death at age 85, he has withdrawn a total dividend income of $2,034,800 plus everything that he paid into the policy – and still delivered $3,119,289 to the next generation. This is a significant improvement over the illustration on page 55 where the insurance company managed all the cash values on his behalf.

All of this is because the interest that he had been paying the finance company is now going to his policy – not the life insurance company.

Take all the time you need to study these two illustrations because they need to be thoroughly understood before we go any further. You must realize that the improved results are not the results of something that the life insurance company did. It was all because of how the policy owner directed his cash flow in payment for the truck he needs in his business. He has cut the "gate-keeper and toll-taker" out of the pattern.

And so, our policy owner says, "I'm beginning to see a pattern here – can I finance two trucks through this system?" We will look at that in the next lesson.

Take control of your financial world by

Becoming Your Own Banker

Find a Practitioner Near You

The following financial professionals joined or renewed their membership to our ***Authorized Infinite Banking Concepts Practitioners*** team this month:

- Dave Swanson, Naperville, Illinois
- Todd Gregory, Springfield, Missouri
- Dale Moffitt, Red Deer, Alberta
- Jim King, Cody, Wyoming
- Brandon Goswick, Marshall, Texas
- Will Moran, Edmonton, Alberta
- John Perrings, Oakland, California
- Frank Lupu, Boise, Idaho
- Michael Burrill, Sacramento & Auburn, California
- Kyle Mans, Red Cloud, Nebraska
- Steven La Bella, Fontana, California
- Kyle Fuller, Mesa, Arizona
- Nick Kosko, Louisville, Kentucky
- John Montoya, Dublin, California
- John Urbik, Tyrone, Georgia
- Henry Mora, Houston & Lubbock, Texas
- Karen Powell, Atlanta, Georgia
- John Ward, Salem, New Hampshire
- Henry Wong, Markham, Ontario

You can view the entire practitioner listing on our website using the Practitioner Finder.

IBC Practitioner's have completed the *IBC Practitioner's Program* and have passed the program exam to ensure that they possess a solid foundation in the theory and implementation of IBC, as well as an understanding of Austrian economics and its unique insights into our monetary and banking institutions.

The *IBC Practitioner* has a broad base of knowledge to ensure a minimal level of competency in all of the areas a financial professional needs, in order to adequately discuss IBC with his or her clients.

Before you look for a practitioner, we suggest listening to the following two episodes of ***The Lara Murphy Report.***

How-To Guide for Starting IBC, Part 1
How to begin your study of Infinite Banking, including finding an Authorized Practitioner.

How-To Guide for Starting IBC, Part 2
How to prepare for your first meeting with an Infinite Banking Authorized Practitioner.

THE FOUNDATIONS OF IBC

This online **video series** for the general public provides a comprehensive introduction to the *Infinite Banking Concept.*

The first four modules are free, you can view them here:
infinitebanking.org/foundations
The remaining eight modules are subscription-based, costing $49.95 for all eight.

*Or contact an **Authorized IBC Practitioner** and ask for a coupon code that will enable you to watch all twelve modules FREE.*

Module 1: Introduction to the Nelson Nash Institute

Module 2: What the Infinite Banking Concept Is

Module 3, Part 1: How IBC Works

Module 3, Part 2: Policy Loans & The Nature of Collateral

Module 3, Part 3: How to Read a Policy Illustration

Module 4: Why Nelson Calls It The Infinite Banking Concept

Module 5: The Life Insurance Industry

Module 6: Why Not Buy Term and Invest the Difference?

Module 7: Using IBC to Pass Wealth to Future Generations

Module 8: The MEC Rule and Policy Design

Module 9: Does IBC Work for Older People?

Module 10, Part 1: IBC for the Business Owner

Module 10, Part 2: IBC for the Business Owner

Module 11, Part 1: Using Your IBC Policy: Premiums, Dividends, and Policy Loans

Module 11, Part 2: Using Your IBC Policy: Premiums, Dividends, and Policy Loans

Module 12: IBC as a Way of Life

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