The Perfect Time for Whole Life

by Jerry Borrowman, MSFS, CLU®, ChFC®, CAP®, LUTCF

> Saving for the future with a whole life policy

I recently met with an extremely high net-worth client who has extensive experience in market analysis, real estate development and project management to discuss using whole life as a tax-efficient place to hold idle cash. His chief financial officer joined us. The client needs additional tax-free death benefit, and the current return on policy cash values is very positive relative to other cash investments, such as money market funds, CDs and fixed bonds.

In the course of the discussion I pointed out Internal Rate of Return (IRR) values at the current dividend scale, then indicated I wanted to show him how the policy would perform at a 50 percent dividend reduction and a 100 percent dividend reduction (zero dividends, in other words). He was surprised by that, asking, "Why would you show me zero dividends—it's not likely that will occur is it?"

"Not likely, particularly to fall to zero immediately," I replied. "But what we're finding is that many of our potential customers have convinced themselves that the economy is in for a very rough patch and they want to know exactly what is guaranteed and what is not." He nodded thoughtfully, and allowed me to show him the two scenarios. Of course even at a zero dividend rate, the guaranteed values of the policy grew from year to year. At the guaranteed rate, our policy IRR exceeds most of the alternatives currently available.

After absorbing the various figures presented, he turned to his CFO and said something that surprised me, and is very illuminating about the near perfect conditions that now exist for selling whole life. "This is pretty good when you consider the last 10 years in the stock market," he said. "It's no wonder that people who had their money in the market for 10 years with virtually no growth would be interested in something like this that guarantees against loss."

Our discussion then moved on to what happens to a whole life policy if inflation takes hold and interest rates rise. But I made a mental note of his comparison to the market of the last 10 to 15 years if you consider Japan's experience with deflation and essentially zero growth. In my opinion, people are more frightened by economic uncertainty today than during any other time in my 32 years since starting my life insurance career.

I was validated in this conclusion soon after when I read an article by the noted economist, Robert J. Samuelson, entitled "Great Recession Keeps its Stranglehold on the American Psyche." Samuelson explained that this is the...

> "...most egalitarian of all the 11 recessions since World War II," stating that "...In various ways, it has touched every social class through job loss, pay cuts, depressed home values, shrunken stock portfolios, eroded retirement savings, grown children returning home—and anxiety about all of the above. The Great Recession has changed America psychologically, politically, economically and socially."

Samuelson went on to identify four causes of America's angst and to assert that the group hit hardest (from a psychological point of view) is the middle class:

1. **Job loss.** The worst since World War II with unemployment among college graduates doubling to about 5 percent, and overall unemployment hovering just below 10 percent. Many professionals have been out of work for more than a year, with devastating consequences on their financial security and retirement plans.

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2. **Pay cuts.** Nearly a quarter of all workers, and 20 percent of workers earning more than $75,000 per year have experienced a decline in family income.
3. **Loss of housing and stock market wealth.** This decline, more than 25 percent at its peak, "has been concentrated among higher-income Americans, who own a disproportionate share of the wealth," said Samuelson. "A reverse wealth effect has gripped the upper middle class. Feeling poorer, people saved more and spent less."
4. **Children.** "All those jobless college grads and crashing kids must alarm their parents. Only 45 percent of Americans believe their children will enjoy a higher living standard, down from 61 percent in 2002. Pessimism is greatest among those with family incomes over $75,000."

Samuelson concludes his article with this chilling statement:

> "One legacy of the Great Recession is that insecurity and uncertainty have gone upscale. People feel more exposed. They tend to plan for the worst rather than hope for the best. Their reluctance to make major purchase commitments (a new car or home) validates their pessimism by retarding recovery."

Clients, including my own family, who own whole life insurance have experienced just one trend in the past 10 years—our net cash value and net death benefit have increased each and every year. And while returns on other fixed-rate products that guarantee principal have plummeted, whole life dividends continue to provide excellent value, both in real terms (as measured against inflation) and in relative terms compared to other products of a similar type. Consider how whole life has helped out in these challenging times:

- Tax-free death benefit reduces the uncertainty of financial loss due to an unexpected death.
- Strong dividend performance contributes to a positive increase in net policy cash value.
- Tax deferral saves taxes each year, which increases the effectiveness of policy cash value accumulation.
- Access to policy values through policy loans and dividend surrenders helps families in times of distress or to take advantage of opportunities.

A good friend of mine, Bruce Bowen of American Fork, Utah, shared the story of a phone call he received from one of his best business owner clients a year ago. This small construction company has purchased substantial whole life policies on the lives of owners and key executives through the years.

"Can you help me arrange a policy loan?" asked Bruce's client. "We've found a terrific opportunity to develop a piece of property, but the banks won't loan us any money." This in spite of the fact that the firm had excellent credit and a spotless credit history.

"Sure," replied Bruce, "How much do you need?" When the client told him, Bruce gulped. "Alright, let me call our Dallas Service Center and I'll get it right out to you."

Bruce went on to explain that he called his company, explained the situation, and the service rep said that for an amount that large she would input the request immediately and the check would be cut the following night. She even promised to send the check by overnight delivery.

"Literally three days after that call I had a check in my hand for slightly more than $1 million, which I drove over to my client. When I handed him the check, he shook his head and said, 'Buying these policies is the best thing we have ever done. I wish we'd bought more."

Bruce concluded his story by saying, "This client received the money they needed without any loan application, no loan committee—nothing! The money was simply there when they needed it. Of course, this client will repay the loan so the money is there when he needs it next time."

It takes both imagination and self-discipline to purchase whole life insurance. It requires a client to make the very sophisticated decision that they will give up current consumption to create future security and prosperity. In the heady days before the Great Recession many people in our society developed the notion that they did not need to save money because the relentless increase in home values and the stock market would allow them to spend whatever they desired today, with plenty of money to pay back the loans and still retire comfortably in the future. As the article by Robert Samuelson points out, that attitude has been smashed on the unforgiving rocks of economic reality. Even those who didn't lose their jobs, who still are on track for retirement, are uncertain about the future. Now, more than ever before, people are inclined to save for the future, and they hope that the money they save will be safe.

I believe whole life is one of the most effective places to ensure that. Congress has granted whole life three remarkable tax advantages only because of the great good it can do to provide financial security to families and business:

- A tax-free death benefit;
- Tax deferral for growing policy cash values; and
- Tax-favored access to policy cash values through surrender of basis first and tax-free policy loans.

There really is nothing else like it in the world. My only regret about whole life? That I didn't buy more.