Excerpts From "My History With the Infinite Banking concept (IBC)"
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In this article, I will summarize Nelson Nash's Infinite Banking Concept (IBC) for the novice, but I will do so in the context of my own experience in learning about it. It will hopefully prove useful as a general introduction to IBC for any reader, told in the style of "one guy's journey."

Before jumping in, I need to add one last caveat: I am not a registered financial advisor, and the information I offer in this article is not intended as a formal recommendation for any reader to change his or her financial situation. Obviously the reader should check with other experts before taking any action. I am merely telling my own history with Nelson Nash's Infinite Banking Concept.

Meeting My (Future) Co-Author, and Discovering IBC

In the summer of 2008 I was contacted by Carlos Lara, who told me he was currently reading my Study Guide to Murray Rothbard's giant economics text, and he realized from the author bio that we both lived in Nashville. We began meeting for lunch to discuss the unfolding financial crisis and other such weighty matters. At an early stage in these meetings, Carlos – whose consulting business focused on setting up trusts for businesses and households – explained that in addition to being a big fan of Austrian economics, he was also an avid proponent of Nelson Nash's Infinite Banking Concept (IBC). Carlos lent me a copy of Nash's underground bestseller, <u>Becoming Your Own Banker</u>, and asked me to evaluate it.

The basic idea of BYOB (<u>Becoming Your Own Banker</u>) is that the typical American household is flushing away boatloads of money in interest expenses to outside financiers. If people could become disciplined and save up before making major purchases – so that they were relying on their own accumulated capital rather than what others had saved – they would be able to finally start getting ahead.

However, Nash wasn't preaching a simple "get out of debt" philosophy. Instead, he was okay with gross borrowing in order to finance major purchases, but it had to be done under special conditions such that really you weren't borrowing on net. For various reasons (some of which I'll sketch out, later in this article), Nash argued that it made a lot of sense to accumulate a stockpile of wealth inside one or more high-premium, dividend-paying, whole life insurance policies.

Now for the "becoming your own banker" part: Whenever a person needed to buy a new car, send a kid to college, pay for a wedding, go on a cruise, fix the furnace, etc., he wouldn't borrow from a conventional lender, and he wouldn't even draw down "cash" sitting in a bank CD or other type of "savings account." Rather, the person would get a policy loan from the insurance company, using his "well-funded" life insurance policy as the collateral. Then, instead of making periodic "car payments" (or whatever the big-ticket item was" to the conventional lender, the person would direct the same cash flow to the insurance company. Nash had several numerical illustrations to show that this strategy would make a person a heck of a lot wealthier over time, compared to other ways that the average American household might run its affairs.

I must confess – and I've said this several times in front of Nelson; he's okay with it – that at first I couldn't make heads or tails of BYOB. I'd be reading along, thinking, "This guy is really wise, I just love his worldview." Nelson would make very profound statements about the human condition, the weaknesses and temptations we all face, and he was very skeptical of commercial bankers and – most of all – government programs. Further, Nelson was very well read in the great Austrian and libertarian works, and heaped praise on the Foundation for Economic Education (FEE) as well as the Mises Institute – two places for which I had done a lot of work. So there were a lot of things pushing me to tell Carlos that, in my opinion, BYOB was a great book.

But then I'd keep reading and come across a statement that sounded nuts to me. What the heck was this guy Nash saying? Was he making some elementary error at Step 1 in his analysis? Could I just toss this slender book aside, and not have to waste any more of my time trying to figure it out?

Part of the problem was that I knew absolutely nothing about whole life insurance; I thought all life insurance was term insurance, where you make premium payments during the contractually specified slice of time, and the insurance company sends you a check if you die during that period. (My joke at the time was that I had always been baffled at the scene in *It's a Wonderful Life* when Jimmy Stewart's character tries to bargain with the greedy old man, using his life insurance policy. That seemed as nonsensical to me as someone trying to raise money by pulling out his fire insurance policy.) So, when Nelson in BYOB showed various tables talking about the dividends paid out on an insurance policy, and how you could use them to buy more "paid up insurance" and boost your "cash value" and death benefit to higher levels, I didn't really understand what was even going on, let alone could I determine if his numbers seemed plausible.

As an aside, let me remark that my ignorance at that time is really a profound statement on how much things changed in the financial sector over the 20th century. Here I was, with a PhD in economics from a top-15 program in the world, I had done a dissertation on capital and interest theory, and I had even worked for a financial firm, helping with research papers for clients and calibrating the computer model that ranked stocks according to various criteria our chief economist (and head of the firm) would tell me to plug in. Yet I didn't know what permanent life insurance was, even though an economist like Ludwig von Mises – about whose work I had written a Study Guide – casually mentions in several places in his writing that the average household saved via life insurance. To people of my age and younger, we grew up being taught that "saving for retirement" was basically the same thing as "buying into IRS-approved mutual funds with large exposure to Wall Street equities, where you're not allowed to touch your money for decades." In hindsight, it is stunning that I was so naïve, since my career was based on being suspicious of all these shenanigans!

Translating Frameworks

Anyway, back to the story: Because this new acquaintance Carlos seemed like a pretty sharp, no-nonsense guy, who lived in a wealthy neighborhood, advised very wealthy clients on financial matters, and gave the most intuitive PowerPoint presentation on fractional reserve banking that I had ever seen, I kept giving this odd book BYOB additional chances. Carlos thought so highly of this guy Nelson Nash and his IBC philosophy that I didn't want to prematurely dismiss it.

Eventually it started clicking for me. What happened is that in order to feel comfortable with IBC, I had to reinvent the wheel, and reach Nelson's conclusions through a "wind tunnel" of my own educational background, even though one of Nelson's main themes is that we need to stop thinking that way, since the conventional framework could be very misleading and was pushing people into erroneous decisions all the time. But, we have to work with what we know and trust, and I couldn't fully embrace IBC until I had broken it down and understood it with the conventional tools of analysis that I had from my economics background.

The "Rates of Return" Trap, and Other Objections

Let me give some examples of what I mean. Nelson often stresses that IBC "isn't about rates of return." At first, I thought he was basically admitting that the critics were right and that whole life insurance was a "terrible investment" because of its abysmal internal rate of return.

But of course, that's *not at all* what Nelson is saying. His point is that *you aren't "investing in life insurance," rather, you are setting up a very conservative financing system* over which you have much tighter control, compared to any other readily-available option. If you spot a great investment opportunity that will yield (you think) 20% in the first year, then great! Go ahead and borrow against your whole life policy, and acquire the investment. IBC simply describes a *headquarters* or "home base" for your wealth, not a final destination (or prison!) the way 401(k)s are currently designed.

Indeed, some of the most powerful portions of his book show how both the average person but also a business owner, can end up at a future date by using IBC instead of conventional lenders. Obviously, if you end up with a higher net worth at age 65, using the same out-of-pocket cash flows, then you must have earned a higher "internal rate of return" with IBC than the alternative Nelson considered. So to say "this isn't about interest rates" wasn't to reject standard accounting; I could still come in, using conventional financial analysis and make sense of what Nelson was recommending. It's just that it was such an *unusual* idea that at first I didn't even know how to apply the equipment in my toolbox.

Let me give another example. Dave Ramsey is a radio talk show host who (admirably) counsels people on how to get out from their crushing debt load, through obvious but crucial things like making out a budget, communicating with one's spouse on financial affairs, etc. Ramsey is very entertaining and I can certainly understand why his show is so popular. However, Ramsey absolutely has it out for whole life (and other types of permanent life insurance) policies, advocating instead that people "buy term and invest the difference." For example, in a post from his website, Ramsey implies that you won't have *any* cash value for the first three years of a new policy. He goes on to explicitly say that the rate of return on your money is much higher in mutual funds, that you won't need life insurance after twenty years if you follow his plan, and that the insurance company keeps your cash values when you die, giving your beneficiary only the death benefit (3).

Every one of these (typical) objections is either misleading or downright false, at least when it comes to Nelson Nash's IBC approach of using whole life policies. First, if you set up the policy properly with a "Paid Up Addition (PUA) rider", then right off the bat, a portion of your periodic payment is buying a chunk of full paid-up life insurance. Thus, your cash value begins rising immediately, and you can begin borrowing against your policy right away (if you need to).

The IBC Think Tank

Returning to the narrative: I became further reassured that this whole thing wasn't crazy when I first attended the "IBC Think Tank" in Birmingham. (This would have been in February 2010). Because of Carlos' efforts on my behalf, Nelson Nash and David Stearns (who ran the day-to-day operations of IBC) had asked me to be the after-dinner speaker on the first night of the two day conference. Because I really wanted to get to the bottom of this IBC stuff, I made the three hour drive down to Birmingham the day before I was scheduled to speak. This allowed me to sit in on part of a Nelson Nash seminar (which catered to regular people who wanted to use IBC for their household finances) and also ensured that I could attend all of the sessions of the Think Tank itself (which catered to financial professionals that wanted to use IBC with their clients).

At the Think Tank, I saw a CPA give a presentation explaining the proper way to document interest income and deductions, so that the IRS wouldn't object. (This reassured me that the whole thing wasn't some big tax evasion scheme.) Another presenter pointed out that, when you figure in the favorable tax treatment on whole life policies (if they meet certain requirements which I won't discuss in this article,) their "awful" internal rates of return can actually become pretty decent, considering the guarantees in the product and the ease with which you can access the money. Furthermore, several of the other presenters were insurance producers who had plenty of anecdotes of how they had shown clients ways to improve their cash flow management by incorporating IBC.

Conclusion

This article is admittedly long, but I thought it important to explain my history with IBC in one self-contained piece. Now people will understand why I am so interested in the economics of life insurance, and why I'm sensitive to what seem ill-informed critiques of whole life. The more I study it, the more I believe that Nelson Nash's Infinite Banking Concept makes sense, and that a properly designed whole life insurance policy can be an important component in the financial arrangement of the simple household or large business.