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Does IBC Work for Older People? Part 1 of 2

by Robert P. Murphy

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One Of the most common questions we get from the public is whether IBC “works” or “makes sense” for someone who is older and/or in relatively poor health. People naturally worry whether the “pure cost of life insurance”—which is more expensive for older and/or sicker individuals, of course— at some point could make IBC impractical. If so, would it be better for people in this situation to take out IBC policies on *others* who are younger and/or in better health?

My short answer is: no. Generally speaking, IBC “works” for anybody. To a first approximation, the higher mortality rate of an insured party has two opposing forces that roughly cancel out, as far as IBC goes: On the one hand, to achieve a desired death benefit level, an older and/or sicker person will have to pay a higher premium. But on the other hand, since that person is more likely to die, the *cash value* of that policy at any moment will be higher, than an otherwise comparable policy for a younger and/or healthier person. (Think of it this way: the life insurance company would be willing to pay an older/sicker person *more* to surrender a policy of a certain death benefit, than it would pay to a younger/healthier person to surrender a policy of the same death benefit.)

Now it’s true that the *growth* rate of the cash value will—other things equal—be lower for the older/sicker person, but that is counterbalanced by the fact that there’s always a greater chance of such a person dying and achieving the death benefit earlier. Once you take into account all of the relevant variables, the true “financial value” of funding a whole life policy on different types of people isn’t directly dependent on the age or health status of the individuals being insured.

To sum up, in terms of the big picture, yes, a person who’s older/sicker will have to pay higher premiums for a certain amount of death benefit coverage. But those higher premiums will be associated with larger cash values too. The cash value will tend to grow faster for the younger/healthier person (other things equal), but the market value of having such a policy in force is

IN THIS MONTH’S ISSUE:

- [Does IBC Work for Older People? Part 1 of 2](#)
- [Why We Need Hayek Today](#)
- [What’s the Rate of Return on an “IBC Policy?”](#)
- [Unlike Real Insurance, Social Security “Insurance” Creates Greater Risk for the Future](#)
- [A Parent’s Primer On Why College Is So Pricey—and What You Can Do About It](#)
- [Becoming Your Own Banker Part I, Lesson 2: How the Infinite Banking Concept Got Started](#)



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correspondingly lower, since there is less chance of getting the death benefit. To the extent that one also wants to use a life insurance policy as a cashflow management system—i.e. if you want to “become your own banker” as Nelson Nash recommends—then the various forces largely cancel out. You can effectively implement IBC with a dividend-paying whole life insurance policy, regardless of the age or health status of the person being insured (assuming the person can obtain a policy in the first place).

A Numerical Example

We have many experts in IBC who subscribe to the *Lara-Murphy Report*, including financial professionals and even insurance actuaries. So, with apologies to the casual reader who just wants bottomline “news you can use,” let me take the time to walk through a particular numerical example, illustrating the general principles I stated above.

Now the calculations in these types of analyses can get really complicated, really quickly. So in this article I’m going to make it as simple as possible, while still retaining the essence of our topic. To that end, I’m going to sweep away all of the overhead expenses—things like paying the salaries of the secretaries and maintenance staff for the home office—and simply assume that the life insurance company charges the *actuarially fair premiums* on the policies we will analyze. This is obviously unrealistic, but it makes our analysis very pure and crisp, so that we can isolate how an individual’s mortality rate affects the desirability of IBC.

Specifically, we’re going to look at a *single-pay* whole life insurance policy with a \$1 million death benefit. The first applicant is Healthy Hank, while the second applicant is Sickly Sam. They are both 116 years old when they apply for their respective policies. The contract specifies that each applicant will make a one-time premium payment at the start of the policy, after which the policy is fully funded. (Note that in this article, I’m not worrying about turning the policy into a Modified Endowment Contract [MEC] or other subtleties of real-world policy design. We’re just trying to keep the math as easy as possible to study the issue in question.)

Now each of these policies is designed to “mature” at age 121. In other words, even if the applicant is still alive, if he reaches age 121 then he gets paid the \$1 million benefit. This reflects real-world contract design, and also gives our math problem a nice terminal point, so we don’t have to keep carrying out probabilities forever when computing the financial value of an in-force policy.

To keep things simple, we are also going to assume a constant annual discount rate of 5 percent. (Think of this as the going rate of return on very safe bonds.) In these types of calculations, we need to take into consideration the time value of money, and for our purposes we’ll just assume a 5 percent annual interest rate.

With that framework in mind, Table 1 presents the theoretical cash surrender values for the policies on Sickly Sam and Healthy Hank, as well as the market

	<i>Theoretical (Not Statutory) Cash Surrender Value at Start of Year, When Turning Age...</i>					
Assumes Annual Discount Rate = 5%	116	117	118	119	120	121
Sickly Sam (50% yearly mortality rate)	\$955,658	\$956,883	\$959,454	\$964,853	\$976,190	\$1,000,000
year/year internal growth rate:		0.13%	0.27%	0.56%	1.18%	2.44%
Healthy Hank (10% mortality rate)	\$838,799	\$861,933	\$888,921	\$920,408	\$957,143	\$1,000,000
year/year internal growth rate:		2.8%	3.1%	3.5%	4.0%	4.5%
Zero-Coupon Bond (pays \$1m in 5 yrs)	\$783,526	\$822,702	\$863,838	\$907,029	\$952,381	\$1,000,000
year/year internal growth rate:		5.00%	5.00%	5.00%	5.00%	5.00%

Table 1. Theoretical Values for Two Whole Life Policies and a Safe Bond

values of a safe, zero-coupon bond that has a face maturity value of \$1 million.

The calculations underlying Table 1 are quite elementary, meaning that the interested reader can recreate it in Excel and explore other scenarios. Here, I'll explain just a few of the numbers to illustrate the pattern.

It's easiest to start at the end. Clearly, the market values of all three of our financial instruments will be precisely \$1 million at the start of the year when Sam and Hank turn 121. Their respective whole life policies "mature" or "endow" at that point, even if they are still breathing, and so they receive the contractual \$1 million in "death benefit." Like-wise, the holder of the bond at that moment also receives a cash payout of \$1 million, and so the market value of the bond (seconds before payment) must also be \$1 million.

Now let's go back one year, to when the men just turn 120 years old. The bond's present-discounted market value is simply \$1 million divided by 1.05, which works out to \$952,381 (rounding to the nearest dollar). Going the other way, if you start with \$952,381 in Year 120 and invest it to earn 5% in the bond market, you will end up with $\$952,381 \times 1.05 \approx \1 million in Year 121.

But now we move on to the more difficult computations. What is the *theoretical* cash surrender value for Sickly Sam's whole life policy, at the start of Year 120? (And by *theoretical*, I mean: according to textbook theory, just worrying about the pure, actuarially fair cost of life insurance, and the going market rate of interest. We're not worried about real-world statutory regulations or overhead expenses, agent commissions, etc.)

The textbook definition of the cash surrender value is something like: the present-discounted value of the actuarially expected death benefit, minus the present value of the expected flow of future premium payments. As time passes, the cash value on a policy rises, because: (a) the looming death benefit gets closer and closer, rising in present-value terms, and (b) with each premium payment made, there is one

fewer such payment due in the future acting as a "lien" against the death benefit.

In Table 1, though, I have made the cash value as simple as possible to compute, because we assume the only premium payment is made once, on the front end. So at any given time, the theoretical cash surrender value is simply the \$1 million death benefit, *adjusted* for the likelihood of payout (because of mortality) and the time value of money.

Calculating Specific Cash Surrender Values in Earlier Years

Let's return now to Year 120, and actually calculate the cash surrender values for our two policies. First, start with Sickly Sam. At the beginning of Year 120, there is a metaphorical coin toss, with a 50-50 chance that Sam dies and gets the full \$1 million death benefit right away. Or, there's a 50-50 chance that Sam survives the year, reaching age 121 and then (at that time, twelve months in the future) gets the \$1 million payout.

(For purists, note that I am making this calculation easier than it would be in real life. In reality, it's not that individuals have a one-shot lottery at the start of each year, and they either die at that exact moment or live for another twelve months. But I want there to be only two components to each year's calculation, so I'm assuming this unrealistic model for life/death.)

Returning to Sam, at the start of Year 120: We have calculated that there is a 50% chance his whole life policy pays \$1 million right now, and a 50% chance that it will pay nothing now, and end up being worth \$1 million in one year's time. To compute the present-discounted market value of this asset, therefore, we say:

$$50\% \times \$1 \text{ million} + 50\% \times (\$1 \text{ million})/1.05 \approx \$976,190$$

Note that we had to discount the second term in the calculation by the prevailing discount rate of 5%, because that *future* cash surrender value is only available after waiting an additional year.

We'll do one more calculation for Sam, to make sure you the reader understand how it works. If we go back yet another year, to the start of Age 119, we reckon that there is a 50% chance of getting the death benefit of \$1 million right away (because Sam dies that year), plus a 50% chance that Sam lives until age 120, at which time the policy will be worth \$976,190. We therefore compute:

$$50\% \times \$1 \text{ million} + 50\% \times (\$976,190)/1.05 \\ \approx \$964,853^2$$

And so on, for the earlier values of Sickly Sam's whole life policy.

Turning to Healthy Hank, we'll calculate just the first number, to show the pattern. At the start of Year 120, there is a 10% chance that Hank will die, getting the immediate payout of \$1 million. There is a 90% chance that Hank will survive the year, in order to get his hands on a policy with a \$1 million cash surrender value twelve months later. Thus, the market value of his policy at the start of Year 120 is:

$$10\% \times \$1 \text{ million} + 90\% \times (\$1 \text{ million})/1.05 \\ \approx \$957,143$$

And at this point, I trust that the reader can figure out how the other values in Table 1 are calculated.

Reflections on Table 1

Now that we've explained how Table 1 was built, let's step back and consider its implications. In particular, does IBC "work better" for Healthy Hank than it does for Sickly Sam?

Obviously, Sam has to pay a higher one-shot premium. After all, he is much more likely to die in any given year than Healthy Hank, and—by construction—we designed policies that both have the same \$1 million in death benefit coverage. So clearly, Sickly Sam's premium payment will be higher. (Next month, in Part 2 of this series, I'll consider a scenario where Sam and Hank make the same flow of *premium* payments, where their different mortality rates will then show up in different amounts of death benefit coverage.)

In our hypothetical example with no overhead expenses, to get into his policy, Sam would need to pay the "fair" market value of \$955,658 at the start of Year 116, for a fully-paid up policy with a face death benefit of \$1 million. In contrast, Healthy Hank only has to pay \$838,799 for the same policy.

But notice that the available cash values—which they can obtain by surrendering the policy, or which can serve as collateral for policy loans—are different. Again, in our hypothetical world of no overhead or other frictions, the full single-pay premium is immediately reflected in the cash surrender value. So yes, Sickly Sam has to pay more for "the same" policy, but he has a higher cash surrender value right away. And notice this holds for the entire life of the policy, too: In every year during the development of the policies, Sam's has a higher cash value than Hank's. The men only have the same cash value at the very end, when both policies mature and reach \$1 million in cash value.

In Part 2 of this series, I will go through a more complicated example, where Sickly Sam and Healthy Hank pay *annual* premiums on their whole life policies. But for our purposes in this introductory piece, I wanted there to be as few moving parts as possible. As Table 1 shows, Sickly Sam isn't a fool for taking out an IBC policy on himself; all of his money goes toward his cash value, just as the case for Healthy Hank. It's not the case that of his initial premium payment, Sam would see more of it "burned up by the pure cost of insurance," compared to Hank, if what we *mean* by that is: How much of the initial premium payment showed up as cash value?

Let me shout once again from the rooftops: *These are very simplistic calculations, relying only on hypothetical mortality rates and the market rate of interest.* In the real world, there are many other factors at play. But in this article, I want to show the reader that your intuition about how "the pure cost of life insurance" interacts with premium payments and cash value, might not be correct.

“But What About the Internal Growth Rate? Isn't Dave Ramsey Right After All?!”

At the risk of having some casual readers merely look at Table 1 without reading the article, I decided to include the annual growth rates of the market values of the three assets as well. A quick glance probably confirms the intuition of people who think, “Surely it's less efficient to implement IBC on someone who's older or in poor health, because there's more ‘drag’ on the policy being eaten up by the higher pure cost of life insurance.”

And indeed, that *does* seem to jump out of Table 1, doesn't it? After all, we can see that the growth rates of the cash surrender value for Sickly Sam are very modest, while they are much higher for Healthy Hank.³

And should Dave Ramsey happen to see this article, he would no doubt look at the even higher rates on the simple bond, and exclaim, “I told you so! You don't want to use life insurance as an investment vehicle. The performance on the insurance company's portfolio gets diluted by the pure cost of life insurance, and that's especially true if you are older or sick.”

Not so fast. As I pointed out in my full response to his arguments about permanent life insurance—available in the September 2012 issue of the *Lara-Murphy Report*—Dave Ramsey disregards the financial value of having an in-force life insurance policy. Yes, looking at Table 1 and if we only worried about rates of return, you would be a fool to buy a whole life policy (rather than a bond) *if you knew for sure that the insured party would live to age 121*. But of course, a major element in a life insurance policy is that *the insured party might die*, entitling the beneficiary to the full death benefit ahead of Age 121.

To illustrate what I mean, let's do a really simple comparison. Suppose Sickly Sam is in Year 120, and he's trying to decide whether to put his money in a whole life policy on himself, or in a safe bond yielding 5 percent. A very naïve reader of Table 1 might advise Sam, “Clearly you should opt for

the bond. Either way, you end up with \$1 million, but the bond only costs you \$952,381 to ‘get in’ at Year 120. Then you earn a 5% return, with the bond paying back \$1 million a year later. In contrast, you have to pay a one-shot premium of \$976,190 to get your whole life policy at age 120, in order for you to earn a mere 2.44% of internal growth before it matures and pays \$1 million a year later. This is a no brainer.”

However, such advice is totally wrong. It overlooks the possibility that Sickly Sam *dies* in Year 120. In that event, the bond doesn't do anything special; it still pays \$1 million the next year. But the life insurance policy pays \$1 million right away, and the person running Sam's estate can then invest it for the prevailing 5% return in the market, yielding \$1,050,000 the next year.

Thus, at the start of Year 120, if Sam buys the whole life policy, he expects: (A) a 50% chance of dying and ending up with \$1,050,000 in his estate a year later, and (B) a 50% chance of living and getting \$1 million a year later. The statistically “expected” value of this investment would therefore be \$1,025,000, in the Year 121.

And now the grand finale: Sam, at the start of Year 120, has just calculated that in one year's time, his life insurance policy will cause his estate to have a statistically expected \$1,025,000 extra. And what is the *present* value of that future possibility? Well he just discounts it by the interest rate, to calculate $\$1,025,000 / 1.05 \approx \$976,190$, which is exactly what Table 1 shows is the actuarially fair cash surrender value / single-pay premium payment for this policy.

IBC isn't magic. You aren't “cheating” or “taking advantage” of the life insurance company if you practice IBC on someone who is young/healthy, and likewise you aren't getting ripped off if you practice IBC on someone who is older/sicker. Nelson Nash discovered a way to build a cashflow management system on top of conventional life insurance, and this insight holds true regardless of the person being insured.

Conclusion

In this article, I tried to clarify for sophisticated readers some of the conceptual issues at play in whole life insurance policies. If we sweep away the complications of overhead expenses, agent commissions, the possibility of policy lapses, etc., then we see that the relation between a one-shot premium payment and the corresponding cash value of a policy is the same, regardless of the health of the insured individual. It's true that the rate of growth of the cash surrender value (other things equal) will be greater on the healthier individual, but that doesn't mean a whole life policy on a relatively unhealthy person is a "bad asset." Precisely because such a person is more likely to die, the value of having in-force life insurance (holding death benefit constant) is greater, on such a person.

In the real world, there are many complications that this article assumed away, in order to focus on the particular issue of mortality rate and policy performance. Before making any major decisions involving an actual whole life insurance policy, you should consult with the graduates of our authorized IBC Practitioner Program, available at: www.InfiniteBanking.org/Finder

References

1. I acknowledge the helpful feedback from Ryan Griggs on an early draft of this article. (It should go without saying that Carlos Lara reviews all of my *LMR* articles before we go to print.)
2. For the extreme purists who are double-checking these numbers at home: The calculation of \$964,853 for the Cash Surrender Value in year 119 for Sickly Sam is a dollar higher than what you'd get if you did the calculation spelled out in the text. The reason is that there is rounding; the actual value of \$976,190 shown in the table is shaving off some decimals, which are enough to make the actual (rounded) value for Year 119 go up to \$3 for the last digit rather than \$2.
3. To get some intuition of why Sam's policy behaves this way, consider: He has a 50-50 chance

of dying each year, and so his policy always starts out with at least \$500,000 in "expected" value, just from that component. In contrast, Hank's policy only has a "floor" of \$100,000, with the rest being built up on the working-backwards-from-the-last-year component which is constantly discounted by the interest rate as we move to earlier years. That's why, as we move back in time, Hank's policy gets "compressed" more, with each passing year. Yet that's just another way of saying that the growth rate *going forward in time* is higher for Hank's policy.

Why We Need Hayek Today

Hayek argued that we should embrace the idea of a society based on the liberty of its members to find fulfillment in their lives by themselves.

by Kai Weiss

One hundred and twenty years ago today, on May 8, 1899, Friedrich August von Hayek was born in Vienna. The 1974 Nobel Prize winner in economics would go on to live, as Peter Boettke puts it in his recent edition of *Great Thinkers*, quite the life.

... one filled with up close witnessing of man's inhumanity in World War I, the economic ruin of the Great Depression, and a dangerous game of brinkmanship with respect to Western civilization itself, with the rise of fascism and communism in the 1930s and 1940s.

In the end, he would become one of the most influential thinkers of the century, providing the intellectual ammunition for the likes of Margaret Thatcher, Ronald Reagan, and Ludwig Erhard and serving as a hero for classical liberals and conservatives alike around the globe. Likewise, he was one of the main orchestrators of the creation of a movement in favor of classical liberal ideas, trying to bring together often antagonistic schools of thought, including the Austrians, the Chicagoans, and the German ordoliberals, particularly through the creation of the Mont Pelerin Society.

And yet, today, most people do not even know who Hayek is or what his main teachings are. Even

more disturbingly, some parts of the movement helped found see him, at worst, as a “socialist”—a good monetary economist, perhaps, but of no use on any other issues—and at best, a lesser Ludwig von Mises, a copycat who ultimately stole his mentor’s Nobel Prize. All of this is quite tragic. Especially in today’s world—with threats to our liberties arising right and left (quite literally)—Hayek’s incredibly deep system of thought, which spans across economics, law, culture, politics, and philosophy, is crucial.

Ideas of centralization are more en vogue in the West today than at any other point since the fall of the last ultra-centralized state, the Soviet Union, in 1989. One could perhaps assume that the 20th century overwhelmingly showed that mega-states and collectivism of any kind don’t work. Nonetheless, these utopian dreams have returned once more in recent years.

Centralization Doesn't Work

On the left, Bernie Sanders and Alexandria Ocasio-Cortez in the US, Jeremy Corbyn in the UK, and activists all across Europe hail the dream of socialism, all while its most prominent real-world example, Venezuela, is burning down in front of their eyes. The youth leader of the center-left Social Democrats in Germany proposed just last week that corporations such as BMW should be nationalized despite the fact that another socialist experiment, Eastern Germany, burned down right in front of his eyes (he was born in West Berlin). All of these disasters were not “real” socialism, of course (it never is), but the next attempt will surely work. To defeat the greed of the free market, it needs to be replaced by a powerful government.

The right is not much better at this point. Nationalists around Europe, from Marine Le Pen in France to Matteo Salvini in Italy, attack capitalism as ferociously as the left does. But unlike in socialism, the economy isn’t really that important. The nation itself is on the line, and everything needs to make way for its survival—regardless of whether it’s free trade, immigrants, or even the rule of law, as in

Hungary.

In all of this, it is easy to forget that the status quo—the current political establishment—is not in favor of individual liberty and the market economy, either. Ever more centralization, for instance at EU institutions in Brussels but also far beyond the Belgian capital, is highly popular. A powerful government is yet again the answer.

Hayek’s work offers a powerful response to all these different demands that still sound so dangerously similar. More centralization cannot be the answer, regardless of who is proposing it. Jonah Goldberg was on point in a recent article when he called on conservatives to read Hayek once more: on the right,

the new proponents of "economic nationalism," no longer think elites can’t run the economy—just that liberal elites, or "globalists," can’t run it. Part of this stems from the often-paranoid conviction that liberal elites have brilliantly rigged the system in their favor. So, the thinking goes, if they can pull that off, so can we. It doesn’t work that way.

The Power of True Liberalism

Demands for a powerful government, responsible for all areas of life, are misconstruing the world we are living in. For centuries, ever since industrialization put liberalism fully on the map, our world has grown more complex. Largely locally organized economies have grown into today’s global economy, where everyone can trade freely with one another (as long as governments don’t interfere).

Hayek called this international world the “Great Society.” And while this extended order certainly brought with it major breakdowns in communities and identities and always delivered (temporary) negative economic effects for some, it also brought forth the immense wealth and prosperity we enjoy today.

What can be difficult to understand is that this order is so complex that no single mind could direct it. With billions of people interacting with each other across thousands of miles every day, involved in economic processes in which products are created

by millions without anyone knowing each other, this order is difficult to comprehend. But it is the daily reality.

Who could ever take care of this all by him or herself without destroying the structure itself? Who could know every little detail on the ground, know what every individual, from the farmer to the factory worker to the Silicon Valley engineer, thinks and does at every moment in time? This complex order, if left to itself, can take care of its own functioning. All small parts of this fabric work together, and if one falls apart it will be replaced by another. But could any one human being alone take care of it all (or even produce something so simple as a pencil for that matter)?

A benevolent dictator—or president or even parliament—in charge could try to organize all of these activities. But he would fail. And with it would perish the complex order itself. It would be impossible to still function by itself, being intruded upon constantly. Individuals could not do what they want to do anymore. It would only be the wise man or woman making the decision. Poverty and a significant loss in liberties would be the result.

Outcomes over Intentions

Yes, the intentions of those in charge may be well and good, but the actions would prove disastrous. Bernie Sanders, while trying to help the poor in the US, would impoverish them, along with "The 1 Percent," by taking away all their means to prosper.

Marine Le Pen, while trying to protect the French nation, would create a wholly different, autarkic France, which would, from there on, merely follow the road to serfdom until authoritarianism eventually fully prevailed because everything that is not furthering France, in her mind, would have to be eliminated.

As Hayek wrote,

Once you admit that the individual is merely a means to serve the ends of the higher entity called society or the nation, most of those features of totalitarian regimes which horrify us follow of

necessity.

Instead, Hayek argues, we need to let go of these dreams. We should instead embrace the idea of a society based on the liberty of its members to find fulfillment in their lives by themselves. Instead of central planning by one, the individual planning of each member of society, coinciding with one another, would prevail. Hayek saw the role of the government in this as one of an English gardener: one who lays the groundwork and prevents any clear and damaging breaches of the overall structure but does not interfere actively in its processes—or tries to design it all by himself.

This does not mean that the economy could simply do whatever it wants. Indeed, as Hayek pointed out, a free economy would also need the moral foundations that supplement the economy and prevent it from going rogue. Social institutions, mores, traditions, and habits, which have been developed over decades and centuries not by government but by the actions of individuals themselves interacting with one another, would act as a check against those results of the market we do not like. That is, a free society would need a healthy civil society next to a free economy.

It is here where many of today's classical liberals can also still learn something from Hayek. A society that is not allowed to critically examine any outcomes in the economic realm, even if there are clearly adverse consequences in other orders of the society, such as a further breakdown of social institutions, would fail completely—and it possibly does at the moment.

It does not have to be this way. Liberalism can survive. It is what Hayek coined "true individualism," based on the view that free individuals are born into a society, a family, and other institutions and that human relations will influence individuals at every point in their lives as much as individuals influence their surroundings. Humans are social animals, not rationalistic animals striving for their maximum economic gain.

This individualism is based on the belief that orders are created spontaneously, not centralized, and

that traditions, social rules, and institutions—that is, culture—do matter. And that humans, because they are social animals, sometimes prioritize other things in life more than simply economics. That they have an innate need for a sense of belonging, for an identity that goes beyond oneself, and for strong communities that can help in times of personal crises. And yet, it is also based on the realization that a free economy, undisturbed by constant government intervention, can be pure dynamism for one's own community or country but also humanity at large—and for every member of society.

Decentralism and localism on one hand, the market and the global on the other. They might seem contradictory at first. But what Hayek showed is that with the right mix of the two, they prove most successful. It is liberalism that is both attractive as well as sustainable. And it is the kind of liberalism we need today.

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What's the Rate of Return on an "IBC Policy?"

Confronting Investment-Thinking in Capitalization Strategy

by Ryan Griggs

Why the Question Comes Up

Folks who have just heard about the Infinite Banking Concept (IBC) are quick to ask: "what's the rate of return?" After all, aren't we dealing with a financial asset? Surely, it must have some rate of return. Don't we want our money working hard for us? If the rate of return is low, what's the use? Plus, isn't the IBC implemented through dividend-paying whole life insurance? Everyone knows that the "rate of return" in whole life is pretty low—certainly lower than the annual average return in, for example, the S&P 500. I don't know about you, but *I'm pretty skeptical*.

Just like that, the IBC-neophyte has painted himself into the semi-certain conclusion that this IBC business is probably a waste of money. This initial

skepticism makes it pretty difficult to convey the power of the IBC.

In addressing this question, we need to begin by pointing out where this type of question originates. *Why* is it that we are conditioned to wonder about rate of return when it comes to analyzing financial assets? Why don't we immediately wonder about, for example, the contractual guarantees associated with the value of the asset?

The answer is that we have been programmed to evaluate financial assets in the paradigm of *investment*. Americans are taught that the only sensible thing to do with savings is to invest. Everyone knows that investment comes with *risk*—the chance of total loss. Risk bears cost, so in order to tolerate the cost of a certain level of risk for a given investment, the individual (and the market) requires some rate of *return*. The higher the return, the better compensated the individual—or so the thinking goes.

If we follow this line of thought, we cross a number of familiar bridges. We can discuss how higher risk doesn't necessarily mean a higher return. We can point out the difference between *average annualized* rate of return and *actual compounded rate of return*. We can talk about how, in general, the stock market goes up, and that to avoid making psychologically motivated, uneconomic decisions, we might use dollar-cost averaging and systematically put a fixed amount of money into a low-cost, indexed mutual fund.

What advocates of the IBC often fail to realize is that **this is a losing argument**. The individual who has consumed the conventional financial literature is armed to the teeth with all sorts of mechanisms and strategies to confront the fact that every so often investments lose value. And for all intents and purposes, they're right. Even if they aren't right, let's assume they are. The following point still stands true.

If the focus is on the rate of return, then you've missed the point of the IBC.

Exit the Investment-Only Paradigm

Investing is not the only use of savings. Another use for savings is **capitalizing**.

Capital is the money value of property that we use to acquire other property. It's property value that we use to acquire other stuff. It's equity in a house; it's the value of deposits in a checking account; it's the cash value of dividend-paying whole life insurance. Regardless of the form in which it might manifest, **almost no one** in the financial advisory community suggests that individuals strategically accumulate it.

Since we are not taught to strategically accumulate capital, we rely on the capital of those individuals and institutions who do. We borrow from investors, banks, mortgage lenders, credit card and consumer credit companies in order to pay for the things we need. Or, we strategically plan to *liquidate capital*, also known as "paying cash." Thus, the two most popular methods for using capital consist of either **dependency on third parties or capital liquidation**.

The costs of both of these are huge. In terms of dependency on third-party lenders, all sorts of costs accrue to the individual borrower-consumer. In housing, we are hood-winked by single-digit APR, yet effectively pay ~40–55% in interest by volume (total interest and fees divided by the total payments on a mortgage). With automobiles, retailers boost the list price of the vehicle in order to advertise alleged no-interest or zero-interest loans, thereby smuggling the finance charge out of the interest charge and into the retail price. Because credit card interest charges aren't amortized, the APR is huge, and the consumer is lured with initial teaser rates.

And that's just the monetary charges! The individual concerned about the rate of return in an "IBC policy" probably has not accounted for the dollar-cost of the hours of their (non-reproducible) time spent securing financing, arguing with lenders, or restructuring repayments. Yet, all of this bears costs. Equally unlikely is it that the individual has priced the risk of a loan—especially a business loan—getting

called due (either because the bank needs to raise capital, is bought out during an economic downturn, etc.). Yet, this too bears costs. In sum, the lengthy applications, use-restrictions, physical collateral assignments, mandatory repayment schedules, hostile bill collections departments, and the various risks associated with the above constitute a massive cost that usually goes unaccounted for in typical rate-of-return analysis.

Capital liquidation (paying cash) bears costs too. Every dollar that flows out of one's control has a present value opportunity cost. That means all the interest and dividends that the dollar could have earned had the individual first contributed to his own capital is gone. In other words, the capital liquidator actively inhibits the growth of his own capital over the course of his lifetime.

The individual pays the monetary and non-monetary costs associated with reliance on third-party lenders and/or the opportunity costs associated with capital liquidation because *he lacks optimal capital of his own*. He lacks capital of his own because no one has told him that *capital is distinct from investment*. Whereas capital is property value used to accumulate wealth, investment is an allocation of resources to generate a return. This key distinction has a major implication. That implication has to do with **control**.

With investing, the whole idea is to forfeit control of resources to the recipient of the investment. With capital, the whole idea is to maximize control of resources under the authority of the individual.

Dividend-paying whole life insurance designed for the IBC is a tool for optimal capital accumulation. It is not an investment and it should not be analyzed like an investment.

Do "IBC policies" have values that grow over time? Yes. Do those values grow at some rate? Yes. But the salient features of an IBC policy have little to do with these positive growth rates. In fact, the positive growth rates of the values in "IBC policies" (cash value, dividends, and the death benefit) are *bonus features*. An "IBC policy" is optimal for capital accumulation because it is implemented through a

piece of private property—a financial asset under the direct, contractual *control* of the individual. That its values grow is an *ancillary side-benefit*. That its values grow on a *guaranteed* basis with *highly favorable tax-treatment* is an *awesome*, yet ancillary, side-benefit.

In fact, as you may have sensed, there are benefits—plural—that accrue to the individual who practices the IBC. A legitimate quantitative measure—an aggregate rate of return, if you will—would have to price all of those features and permit of present value discounting. To be fully exact, one would have to also apply *expected* present

performance. This presupposes that the individual has understood the difference between capital and investment and recognizes the value in strategically accumulating and deploying capital.

This isn't a mutually exclusive question. It is not a matter of choosing to capitalize or to invest. This isn't a matter of trade-offs. It's a matter of *sequence*.

An individual can approach investing in one of two ways. You can be either *under-capitalized* or *well-capitalized*. Check out the slide below from the presentation I gave at the 2019 *Nelson Nash Institute* Think Tank Symposium for Authorized IBC Practitioners.

Investing & Entrepreneurship Opportunity

Opportunity for the *under-capitalized*

- Few, mass-marketed
 - FRB
- Chase the investments
 - Search costs
 - No resources for entrepreneurship
- *Bonus*: Exposed to conventional lending costs

Opportunity for the *well-capitalized*

- Many, local, exclusive
 - Repeat interactions, trust
- Opportunity is attracted to you
 - Entrepreneurial *and* investment (both?)
- *Bonus*: Eliminate conventional lending costs

Slide from Ryan's 2019 NNI Think Tank presentation

value analysis, since, if the insured were to pass away in a given year, the payment of the death benefit would cause whatever the aggregate performance metric is to skyrocket. Complicating matters further is the fact that these figures, discount factors, and mortality expectations will differ for *every person* and it would differ for *the same person* over time.

Various IBC Practitioners have tried to quantify the benefits of the IBC. I believe that, in terms of technical logic, it cannot be done. The benefits are too many, and the value of them are subjective and diverse.

The Real Key to High Rates of Return

However, an individual investigating the IBC may still be curious about optimal investment

In short, opportunity abounds for the well-capitalized—that is, opportunity of both the *investment* and *entrepreneurial* types. Individuals with control over large pools of financial value (capital) are well-positioned to take advantage of local, perhaps even exclusive, investment opportunities. These are investment opportunities of a categorically different nature than that of the mass-marketed, relatively homogenous, impersonal, Fractional Reserve Banking-risk-exposed options available to the *under-capitalized*.

Where the greatest percentage-gains may lie is in entrepreneurship—the monetization of one's unique skills and abilities. The modern financial advisory paradigm that prioritizes investment to the exclusion of any sort of capital accumulation

leaves the individual utterly bereft of the resources necessary to finance an individual's transition into self-employment or business ownership. Whereas the very concept that, if implemented, would optimally prepare the individual for entrepreneurship and its potential rewards is the target rate-of-return skepticism.

Frankly, the dynamics offered in the conventional investment paradigm pale in comparison to the (investment and entrepreneurial) opportunities the well-capitalized individual can enjoy. Sadly, many who investigate the Infinite Banking Concept neglect *their own potential* to encounter and seize these opportunities with proper preparation. Not least of the benefits that accrue to the well-capitalized "Infinite Banker" is the *autonomy* that comes with possessing such contractual control. Two things are certain of this financial power: it is of unknown magnitude and it is *consistently unaccounted for* in conventional rate of return analysis.

Finally, the *well-capitalized* will enjoy a phenomenon rarely understood in the financial world. This is the feeling of *opportunity attraction*. Everyone knows at some level that people with money have the unique problem of overwhelming petitions from *other people* for the use of *their money*. The well-capitalized face the opposite problem of the under-capitalized. Instead of *seeking after* opportunity (and having to pay costs which then must be minimized through various fund allocation strategies), the well-capitalized are *sought after* and *presented with* opportunities. This is why people with money often hesitate to tell others how well-capitalized they are. The tsunami of opportunity can be overwhelming.

Therefore, if one is truly concerned with optimal investment performance, the question ought to be: how best should I prepare? Answer: first become *well-capitalized*. Or, in the language of the IBC, *Become Your Own Banker*.

In Conclusion

We've covered a lot of ground. We talked about how investment analysis is inappropriate for

investigation of the IBC or the policies used in order to implement it. Dividend-paying whole life is not an investment. In contrast, it is the optimal tool for capital accumulation. In fact, the individual who opts out of the conventional financial thinking and capitalizes *first* will often experience a paradigm upgrade when it comes to investing. Rather than playing the role of *opportunity-seeker*, the well-capitalized individual becomes *sought after* by those with opportunities. In sum, rate of return analysis is categorically insufficient for capturing the power of the IBC due to the multitude and variance in kind of the many benefits it affords the individual.

Thanks for reading!

Article was first published on Medium.com

Unlike Real Insurance, Social Security "Insurance" Creates Greater Risk for the Future

by Gary Galles

Every time the Social Security trustees issue their annual report, some people notice that the system's huge unfunded liabilities (currently, a \$42.1 trillion cumulative shortfall) are inherently unfair to future Americans. That threatens its status as the "third rail" of politics, which electrocutes anyone who tries to touch it.

So Social Security's army of defenders go on the attack. And one of their greatest weapons is that the program has been promoted as insurance program ever since it started and taking away insurance sounds like a bad idea.

In a sense, Social Security does act as a form of mandatory old age insurance for participants. However, rather than paying off with earnings from investments, as with private insurance, its taxes provide only promised future government benefits (though the Supreme Court long ago ruled in favor of the government's claim that it did not need to provide the benefits promised).

However, for Social Security to really be insurance,

a group's "premiums" would have to finance the benefits they receive. But that has not even remotely been true of Social Security. Older generations got far more in benefits than they paid. They may believe they deserve a massively subsidized deal (especially when it is falsely presented as if early recipients actually paid all the costs of their benefits), but that deal is dramatically unfair to younger generations forced to pick up the multi-trillion dollar bill to make good on program promises.

And this is where a key distinction must be noted. In real insurance, people pay more now so that they will have more assets in their future. But Social Security has transferred money in the opposite direction — giving more money to those currently older at the expense of subsequent generations. From society's perspective, then, Social Security acts as reverse insurance, leaving less for the future.

At Social Security's inception, and with each of its many expansions, those already retired paid no new taxes, and those near retirement paid more for only a few years, but both groups received increased benefits throughout retirement. That necessarily meant that those who were younger (including those not yet born) would have to pick up the remainder of their tab. And the attempt to make good on the unfunded commitments of this massive income redistribution to earlier beneficiaries is the source of Social Security's current financial problems, as well as why there is no fair way out of them--there is no way to make good on its over-promises but by being unfair to someone.

Social Security's reverse insurance accumulation of negative balances is also used to oppose any attempt to shift toward private retirement mechanisms. Under private insurance, current workers finance their own retirement benefits — and only their benefits. But if those younger could access such options to escape having Social Security's huge unfunded liabilities imposed on them, someone else would necessarily be left holding the bag. So politicians instead pander to seniors who are much more likely to be politically engaged and vote than the young, by demonizing any such move as

threatening the status quo, even though the status quo is unsustainable anyway.

Looking at Social Security's finances as of a certain future date, while depressing, injects a similar bias in favor of the program. It means that trillions of dollars owed to those who have paid in, but who have not yet received all their promised benefits, can be made to disappear from public view. However, such arbitrary cut-off dates misleadingly make any private retirement mechanism, which produces no such "hidden" burden on later generations, look worse by comparison.

Assertions that Social Security is essentially just insurance, good to have in an uncertain world, so that it should be politically untouchable, ignore the fact that benefits far exceeded "contributions" paid for earlier recipients every time it expanded. The great deal it offered them was provided by stealing a substantial part of what would be actuarially fair premiums from future generations. But that makes it a bad and unsustainable deal today, which will only get worse the longer we ignore that reality. A program which leaves fewer resources for future Americans is the opposite of insurance, which doesn't justify maintaining or expanding it on the backs of younger generations who are already big losers from the system. If we are to make rational policy in this area, we need to confront this government-sponsored "child abuse," rather than letting a rhetorical cheat "insure" that it is overlooked.

Gary M. Galles is a professor of economics at Pepperdine University. He is the author of *The Apostle of Peace: The Radical Mind of Leonard Read*.

Article was originally published on Mises.org

A Parent's Primer On Why College Is So Pricey—and What You Can Do About It

All of this talk about free college and student loan forgiveness should lead us to wonder why college costs and debt are rising in the first place.

by Kerry McDonald

All of this talk about free college and student loan forgiveness should lead us to wonder why college costs and debt are rising in the first place. Not that long ago, many of us paid for much or all of our college tuition—even at private institutions—by working campus and summer jobs. Now, that seems laughable, particularly when some colleges and universities charge more than \$70,000 a year.

What is causing these soaring college costs and debt burdens, and what can parents do about it? Here are three reasons higher education is expensive and three suggestions for how parents can cope:

1. Administrative Bloat

Parents may not fully appreciate how big and bureaucratic higher education has become. I certainly didn't until I learned about "administrative bloat," or the expansion of higher education administrators and student support services that have nothing to do with teaching and learning and a lot to do with jacking up college costs. Mark Perry, a University of Michigan economist, determined that in his university system alone there are nearly 100 "diversity, equity, and inclusion bureaucrats," or what he calls "diversicrats," and a quarter of them make over \$100,000 a year.

Throw in generous employee benefits packages, and these administrators cost the University of Michigan \$11 million every year. It's no surprise that tuition and fees for in-state students at this public university top \$30,000. The work these staff members and others do may be worthwhile, but most parents think they are paying hefty tuition bills to expand their child's knowledge and inquiry—not to

subsidize administrative bloat.

It's a common narrative to blame declining public support for increasing costs at public universities, but that ignores the alarming trend of rising administrative costs. As HuffPost reported:

The number of non-academic administrative and professional employees at U.S. colleges and universities has more than doubled in the last 25 years, vastly outpacing the growth in the number of students or faculty, according to an analysis of federal figures.

This bureaucratic bloat would be unsustainable in most other industries, with customers refusing to pay for such inefficiencies. Yet, college costs keep rising, and parents and taxpayers largely foot the bill.

What Can Parents Do?

It's easy to be wooed by gleaming new buildings on campus and pamphlets showcasing the many non-academic student services and programs available, but parents and students may want to connect the dots and realize that they are paying for these extravagances. Maybe they don't mind, but if it troubles them, then looking toward leaner colleges and universities that prioritize teaching over administrative staff may be the way to go.

2. Government Subsidies

While parents should be more discerning about where their child's tuition costs are going, parents as taxpayers should also be leery of investing more in higher education. According to Todd Zywicki and Neal McCluskey, editors of the new book, *Unprofitable Schooling: Examining Causes of, and Fixes for, America's Broken Ivory Tower*, government subsidies to colleges and universities have mushroomed. In an op-ed this week in *The Hill*, they write:

The problem is the entire Ivory Tower sits atop an ever-rising swell of subsidies. Between 1980 and 2018, inflation-adjusted state and local educational appropriations to colleges rose from \$50 billion to \$86 billion. Inflation-adjusted federal subsidies

to students ballooned from \$34 billion to \$154 billion.

They argue that this increased government spending has led to increased government regulation, which then “restricts what new models, such as low-cost online education, can viably enter the market.”

Newer, private for-profit and non-profit colleges and universities often get blamed for higher student loan burdens or lower completion rates, but these criticisms fail to acknowledge that these emerging higher education programs often serve students who are currently not being served by conventional college systems. Older working students, veterans, single parents, and others may choose newer for-profit or non-profit higher education programs because of their comparatively lower costs, more flexible scheduling options, online offerings, workforce relevance, and agile programming.

These alternative higher education programs meet student demand in ways that traditional colleges do not, and they are increasingly threatened by government regulators for doing so. Writing recently at RealClearEducation, Cherylyn Harley LeBon explains:

Some politicians in Washington are waging a concerted and deceitful effort to make it difficult for private, for-profit and non-profit colleges to exist.

She argues that one reason for the attack is to protect public higher education programs, especially community colleges that have seen declining enrollment in some areas.

What Can Parents Do?

Do your research on the college or university programs that your child is considering, and recognize that there is risk in any investment; but don't rule out newer, private for-profit or non-profit higher education programs. Sometimes these innovative programs cost less, are more responsive to student needs, and can add value where traditional programs cannot.

3. Low-ROI Majors

While not directly related to college tuition increases, parents should be aware of how their child's chosen major can influence the full cost of a college degree. Certain majors are more likely to lead to burdensome student loans that can be difficult to pay off. The Brookings Institution's Hamilton Project found that those with a college degree on average make more throughout their lifetime than those with only a high school diploma, but earnings vary dramatically by college major.

College graduates with majors in engineering, computer science, operations and logistics, physics, economics, and finance had the highest lifetime earnings, while graduates with degrees in early childhood education, family sciences (home economics), theology, fine arts, social work, and elementary education had the lowest lifetime earnings. With student loan debt a concern for the majority of students, it makes sense to evaluate the return on investment of a college major and its potential career path.

If a certain major will result in jobs that make it more difficult to pay off loans or pay them off more slowly with accruing interest payments, then parents and students should recognize the higher financial costs of their college investment decision.

What Can Parents Do?

As a parent who may be helping to pay for your child's college degree or who would like to help your child avoid hefty student loans, you can encourage your child to major in a subject that yields a better return on investment. If your child's passion is fine arts or social work, then perhaps suggest that she double major in economics, as well.

It's also important to note that education is a human activity, but college is a purchasable good. As with any purchase, the consumer needs to be aware of the full cost of a college degree; but there are other ways to be educated, and have a good life and livelihood, without college. Recent research shows that vocational education increases lifetime earnings

and can be a secure career pathway.

Apprenticeship programs offer an alternative to college by providing a signaling mechanism for potential employers that goes beyond a degree or credential. And more big companies like Apple, Google, and Netflix no longer list a college degree as a requirement to get hired for certain high-paying jobs.

College costs are rising for a variety of reasons, including more bureaucratic indulgences and more government regulations, and student loan debt is ballooning. Parents can help to control these costs by being more discerning about various college offerings and expenses, guiding their child to consider leaner or more innovative higher education programs, and suggesting college majors that will most likely enable that college investment to pay off with the least debt.

Moreover, parents as taxpayers can hold off on supporting more public funding for higher education—at least until they see if their tax dollars are actually going toward a more educated citizenry and not some college bureaucrat's six-figure salary.

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Second 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 I, Lesson 2: How the Infinite Banking Concept Got Started. Content: Page 12, *Becoming Your Own Banker; Fifth Edition.*

Welcome back to lesson 2. It will probably be useful for you to understand just how this concept came into existence. We are all products of our prior understanding of things. First of all, my initial college degree is in the field of forestry, graduating from the University of Georgia in 1952. A large portion of the root thought of this concept is coming from the study of forest finance -- the fact that you are dealing with compound interest over a long period of time with no taxation on the build-up. The reverse fact is that you must make an investment in planting trees and you won't see any financial return for that same long period. In the forestry world one must think many years into the future.

Some of it is coming from the life insurance business. I made a good living in life insurance sales for 35 years. Knowing how dividend-paying life insurance works is an essential ingredient to it all. Most people have a minimal understanding of the subject, including the home office personnel at life insurance companies. That may seem strange to you, but it is very true. In fact, a case can be made that it is probably the most misunderstood subject in the world.

Lastly, it was strongly influenced by my experience in the real estate business. Recalling that I was educated as a forester, timber is real estate as well as the land on which it grows, so I have been around real estate for all my working life, and I developed a deep interest in the subject and studied many books on it. If you read those books, the central message is not about real estate at all – it is about the magic of leverage! Essentially, they all say, “Buy some real estate, borrow the money to pay for it (because you are always dealing with borrowed money -- you either borrow money and pay interest or you use your own money and give up interest that you could have earned elsewhere) – pay interest for a while, then sell the property. All you have given up is the interest you have paid out. That leverage is wonderful.”

That is all true – as long as things are going the way the “financial geniuses” describe it in the books. But they

never tell you what happens when the lever goes the other way! Frankly, I made some money in the late 70's doing it the way the geniuses explained it. By the way, there have been a number of people who have observed that "financial genius" is a rising market. There were several successful ventures in a row, and it looked like there was no end to this bonanza. I could do no wrong! The ventures got bigger and bigger and I got more involved, buying a large number of acres of rural property.

And then I got into real estate development. With the profits from one small parcel, my wife and I went to Europe in 1977 and spent a month! Would you believe it – I have never seen that property yet? I don't even know where it is! And I did it all according to the "book by the financial geniuses" – leverage – other people's money. Just have your realtor find such a deal and attend to all the particulars for you – and then sell it for you. Marvelous!

There was no logical reason not to expand – and so I did. The interest rate (they called it "the prime rate" in those days – now called "base rate." This is the rate charged to the bank's most secure customers) at that time was 8%, but you must pay 1.5% over "prime" because you are not in that category. They are not lending you money because you have real estate – they are lending you money because they think you can make payments. Why else would they require personal endorsement on the loan? And you must renew the notes every 90 days (or pay off the loan) at the current interest rate.

I got accustomed to paying 9.5% and that was "normal." And then, along came 1981 and 1982. The prime rate rose and peaked at 21.5%! Add 1.5% on top of that and you see my situation – 23% interest – and I owed them \$500,000.00! That amounts to \$67,500 of interest per year that I was not expecting to pay.

When this happens to you, what do you do? Go as the "financial geniuses" that recommended that you do this and ask, "What do I do now?" If you can find them, they may mumble something about "selling the real estate." But where do you find a fool who will buy it under those circumstances? Of course, everything will

sell if you get the price low enough – but losing five times what you paid for it is hardly a good way out. You can see the predicament that I was in, but that is only part of my total situation. We will save that for Lesson 3. I'll see you there!

Authorized IBC Practitioners
<https://www.infinitebanking.org/finder/>

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

- Jake Chesney - Chicago, Illinois
- Bill Skinner - Williamsburg, Virginia
- Mary Jo Irmen - Bismarck, North Dakota
- Mark Mappa - Glenview, Illinois
- Wayne Durksen - Warman, Saskatchewan
- Isis Palicio - Coral Gables, Florida
- Kenneth Johnson - Columbia, South Carolina
- Bryan Nelson - Orange, California
- David Befort - Minneapolis, Minnesota
- Jim Buzhardt - Nashville, Tennessee
- Jim Oliver - Bonita Springs, Florida
- Colton McGriff - Birmingham, Alabama

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.