



# OWN YOUR DEBT

by Robert P. Murphy

THERE ARE VARIOUS WAYS OF MOTIVATING the philosophy of Nelson Nash that he lays out in his classic book, *Becoming Your Own Banker (BYOB)*. In this article I want to focus on the benefits of “owning your debt,” a phrase that I first heard from David Stearns. I want to be clear that what I discuss in this article is not the *sole* rationale for implementing Nash’s Infinite Banking Concept (IBC), but I hope my discussion resonates with a large segment of American households who are crippled by outside debt.

## An Introduction to IBC

The central message of Nelson Nash in *BYOB* is that everybody needs to rely (at least implicitly) on financing for life’s major purchases. Even if you buy a car with cash, you are forfeiting the opportunity of investing that cash and earning a return on it. So even people who always “pay cash” still experience the same implicit tradeoffs between spending now versus later. Therefore, Nash argues, the real question is whether you



paying whole life policies. There are ways to calibrate such policies so that they are excellent tools for cash flow management. They are the best place, all things considered, to “warehouse your wealth” (which is the title of a subsequent Nash book).

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are going to obtain your financing from a bank controlled by *outsiders*, versus a bank that *you* control.

Now once you’ve decided that it makes sense—for a variety of reasons—to rely on financing coming from yourself, Nash then explains that in today’s environment, the most convenient and advantageous way to establish your own private “bank” is to take out large, dividend-

As time passes and you plow your savings into properly designed whole life insurance policies, their cash values grow. Then, when you need to make a major purchase, you can take out a “policy loan” from the insurance company, with your cash value serving as collateral. The terms on this loan are quite generous: There is an attractive interest rate, no credit check, no questions about the use of the funds, and no payback schedule. The explanation for these attractive

features is that the collateral on the loan, from the lender's perspective, is absolutely airtight: the life insurance company *itself* guarantees the asset. In this respect, a policy loan is a safer investment from the insurer's viewpoint than even a U.S. Treasury bond.

To be clear, Nelson Nash is not advising everyone to "invest in life insurance." Again, he

## Advice From the Financial "Experts"

Naturally, Nash's advice is far too straightforward for the gurus to endorse. The conventional wisdom from financial planners is that while it may be important to have life insurance in the form of a cheaper term policy (not a more ex-

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recommends using these policies as *warehouses* for one's wealth—a *headquarters*, if you will. If a person sees an attractive real estate deal, he is certainly free to take out a policy loan and use the funds to invest in the land. Indeed, that's part of the *rationale* for implementing IBC: You always have ready access to your wealth, allowing you to pounce on investment opportunities as they arise.

pensive whole life policy) for its death benefit protection—especially for a young breadwinner with kids to support—nonetheless life insurance makes a terrible saving or investment vehicle. Rather, the conventional financial advice in America today says that an individual should turn to tax-qualified mutual funds to build up a nest egg for retirement. Putting the two ideas together yields the familiar slogan: "Buy term and invest the difference."



According to the gurus, “buy term and invest the difference” is a much more sensible strategy. For a given death benefit, the premium on a term policy is lower than for a whole life policy, so that the pure life insurance coverage is cheaper. Then with the savings (because the premium is lower), the household can invest in, say, a 401(k) mutual fund with pre-tax dollars. These holdings then grow at historically higher rates




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than the cash value in a whole life policy. Thus it seems that “buy term, invest the difference” is a no-brainer: you get the desired death benefit coverage for your family at the lowest possible price, while your retirement investments earn a better rate of return. What kind of an idiot would follow the Nelson Nash strategy in light of this seemingly superior approach?

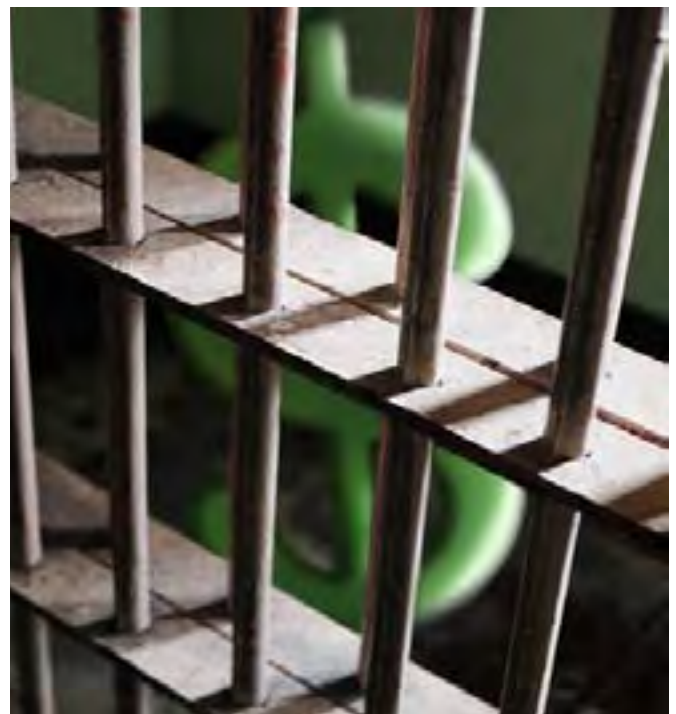
In other issues of the *LMR* I have tackled this mindset;<sup>1</sup> I won't repeat my arguments here in this article. Instead, I want to describe the trap into which many American households fall, because they follow this typical advice that I have just described. In the next section, I'm doing nothing more than restating what Nelson Nash describes as the typical American's problem early on in *BYOB*, but I'll talk about it from a slightly different angle.

## Putting Your Money in Prison

Now in fairness, I should be clear that Dave Ramsey tells his followers to stay out of debt

altogether. So in that respect, someone who literally obeys the Ramsey approach is going to be ahead of the average Joe. But more generally, that's *not* what American households do when they listen to the conventional financial wisdom.

For millions of American households, this is what happens in practice: After they siphon some of their paycheck into stocks and bonds



which they can't touch until retirement, they then discover that they can't afford their desired lifestyle. So what do they do, when they want to buy a car or a house, send their kid to college, or pay for a wedding? Because the government won't let them access their "savings"—which makes it an odd form of "savings"—these households have to go hat-in-hand to outside creditors.

30 percent of Americans report having higher credit card balances than they could pay off with their "emergency savings." Finally, the average APR on a credit card with a balance on it was 13.14% as of February 2014.<sup>2</sup>

These statistics are staggering.<sup>3</sup> The conventional wisdom of putting money into a 401(k) is *clearly* not working for any household carrying

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Depending on how much outside debt a household takes on, the situation can border on the absurd. Currently the average credit card debt per U.S. adult is just shy of \$5,000, while the average balance on a card that usually carries a balance was above \$8,000. Looking at *households* (not individuals), the national average of credit card debt is \$7,000, while focusing on just *households with credit card debt* the average figure jumps to a whopping \$15,000. Nearly

credit card debt. The Federal Reserve may have a "zero interest rate policy" but the credit card companies certainly don't. If a debt-strapped household can somehow manage to pay off its \$15,000 of credit card debt rolling over at 13%, why that's the equivalent of a *guaranteed rate of return* of 13% on a \$15,000 investment. The stock market doesn't offer *that* kind of sure-thing.





Let me spell out the absurdity to make it crystal clear: There are households who have thousands of dollars of credit card debt rolling over at more than 10% APR, while they simultaneously hold more than enough to pay off these balances tied up in tax-qualified mutual funds that feature a mix of equities and bonds. When questioned, the people making these financial decisions might justify the arrangement by saying that they need to “save for the future,” and that it would be “irresponsible to tap into my

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## Own Your Debt

Thus we see that there are millions of households waiting to be helped with IBC. Note, I’m *not* saying that IBC *only* makes sense for such

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retirement.” Yet the blend of growth and safety offered by the mutual fund(s) does not match the *guaranteed* return—in the sense of total wealth—that comes from paying down credit card debt.

This is particularly true in our environment where “safe” bonds have very low yields, while credit card APRs are still quite high for many households. And as an added kicker, keep in mind that many households have *variable-rate* debt, on credit cards and other types of loans (some even with adjustable rate mortgages). If

people—after all, the IRS changed the tax rules in the 1980s because so many rich people were piling into whole life policies. Instead, I’m just focusing on this particular aspect of the case for IBC.

To repeat, the technique I am about to describe is not the only way that people use IBC, but for millions of middle-class households with sizable assets in tax-qualified plans, *and* who are carrying large amounts of credit card debt, the technique makes perfect sense, and is a specific application of IBC.

The technique is to sell off enough of the outside assets—even if that means paying a tax penalty because they are in 401(k) or similar environments—in order to fund a dividend-paying whole life policy large enough to then allow for the rapid payoff of the credit card debt.

The benefits of this move are obvious. On the one hand, it represents a simple swapping off assets and liabilities: On the asset side, the house-

thrown off by the policy are also more stable than the volatile stock market. Furthermore, the debt (in the form of a policy loan balance) can be paid off on any schedule the household desires; there are no minimum monthly payments due, which if missed will trigger penalty APRs and black marks on a credit report.

Finally, when you consider the APR that the household was originally paying on the credit

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hold reduces its holdings of stocks and bonds in the tax-qualified environment, while raising its cash surrender value in the form of a whole life policy (and also the death benefit coverage which has an economic value itself). On the liability side, the household pays off its credit card debt while incurring a comparable loan owed to the life insurance company.

Yet this "mere" swapping of assets and liabilities puts the household on much firmer ground. The assets now grow at a more dependable rate: there are guaranteed returns, and the dividends

card balances, this new plan will mean that the total wealth of the household appreciates at a higher rate, all things considered.

## Notes of Caution

The actual mechanics of this operation depend on the specific numbers of the individual household. There are also IRS rules concerning how rapidly wealth can be moved into a whole life policy; you don't want to "MEC" the policy. Furthermore, if there are *large* movements of wealth out of a tax-qualified plan, staggering that outflow might make sense to stay in a lower income tax bracket. Because of such subtleties in execution, it's critical to discuss these types of financial plans with a graduate of the IBC Practitioner's Program—see our listing of such individuals at [www.InfiniteBanking.org/Finder](http://www.InfiniteBanking.org/Finder).

Let me also put in a warning for any financial professionals reading this article: If you are talking with a client, you *cannot* advise him or her



to sell off equity holdings if you do not have the proper licenses. FINRA is very picky on such matters. For example, if you are only licensed as a life insurance agent, then your job (should the client desire it) is to set him or her up with a properly designed, dividend-paying whole life policy with the proper PUA and term riders, which will have the correct premiums and cash value targets for the cash flow (in and out) that the client has in mind. The client has to already have decided where the money to fund the policy is coming from; you can't steer the client into selling off stocks in order to buy a life insurance policy from you.

## Conclusion

The conventional financial wisdom has placed millions of American households in an untenable position. After taking out income tax and payroll deductions, health insurance premiums, and contributions to tax-qualified retirement accounts, the average employee has little left. Thus to buy a car or just keep up with daily living entices him to turn to credit card companies and other outside lenders.

One way of understanding IBC is that it allows you to "own your debt." Specifically, you build up enough cash value in one or more whole

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life policies so that you can take out policy loans large enough to knock out what you owe to outside lenders. In this article, we focused on credit card debt because it is the most obvious, but the principle applies more generally.

Besides looking at the specific numbers (APRs on credit card balances, the volatility of the stock market, etc.) the qualitative benefit of “owning your debt” is *the peace of mind it yields*. By collapsing your outside debts—which are often collateralized on your assets such as

a car or house—and bringing them within one or more whole life policies, you suddenly buy yourself a whole *lifetime* to plan your financial strategy. You no longer have someone sending you threatening letters, making nagging phone calls, or repossessing your car, if you get laid off or have other financial hardships.

Especially in this awful economy, the psychological benefit of owning your debt should not be underrated.




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#### References

1. Specifically, my September 2012 article was on “Why Dave Ramsey Is Wrong on Whole Life.” Also related is my June 2013 article, “Does IBC Mix Two Goals Inefficiently?” in which I showed that it made sense to use a single financial instrument—namely a whole life policy—as both a savings vehicle and to provide death benefit coverage.
2. Credit card statistics taken from <http://www.creditcards.com/credit-card-news/credit-card-industry-facts-personal-debt-statistics-1276.php>, <http://www.nerdwallet.com/blog/credit-card-data/average-credit-card-debt-household/>, and <http://www.cbsnews.com/news/51-percent-have-enough-cash-to-pay-off-credit-card-debt-study/>.
3. By the way, I should clarify that I personally am not wagging my finger at households carrying credit card debt—I too behaved foolishly in my younger days and have not fully extricated myself from my poor decisions.