Leading by example

Cash-value life insurance reliably builds wealth during a client's working years.

By John L. Gilfoil, CLU, CFP

My client, Muriel, and I go way back. We met in seventh grade — long before I knew that I would enter this business or that she would become my first client.

It wasn't easy when I first started out. Interest and unemployment rates were in the double digits. Income tax rates were at an all-time high. Competition was keen; 27 life insurance companies with nearly 500 sales representatives were soliciting business in my home city of Springfield, Massachusetts.

As I was completing my sales training, I called on Muriel. We had remained close all those years, and I thought she would be a good person to test my skills as a new financial advisor.

A typical 22-year-old, Muriel had a job, but no money in the bank, a fair amount of debt and no idea how to build a financial plan. During the fact-finding process, I learned that she wanted to save, but she had no idea how to design and implement a plan.

The plan we put together was very simple. We designed a budget that had her paying income taxes first. We then set a goal for her to increase her savings by contributing up to 20 percent of her gross income. That would be split between matched money in her employer's 401(k) plan, a money market fund and permanent cash-value life insurance. She used the rest of her paycheck to live on. We also put together a balance sheet showing her total cash and investments compared to her debt. We agreed that she would use one-half of any raises to pay down debt and the other half to get her savings contribution up to the full 20 percent. I had my first client.

Two years later, Muriel got married. That was when she saw her plan was coming together. She paid off all her debt. She and her husband, John, continued to follow the plan of saving first and spending whatever was left. They were able to buy a house and fix it up over time.

Three years into their marriage, they found their dream home. With two acres on top of a mountain with a barn, it would be the perfect place to raise a family. They secured an excellent purchase price since mortgage rates then were more than 17 percent, which also prevented them from selling their first home. By that time, they had just enough cash value in their life insurance programs along with funds from a few other sources to make a down payment on the new home. They rented their first home until the market improved. A few years later, mortgage rates came down, and their first house sold for more than double what they had paid for it. They paid back all they borrowed, set aside cash to improve their new home and refinanced it at a more reasonable fixed rate.

A baby soon came into the scene, then a second and a third. The couple wanted Muriel to stay home with their children. They purchased rental property and managed other investors' properties as supplemental income and potential wealth through real estate appreciation on the long-term. They continued to pay taxes first, save second and spend what was left as their income and assets grew.

Then the real estate market blew up. The tax incentives disappeared; positive cash flows were in the rear-view mirror. The banks called all their loans. John and Muriel were in deep financial trouble.

Fortunately, their reserves enabled them to continue paying for their mortgage on the house on the hill. It took almost six years for them to get back on their financial feet. Their dream of easy money through leveraged investment real estate hadn't come to fruition. With hard work and discipline, they stuck to their plan. Just as they could see the light at the end of the tunnel, they had three children in college at once, requiring them to again raid the cash value of their life insurance program. They planned to use other equity-based investments to help out, but the economic dip following the events of September 11, 2001, put the brakes on that plan.

Around that time, they came to a very interesting discovery: Their best investment over the long term was their cash-value life insurance. They originally bought it as a safe, tax-efficient supplement to their other investments. They wanted to have the death benefit and disability self-completion clause to protect them if the unthinkable happened. It turned out to be much more than they ever anticipated.

After the kids graduated from college, John and Muriel recommitted themselves to repaying those life insurance loans and rebuilding their cash accounts. They were very happy with the substantial amount of cash accumulation in their life insurance and looking forward to when they could spend some of their wealth on themselves.

When revisiting their goals, however, we found some new challenges. The couple's parents were seeing the effects of older age and the need for some sort of assistance. That wake-up call encouraged them to purchase long-term care insurance and put updated wills, trusts and durable powers of attorney in place. They moved a substantial amount of their life insurance into one of the trusts to ensure that it would replace any assets used for their care in their twilight years.

THEIR BEST INVESTMENT OVER THE LONG TERM WAS THEIR CASH-VALUE LIFE INSURANCE.

John and Muriel are now in their mid-50s and enjoying life. They belong to a country club in the summer and ski in the winter months. Their three children are now on the road to building their own financial plans.

Looking back over those three decades, I came to some conclusions. You can't wait until times are good; a good financial plan requires saving first and then living on what's left. Build a strong foundation made of insurance and savings, and then put higher-risk investments on top. We can't expect our clients to do something we don't do. Lead them by example.

I should probably mention that John and Muriel's last name is Gilfoil. ■