Pay Cash Or Use A Policy Loan?

by L. Carlos Lara

Individuals who own one or several dividend-paying Whole Life insurance policies that are designed in the special way advocated by Nelson Nash's *Infinite Banking Concept (IBC)* are often faced with a perplexing question and a decision they must make whenever the need arises to purchase or pay for something.

It's a puzzling dilemma because they have cash set aside (probably in a conventional bank checking account) to make the purchase, but knowing how an IBC policy works they hesitate, wondering if they might be better off purchasing the item using cash from a policy loan instead. The entirety of their question can be worded something like this: *"Should I pay for this expenditure with the cash I already have sitting in my bank account, or should I first put that cash in my IBC policy and then use the cash from a policy loan to purchase the needed item?"*

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Since this is one of the most often asked questions by listeners of the *Lara-Murphy Show* podcasts, readers of the ***LMR,*** and also by many attendees at our *IBC Seminars For The General Public,* I thought that a stand-alone article addressing this one topic in particular might prove beneficial for all of us who practice IBC.

The more people discover and learn how these nifty cash flow instruments work the more they want to know the full extent of their potential. So I am not at all surprised to see this particular question come up so frequently.

Setting The Table For Our Discussion

Before going any further let's make sure we all recognize some of the very unique distinctions of the people asking this important question. As we have already stated, these people have the cash available at their disposal. This fact by itself tells us a lot about these inquirers. They are obviously not cash-

strapped individuals. These are people that have the ability to accumulate and save money. That does not say that these people are necessarily wealthy, but the cash they have in their possession speaks to their established discipline. Plus, we can't fail to notice that these people already own an IBC policy, which is yet another sign of an individual with elements of financial maturity.

In observing these simple facts we can now consider their question in a better light. The primary reason these people ask this important question is because they already know that the special calibration of their IBC policy (i.e. its special design) has the ability to produce more cash value, more dividends, and more death benefit every time money is injected into the policy's PUA Rider. So what these inquirers are really asking is if there are any special conditions or guidelines they should take into account before deciding whether to use cash or a policy loan for their expenditure.

They also know, especially if they have implemented their Whole Life insurance contract using one of our graduates found on the IBC Practitioner Finder https://infinitebanking.org/finder/, that a policy loan is still a *debt*. Once that policy loan is taken, the policy owner now owes the debt to the life insurance company and it carries with it a rolling interest charge. In other words, these practitioners are well aware that there is no free money that comes with a policy loan. A loan is a loan, and until it's paid off the insurance company holds a security interest in the policy owner's available *cash value, limited*, of course, to the amount of the loan and any accrued interest.

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funds "on the side," as it were, with your life insurance policy chugging along. (For purists, there is a complication of direct vs. indirect recognition, but newcomers shouldn't worry about that for my present point.) In this respect, it's analogous to a mortgage on a house: When you borrow money "against the property," that act by itself doesn't reduce the market value of your house, and it doesn't directly affect the sale price of your house, as the real estate market goes up or down. Of course, the *equity* you have in your house takes into account the mortgage, because that is a lien against your asset. In a similar fashion, even though we casually sometimes may loosely speak of "borrowing out of your IBC policy" or ask "how much cash value do you have left in your policy," make sure you realize the underlying mechanics: When you take out a policy loan, the life insurance company is using *its* money to give you the loan, and your cash surrender value in the policy serves as the collateral.

Now back to our central dilemma that is the focus of this article, namely, people who must make a purchase and who have enough "cash in the bank" but also have a properly designed IBC policy: The essence of the question is regarding the appropriateness of their expenditure and also under what special circumstances should they *first* inject the available cash they have in their bank account into their policy's PUA Rider and then use the cash from a policy loan to pay or purchase the wanted item. They want to know what superior benefits, if any, they will receive using the policy loan method as opposed to simply paying with cash and *not* going into debt with the insurance company (by taking out a policy loan)? Even though ultimately this decision is left entirely to the discretion of the policy owner, this inquiry really gets to the crux of the matter and why I consider it to be so relevant.

Not All Expenditures Are The Same

There are several things to consider at the outset before deciding whether to use cash or a policy loan, the first of which is the nature of the expenditure itself. We should begin by asking ourselves if the expenditure we have in mind is a lifestyle "necessity," a reduction of debt, or an investment. If it is any of these types of expenditures my personal preference is to use a policy loan after I have first put the cash in the PUA Rider of my policy, simply because these types of expenditures, given the mechanics of IBC policies, serve to conserve and grow the wealth I already own.

This wealth that I already own actually exists inside and *outside* my IBC policy. So in effect the triggering of this wealth increase generated by the injection of the cash into my policy's PUA Rider will partially offset the interest charges on the loan. But in certain situations (mostly in the future), the expenditures I have selected to pay for using my policy loan will have the potential to completely offset the entire loan balance when they are sold for a profit.

Let me explain. Lifestyle necessities, as I see them, can be thought of as repairs, main-

tenance, and replacement costs of facilities and infrastructures that serve to increase my future production, and/or future revenue. Debt reductions serve to increase net worth. Investments appreciate and then can be sold for a profit. Hence all three of those types of expenditures contribute to building my estate in the long run and are appropriate expenditures for using a policy loan.

There are other reasons why this approach is superior to using cash and I will cover them as we proceed deeper into our discussion. But just to clarify, I think you know what I mean when I point to investments and reduction of debt as good expenditure options for policy loans. But I should spell out once again what I mean by a *lifestyle necessity.* There are a lot of things we can buy and spend money on, but not all expenditures have the same end result.

For example: A car that is used up and needs replacing is, in my opinion, a lifestyle necessity. So is the replacement of a major home appliance that has reached the end of its usable life such as a central heat and air unit in your home or office. Or, it could be the roof over your head, or any expense that can easily be classified as an ongoing lifestyle essential that needs fixing or replacing to keep it operational and help maintain the market value of its underlying asset that can be sold at a profit or at least converted to cash.

On the other hand, *living expenses* such as food, gasoline, utilities, clothing, and similar consumption costs are completely different types of expenditures. They should be paid for with cash, not policy loans. Now there is certainly nothing in writing that says you can't use policy loans to pay for these types of bills, or any type expenditure of your choice. But if you are truly attempting to manage your money well and grow an estate you should draw the line between certain expenses, especially between lifestyle necessities that affect the growth and value of your estate and those that don't. Otherwise you would wind up using your IBC policy as though it were an ATM machine practically every month, which is a gross misinterpretation of IBC.

Windfalls

Windfalls also play a major role when considering taking out policy loans versus paying with one's base working capital (the cash in our checking accounts). We should never

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forget that we are *"banking"* with these policies, which involves the full scope of cash management and finance. Although a windfall is often thought of as a piece of unexpected good fortune, typically one that involves a large amount of money, sound money management can actually create windfalls. As IBC *"bankers"* we should manage our money with expected windfalls in mind. In fact, all of our efforts should strive to create windfalls and policy loans can be used for that specific purpose.

For example: Let's take the case of an expected, or even an unexpected, family inheritance. This event can certainly be described as a windfall, actually more like a gift from heaven—an expression of love in the form of money from a deceased family member. A bonanza such as this can take care of a lot of previous money mistakes for some lucky person or family.

Yet an IBC Practitioner, by the mere fact that he has taken out an insurance policy and has assigned a beneficiary to it, has already taken a very first important step toward establishing an estate. If he or she now begins to take out policy loans in the manner prescribed above, over time this *privatized banking* system will create living benefits for the policy owner while alive, and an inheritance (windfall) for the beneficiary upon death.

Keep in mind that what we are doing is practicing IBC while *"thinking long range"* as Nelson Nash advocates. Also, with everything that I have stated up to this point in our exploration, I have been addressing it to salaried individuals and managers of households. What I am trying to make clear is that when practicing IBC you must learn how to start thinking like a business owner because, whether you realize this or not, an IBC policy has placed you squarely in the managerial role of a business—*a banking business.*

Business owners reading this analysis are more naturally inclined to understand the points I have made thus far in this report in addition to understanding the value of creating windfalls because this is their *modus operandi.* Business owners use business profits (after taxes) to deliberately invest in hard assets that they hope to sell in the future at a profit. Since they generally think of their business enterprise as their chief asset, they tend to reinvest these profits into their businesses in order to increase their wealth and eventually sell the business in the future—the final windfall.

In the meantime, and at great risk to themselves, business owners will not hesitate to take out loans and borrow from lines of credit from commercial banks in order to create those windfalls. But once they become their own bankers using IBC, policy loans take preeminence over commercial bank loans.

Space constraints prevent me from unpacking each of the steps business owners use to wean themselves away from commercial banks using IBC, but for a complete treatment of how they make the switch, please read our newest book co-authored by Nelson Nash and Robert Murphy, *The Case for IBC*. https://thecaseforibc.com/

The Power of Whole Life

Let's also not forget that dividend-paying Whole Life not only has multi-dimensional benefits unlike any other financial instrument, but it also has three very important characteristics that are foundational to this particular discussion. Briefly summarized, the first of these is the legal right every policy owner has in his policy contract to take out policy loans so long as he or she has cash value in the policy.

Second, although an outstanding policy loan rolls over at interest, you can pay the loan back on your own terms and schedule, or not at all, if you wish. This is extraordinary! That kind of payment flexibility on any kind of loans exists nowhere else in the financial world, but obviously with that kind of freedom also comes responsibility. With regards to this I have a suggestion. My August 2017 ***LMR*** article, "An IBC Tax Strategy: Part III," contains a thorough treatment of the most important discretionary guidelines on policy loans that every policy owner should know. The 2017 article is a great companion to this article because it breaks down the functions of practicing IBC correctly and responsibly and will eliminate the worry of a 1099 surprise or the worry of the IBC policy ever being underwater. https://s3.amazonaws.com/Greatest-HIts/An+IBC+Tax+Strategy+Part+III.pdf

The third foundational characteristic of Whole Life is that no matter what amount of money you borrow from the life insurance company with the cash value serving as collateral, that very same amount of money continues to earn interest, dividends, and a growing death benefit in your policy for as long as you live and for as long as your policy remains in force. But when additional cash is injected into the policy's PUA Rider it grows even more and it grows even faster. For that reason all three of these elements of a specially designed Whole Life policy when used in combination make it the ideal financing system that every household and business owner should own.

Conclusion

In this article we have examined all sides of a perplexing conundrum that IBC practitioners often face, which is deciding whether or not they should make a necessary expenditure with cash or with a policy loan. In order to condense the thoughts in this commentary into a final summary and answer this important question I am providing a personal case study for your consideration.

Several years ago I was confronted with

having to make a $25,000 expenditure. I had the cash sitting in my checking account, but as I began the process of examining the nature of the expenditure and weighing the options of paying for it with cash or using a policy loan I was suddenly struck with an amazing revelation. This spectacular insight came to me after taking the time to calculate the actual costs of saving just one dollar. If you have never done this analysis, you should. It's a staggering amount! No wonder the savings rate for U.S. households is a mere 5% or less. This is definitely one powerful way to discover that the financial system is rigged and works against us. I highly recommend this exercise in your decision-making.

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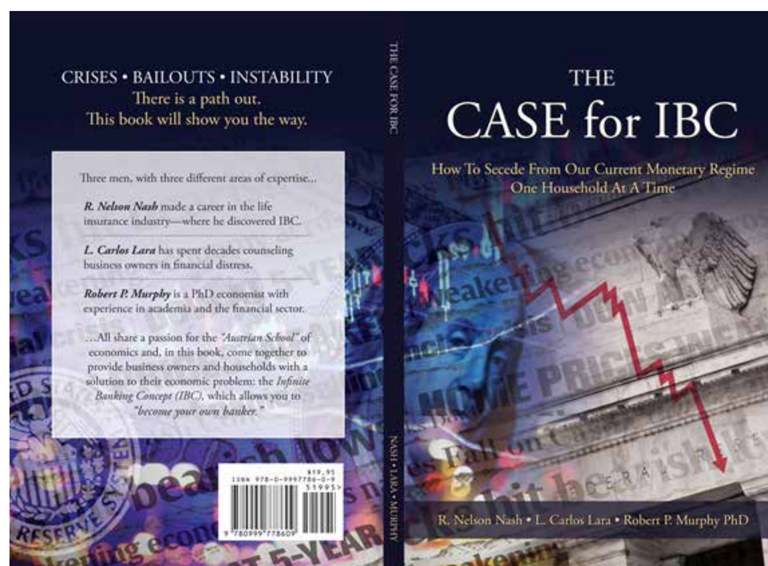
First of all realize that every saved dollar is the *"residual"* of profit. This means that it is the money left over after paying taxes on it. But even before that profit is earned you have to consider the total revenue you first had to generate (in income or paychecks) and then account for all the expenses you had to pay to arrive at that profit (your taxable income). After you calculate the numbers you finally wind up with the *residual*—the saved dollar.

Since everyone has their own tax bracket and their own expense structures the calculations will vary from person to person, but the numbers will alarm you and it will teach you a vital lesson. That lesson is that you should not easily let go of a *saved* dollar, because that saved dollar cost you a whole heck of a lot! In my case I have to generate $145,000 in revenue in order to be left with $25,000 free and clear after taxes! That's a lot of work.

Realizing this, I moved my $25,000 savings into my IBC policy and locked in my savings and their future growth and then did not hesitate to request a $25,000 policy loan from my insurance carrier, which arrived in a matter of a week. Since it's a loan to me, it arrived expense and tax-free. What I gave up, however, for the policy loan amount was a security interest in my cash value to the extent of that loan. But my insurance policy portfolio was kept intact and continued to earn interest, dividends, and a growing death benefit regardless. The lent money I used to purchase an investment that I believe will

yield a profit sometime in the future— a sound expenditure.



When I moved the saved $25,000 that was originally in my checking account into my IBC policy it was injected directly into my PUA Rider, creating an immediate increase in cash value, also in dividends, and purchasing for me additional life insurance, all in one fell swoop. The additional increase boost in cash value and dividends bought me approximately $50,000, of additional death benefit in my policy. (These increases will vary from person to person depending on the age of the insured.)

Of course, I now had a loan of $25,000 with a rolling interest charge, but the new assets generated partially offset the interest charge. So long as I continue to pay at least the interest on this loan each year I will keep the loan from snowballing. So in effect I was left managing an interest-only loan with absolutely no time pressures from the insurance company to pay off the indebtedness. The sale of assets in the future that I originally purchased using my IBC policy will create the necessary windfalls to pay off my policy loans. I will want to pay off this loan and other loans because in doing so it will open up my credit lines, increase my net worth and enhance my overall estate.

What happens if I die the day after executing this one transaction? If we examine only this one financial move under the scenario of my premature death, the life insurance company would simply subtract the $25,000 loan from the $50,000 death benefit and my beneficiary (my spouse, in my case), would still receive a windfall of $25,000. She would not be shortchanged at all by my decision.

Yes, I realize that at first glance it may first appear as though I am playing fast and loose managing money in this way, but if you will simply do the math for yourself you too will discover why Nelson Nash says that this is the most peaceful way to live. And, you will never have the need of a commercial bank ever again.

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