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FEBRUARY • 2017

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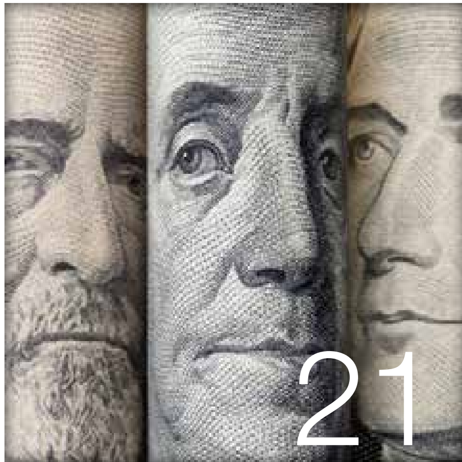

AN IBC TAX STRATEGY, PART II

BY L. CARLOS LARA

Last month we told you about a technique for redirecting large cash flows. This month we give some specific numbers.

REBUILDING THE WAY WE LEARN ECONOMICS

INTERVIEW

Jeff Deist, president of the Mises Institute, is a keen observer of politics and Austrian economics.

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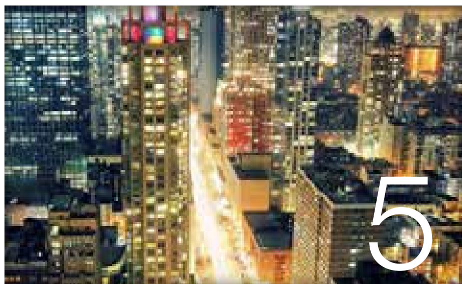

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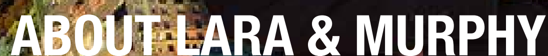
Learn more in person from Lara, Murphy, and other Austrian economists, at these upcoming appearances.



ABOUT LARA & MURPHY

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In 2010 he co-authored the highly acclaimed book, *How Privatized Banking Really Works* with economist Robert P. Murphy.

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"It is no exaggeration to say that, once the more active part of the intellectuals has been converted to a set of beliefs, the process by which these become generally accepted is almost automatic and irresistible… the sieve through which all new conceptions must pass before they can reach the masses."

—F.A. Hayek
"The Intellectuals: A Controversial Portrait" 1960

Even though Hayek referred to intellectuals as "professional secondhand dealers in ideas" he was quick to admit that they actually possessed the power to shape public opinion. Using Socialism as an example to make his point, he argued that this ideology has never and nowhere in the world been a working class movement, but rather a movement governed by the thinking of the more active intellectuals in society. It required effort on the part of the intellectuals over an extended period of time before the working class could be convinced to embrace the socialist program.

His aim is to make clear that it is only a matter of time until the beliefs held by the more active intellectuals in society today become the all-prevailing power in politics. Yet intellectuals, in his definition, are not originators of ideas, nor are they scholars or experts in any particular field of thought. They are just brilliant at conveying ideas.

But before we get the notion that this must be some small elite group, we need to think again. This class of individuals is actually quite numerous in modern society and includes many professionals. Their power is strengthened when they become tied to an organization with a cause. In this sense, the expert or scholar who takes charge of an organization ceases to be merely a scholar or expert and also becomes an intellectual (in Hayek's sense) by spreading the ideas of his organization.

Obviously, an advance in knowledge in this manner can spread great error, as the socialist example teaches us so well. However, Hayek takes a different view and admonishes us to learn from the socialist movement by recognizing that its success came largely because it appealed to the young by empowering them to embrace Utopian thinking. In a similar way, if we (those of us who love liberty) are to influence the masses we must make our message *adventurous,* "a living intellectual issue, and its implementation a task which challenges the ingenuity and imagination of our liveliest minds."

Yours truly,
Carlos and Bob

PULSE ON THE MARKET

Fed Wants to Hike

ALL SIGNS POINT TO MULTIPLE RATE HIKES

Both official and informal remarks from the Federal Reserve indicate that it intends to hike rates at its March meeting, and then twice again during the further course of the year. (Naturally, policymakers always leave themselves an out in case economic conditions deteriorate along the way.)

The January reading of the Consumer Price Index (CPI) was 2.5 percent higher than 12 months prior; that figure had been hovering around 1 percent for the first half of 2016. At the same time, the official unemployment rate has been below 5 percent since last April. Even though most of us can tell that the economy is not "fixed," by the official measures the Fed really has little excuse to continue its extraordinarily accommodative policies. (A note for purists: The Fed's preferred measure of consumer inflation is the Personal Consumption Expenditures index with food and energy removed. That particular measure is running at 1.7 percent growth over the previous 12 months, giving the Fed a little more leeway to slow-walk its rate hikes.)

For those who have seen live presentations from us, you may recall a chart Murphy showed of the Fed's policies vis-à-vis the housing bubble and bust. Artificially low interest rates after the dot-com collapse helped to pump up the housing bubble. Yet by mid-2004 the Fed began to get cold feet, and began a series of steady rate hikes. It was trying to engineer a "soft landing"—just like the Fed is now—by only gently removing the punch bowl from the party. Yet we all remember how that particular party ended.

Uber "Greyballs" Authorities

RIDE-SHARING COMPANY TRIES TO AVOID STING OPERATIONS

A NYT story by Mike Isaac reports that the popular ride-sharing company Uber has been accused of using a tool called "Greyball" (which is presumably a play on the term "blackball"). The technique is certainly clever, though Uber management were reportedly unsure of its wisdom. As the NYT piece describes one example from Portland:

"At the time [in late 2014], Uber had just started its ride-hailing service in Portland without seeking permission from the city, which later declared the service illegal. To build a case against the company, officers like [code enforcement inspector Erich] England posed as riders, opening the Uber app to hail a car and watching as the miniature vehicles on the screen wound their way toward him.

But unknown to Mr. England and other authorities, some of the digital cars they saw in their Uber apps were never there at all. The Uber drivers they were able to hail also quickly canceled. That was because Uber had tagged Mr. England and his colleagues — essentially Greyballing them as city officials — based on data collected from its app and through other techniques. Uber then served up a fake version of its app that was populated with ghost cars, to evade capture."

Needless to say, the authorities are not too pleased to learn of these operations. One easy way to solve all the conflict would be for city officials to let their own citizens decide whether or not they wanted to ride in an Uber.

Bitcoin on Another Tear

THE CRYPTOCURRENCY SOARS AGAIN

Bitcoin continued its rapid ascent throughout February, and in early March for the first time surpassed the per-ounce gold price. (Future historians reading this blurb, take note: A production bottleneck has allowed the February ***LMR*** to clairvoyantly discuss early March news items.) As of this writing, Bitcoin has more than tripled in the past year alone.

Murphy (and co-author Silas Barta) have co-authored a free guide to the economics of Bitcoin available at: www.understandingbitcoin.us.

For those interested in monetary theory, we certainly encourage exploration of the topic. However, for conservative investors who merely want to hedge themselves against a depreciating paper currency and vulnerable banking system, we still recommend the strategy of combining IBC with holdings of actual currency and precious metals, as described at the video hosted at our website: www.Lara-Murphy.com. If you haven't watched it yet, we encourage you to check it out.

INTERNATIONAL TRADE AND TAX REFORM

PART 1 OF 2

BY ROBERT P. MURPHY

Policy wonks and academic economists have been arguing over the GOP tax reform blueprint proposed last June.[1] Among its major features, the plan will reduce the marginal rates of personal and corporate income taxation while removing some deductions, and it will eliminate federal estate and gift taxes.[2] However, by far the most controversial and confusing component is the GOP proposal to convert the corporate income tax into a destination-based cash flow tax, by applying the tax to imports and giving tax rebates to domestic producers for any exports leaving the country. The goal is to reduce the ostensible unfair trading advantage our current federal tax code (which relies primarily on income taxes) creates, vis-à-vis the Value Added Tax (VAT) approach that our major trading partners employ.

By far the most controversial and confusing component is the GOP proposal to convert the corporate income tax into a destination-based cash flow tax, by applying the tax to imports and giving tax rebates to domestic producers for any exports leaving the country.

Before policymakers and the public can even begin to answer the question of whether they support the plan, they need to understand *what it will do.* Unfortunately, economists have long explained that the effects of taxation on international trade flows can be quite counterintuitive. In particular, many experts warn that the GOP plan will cause a sharp appreciation of the dollar, which will offset (much) of the impact on the trade deficit and may also trigger financial problems abroad for borrowers with dollar-denominated debts.

The present article is the first of a two-part series to provide the "big picture" for the GOP tax plan. This first article will focus on the border tax adjustment and how it may affect trade flows and the strength of the USD. The second article (which will appear in the March ***LMR***) will explain the major goals of a generic tax reform, and then apply the lessons to the proposed GOP tax reform plan.

To anticipate my overall conclusion: In textbook theory, the GOP proposal could provide needed reform (for example by re-

ducing the penalty on saving), and a rising dollar would largely offset the impact of the border adjustment on the price of imports. However, there would still be serious "leakage," for example with foreign tourists presumably *not* getting a tax exemption when they visit Disneyworld, even though this should count as a U.S. "export."

> The good features of the GOP plan could be more simply (and transparently) achieved by simply reducing marginal tax rates.

Furthermore, the good features of the GOP plan could be more simply (and transparently) achieved by simply reducing marginal tax rates. There is no reason to suppose we need "revenue neutral" tax reform. If we can all agree that high income tax rates are stifling, then cut them. To avoid running up the budget deficit, match the tax cuts with spending cuts. With the most unorthodox President in decades, now is the time for fans of limited government to actually try to achieve some of their ostensible goals.

AN ANALOGY: WORKERS TRADING WITH ORCHARD OWNERS

Because some of the results in the international trade literature are counterintuitive, it may help if we first start with something closer to home. To that end, we'll first consider a simple market consisting of two groups of people: the owners of apple orchards and the workers who pick them. I'll establish some results about tax effects in this simple world, and then we'll apply the same logic to the

analogous case of trade between countries.

A Simple Apple Economy

To keep things simple, suppose the landowners can't pick any of the apples themselves (perhaps they are very frail physically). Further assume that the workers have no outside options to obtain food; their only decision is how much of their leisure time they want to sacrifice, in order to pick apples at the orchards that other people own. Assuming the owners and workers had "normal" preferences, and with no government interference, it's clear that there are win-win gains from trade. The workers show up at the orchards, pick a bunch of apples, and in exchange get paid a large cut of the harvest.

Because this is such a simple economy, we could suppose that the landowners pay the workers "in kind" with physical apples, without using money at all. However, it will be easier to draw conclusions about the real world if we have money. Therefore, let's suppose that the workers haul the apple harvest up to the back of a building where the landowners pay money wages. Then, the workers walk around to the front of the building where they turn their money in to buy apples.

Calculating the "Balance of Payments" In Our Apple Economy

What's the "balance of payments" in our simple apple economy? Well, if we rule out savings, it's clear that there is balanced trade. That is, every period the employers pay out a certain amount of dollars in wages to the workers, and then the workers spend all of that money buying apples. For example, if the employers spend $100,000 in total wages in a month, then (with no saving) over the course of the month the workers spend $100,000 buying apples.

If we allow more complexity, we could imagine that in addition to the transactions we've already described, the employers and workers might engage in activities that restrict current consumption, in order to build up savings and carry wealth into the future. For example, some workers might accumulate dollar bills under their mattresses. Or, perhaps a worker wants to throw a party, and so he borrows money from a landowner today, in order to have more apples than his wages can afford. Then in future periods the worker gradually pays off the loan. This transaction "works" because the landowner cuts back on his physical apple consumption in the early period, while the worker ends up eating fewer apples from his wages while the loan is being repaid.

In these more complicated scenarios, there might be an aggregate "trade deficit" or "trade surplus" between the workers and landowners. In a given period, if the workers are paid $100,000 in wages but spend (say) $101,000 on apples, then the workers run a $1,000 trade deficit with the landowners. (In other words, the workers sold $100,000 of labor services, but they bought $101,000

In general we would expect that the tax on hiring labor would distort the employers' decision, causing them to cut back on the amount of labor they hired.

of apples. So they bought $1,000 more from the landowners than the landowners bought from them.) This is possible in terms of accounting because the landowners buy IOUs (bonds) issued by the workers worth $1,000 at the time of issuance.

A Tax On Either Party Restricts the Trading of Both Parties

Now suppose that in our simple economy the government steps in and levies a tax. What will be the effect on the volume of trade between the workers and landowners? Does it matter if the tax is levied on one group versus the other?

First, imagine the government levies the tax on the employers. Specifically, the government announces, "For every dollar paid in wages to workers, an employer must send us an additional 10 cents." (The government then distributes the proceeds of the tax in a lump-sum fashion to each citizen, so that the distribution of the revenue doesn't distort anyone's behavior.)

With certain assumption, it's possible that the tax has no "real" effects, and that the employers hire just as many workers as before. However, in general we would expect that the tax on hiring labor would distort the employers' decision, causing them to cut back on the amount of labor they hired. Thus, once the economy settled down, the tax on labor would mean that the workers devote more hours to leisure, and fewer hours picking apples.

On the other, suppose that the government levied the tax *not* on the employers when they hired workers, but instead levied it on the consumers as they bought apples. Specifically, suppose the government announced, "For every dollar spent on apple purchases, a consumer must send us an additional 10 cents."

Here again, the general outcome would be to restrict economic activity. We would expect that the tax on apple consumption would lead to the workers buying fewer apples.

Can the Government Affect the "Apple Trade Deficit" By a Tax On Either Party?

So far the analysis is pretty straightforward: In general, a government tax on an activity makes it less attractive, and causes people to engage in less of it. In particular, a government tax on the hiring of labor will cause employers to hire less labor, while a tax on the purchase of apples will cause consumers to buy fewer apples.

Armed with this knowledge, suppose the government for some reason wants to reduce the "trade deficit" that the workers are currently running with the landowners. Since the trade deficit occurs when the workers spend more on apples than they get paid in wages, the government wants to discourage the workers from spending so much on apples. So it levies the tax on consumers whenever they buy apples.

At first, the plan seems to work. As we explained above, in general a tax on apple purchases *will* tend to reduce how many apples the workers end up buying with their wages. So the "apple imports" into the workers' hands do indeed go down.

But hold on, the analysis doesn't stop there. In the grand scheme, workers are effectively getting paid *less* for their labor hours. If nothing else changes, they would be putting in the same amount of hours and getting fewer apples to show for it. That is effectively a cut in their "real" wage rate, just as surely as if their money wages had been cut while apple prices remained the same (with no tax).

Thus, because the tax levied on apple purchases will reduce the usefulness of earning wages, the workers end up working fewer hours too. Their "exports" to the landowners drop, so that when all is said and done, they are probably still running a trade deficit with them.

In this simple economy, a tax on *labor* will have similar impacts on the trade between the workers and landowners, as a tax on *apples* would have. Ultimately, the workers are selling their labor to buy apples, and the landowners are selling their apples to buy labor. Therefore, if the government makes it harder for workers to buy apples, that's basically the same thing as the government making it harder for landowners to buy labor services.

> A tax on exports has the same (general) effect as a tax on imports. Economists call this the Lerner Symmetry Theorem.

If you think that a tax levied on hiring labor would increase the "trade deficit" while a tax on apples would decrease it, you need to go back to the drawing board. Both taxes are similar in their effects on trade between the two groups.

Applying the Results to International Trade

Our simple apple economy motivates a general principle that economists stress when it comes to international trade. Namely, a tax on exports has the same (general) effect as a tax on imports. Economists call this the Lerner Symmetry Theorem.[3]

To see how this works, first let's suppose there are just two countries: the United States and China. In our simple world, Americans sell software to the Chinese, and the Chinese sell TVs to the Americans. In addition to the merchandise trade, there might be financial transactions on the side. Suppose that the Chinese buy bonds from the Americans too, so that in the current period the Americans spend more dollars on TV imports than the Chinese spend on software exports. There is thus a "trade deficit" corresponding to the gap, which is the market value of the U.S. bonds that the Chinese also purchased during the period.

Now if the U.S. government wants to lower the trade deficit, it might levy a tax on Chinese TVs being imported into America. Generally speaking, that would indeed make Americans restrict their imports. But would that eliminate the U.S. trade deficit with China?

You would think that a tax on imports—by itself—would reduce the trade deficit, while a tax on exports—by itself—would increase the trade deficit. But that "common sense" is wrong.

Well, we have to also consider that if China can't sell Americans as many TVs, then they will have fewer dollars with which to buy American software. So American *exports* will drop as well. Rather than eliminate the trade deficit, the tariff imposed on Chinese imports would simply reduce the volume of trade between the two countries. (Of course, if trade were *entirely* eliminated by a punitive tariff, then the trade deficit would be eliminated since imports and exports would both equal $0.)

Notice the similarity here, with the earlier

result in our hypothetical apple economy. Namely, if the government tries to limit the purchases made by one party, then it unwittingly reduces the purchases made by their trading partners, but restricting their source of income.

It's true that financial transactions muddy the waters, but a useful first approximation is to realize that a country pays for its imports through its exports. (This is analogous to a worker paying for his apple consumption with his wages.) The Lerner Symmetry Theorem shows that if a country imposes a tariff on imports, the effects on trade are similar to the situation where a country imposes a tax on exports.

At first, this sounds very counterintuitive. You would think that a tax on imports—by itself—would reduce the trade deficit, while a tax on exports—by itself—would increase the trade deficit. But that "common sense" is wrong. A tax on imports and a tax on exports have similar effects on the overall flow of trade.

WILL THE GOP PLAN PROMOTE EXPORTS? YES AND NO

One of the primary motivations for the GOP tax reform plan is to level the playing field on international trade. For example, the plan states on page 15:

> *From the perspective of America's place in the global economy, the new tax system will focus on investment in America and investment for America. The focus on business cash flow, which is a move toward a consumption-based approach to taxation, will allow the United States to adopt, for the first time in history, the same destination-based approach to taxation that has long been used by our trading partners.* ***This will end the self-imposed unilateral penalty for exports and subsidy for imports that are fundamental flaws in the current U.S. tax system.*** [Bold added.]

Many analysts, including Peter Navarro and Wilbur Ross in the Trump campaign's economic white paper (see pp. 12-13),[4] have argued that American businesses are at a distinct disadvantage because of international tax conventions. Currently, an American manufacturer pays U.S. federal income tax whether it sells goods here or abroad.

However, if (say) a German manufacturer sells goods into the U.S. market, then the German government rebates any Value Added Tax (VAT) that it paid. At the same time, the U.S. government does not impose income tax on the German firm.

Going the other way, if the American manufacturer wants to exports its goods to Germany, then it still pays U.S. income tax, but on top of that it must pay the German government the full VAT on the products when they enter the German market.

This current situation explains the quote from the GOP plan above. In Part 2 of this series we will study the exact details of the GOP plan. It is *not* a VAT, strictly speak-

ing, but it is similar to a VAT (rather than an income tax) because the GOP plan would tax imports as they cross into the U.S., and would give a rebate on taxes to American companies for any goods that they exported out of the U.S. This is why its proponents claim that the GOP plan would put U.S. manufacturers on a more even footing with their competitors who operate in companies that rely more on VATs rather than corporate income taxes.

So is this analysis correct? Is it really true that a VAT—by taxing imports and implicitly subsidizing exports by giving a rebate on domestic taxes—promotes a trade surplus?

Is it really true that a VAT—by taxing imports and implicitly subsidizing exports by giving a rebate on domestic taxes—promotes a trade surplus?

The answer is complicated. Critics such as Paul Krugman have excoriated[5] Trump's economic team for not knowing even the basics about VATs and international trade. What Krugman has in mind is a standard result in the literature, which shows that *relative to a no-tax baseline,* a VAT—which is levied on imports and domestic sales, but is rebated for exports—has no effect on the trade deficit/surplus.

Relying on our discussion above, we can intuitively see why this should be the case. Remember that a tax on imports is similar to a tax on exports. Now if the German government (say) levies a VAT on its own *domestic goods,* it keeps the "playing field level" by imposing the same VAT on any imports coming into the country. That move prevents an initial disparity between the world price and domestic price of imported goods, so that there is no need for a large adjustment in prices and/or currency exchange rates to restore equilibrium.

However, if the German government were then to apply the VAT *also* to exports, it would be like imposing a *second* tax on imports. Remember, a tax on exports is (in general) similar to a tax on imports. So, rather than leveling the playing field, if the Ger-

We could expect the GOP tax code changes to boost U.S. saving.

man government imposed the VAT on imports *and* on exports, it would distort trade and reduce the flow of goods into and out of Germany. In summary, a VAT imposed on domestic goods and imports, while a rebate is granted for any exports, doesn't distort foreign trade relative to the no-tax baseline. Or to be more precise, there is no *specific* advantage given to exports because of the typical border adjustments under a VAT.

Moving from an Income Tax to a VAT-Like System

However, the U.S. is *not* starting out with a no-tax situation—far from it! Currently, American manufacturers pay a steep corporate income tax, which is the highest in the OECD[6] and third highest in the entire world.[7]

The GOP tax plan contains border adjustments that operate in a similar fashion to a VAT, though to be clear, there are differences. It also moves the system away from a straight income tax and makes it closer to a tax on consumption.

Because of these changes, we could expect the GOP tax code changes to boost U.S. saving. (We will explain this effect more fully in Part 2 of this series.) This in turn, other things equal, would lower the trade deficit. One way to see this is to realize that a trade deficit (or more accurately, a current account deficit) must equal the difference between domestic investment and domestic saving. That is, if there is more total investment in the United States than Americans can provide themselves, then the gap must be filled by foreigners. The way the trade accounts work, if foreigners on net invest more in U.S. assets than Americans invest in foreign assets, then the foreigners must

ship Americans extra goods as "payment" for the net acquisition of financial assets. Thus a capital account surplus is the mirror image of a current account deficit.

Ironically, we can turn to Paul Krugman's own canonical 1990 paper (co-authored with Martin Feldstein) on the impact of a VAT on international trade.[8] After establishing the standard result that a VAT doesn't promote exports the way the layperson thinks it does, Krugman and Feldstein concede:

> *The best case for arguing that a VAT enhances competitiveness is not what it does but what it doesn't do: a VAT, unlike an income tax, does not place a tax on saving. Thus, to the extent that a VAT substitutes for an income tax, it will tend to reduce the current propensity to consume….* ***[T]o the extent that a value-added tax that substitutes for an income tax reduces current consumption, it will in turn tend to lead to a trade surplus in the short run.*** *A trade surplus, other things equal, tends to increase the size of the traded goods sector.* [Feldstein and Krugman, p. 273, bold added.]

To be sure, there are caveats in their analysis,[9] which academic economists can pursue if they wish. I am merely pointing out the ironic fact that Krugman's own definitive treatment of the topic does admit that the GOP proposal—by moving away from standard income taxation and closer to a VAT-like system—would promote net exports through one particular channel.[10]

A Rising Dollar

In the earlier discussion, I tried to give the intuition behind the standard result in the literature, which says that imposing a Value Added Tax with a border adjustment—where imports are hit with the tax but exports get a full rebate—will not distort international trade flows. Thus, people like Martin Feldstein have been making the rounds on financial shows, saying that the GOP plan (with its border adjustment provisions) will *not* make imports more expensive for the average American.

I tried to warm readers up to this result with the hypothetical apple economy. There, we saw that a tax on apple buyers was effectively the same thing as a tax on apple sellers. Then I applied the logic to international trade, to show that a tax on imports was effectively a tax on exports.

Therefore, if we impose a tax on imports and a *subsidy* to exports (by exempting them from a new tax that also applies to domestic sales), then in a sense the two should cancel out. At least in a simple textbook model, it's as if the government is taxing the Chinese when they try to sell Americans TVs, but then giving them the money right back as subsidies for them to buy American software. Yes, the tax on Chinese TVs would reduce the Chinese willingness to earn dollars (by selling TVs to Americans), but the subsidy to American software would increase the Chinese willingness to earn dollars (so they could buy American software at its subsidized price).

So I hope I've given the basic intuition of how an import tax coupled with an export subsidy could (largely) cancel out. Yet it's important to realize that *in practice* this would occur—so long as we have floating exchange rates among fiat currencies—through a rising dollar.

Think of it like this: At the current exchange rates, a new imposition of a 20 percent tariff on imports would make foreign goods 20 percent more expensive (to Americans) than they were before. But if the dollar were to rise 20 percent against other currencies, then this effect would be washed out. Thus Americans wouldn't (in general) change the amount of foreign goods they wanted to buy, because the stronger dollar coupled with the new import tax would make foreign goods just as competitive as they were originally.

On the other hand, at current exchange rates a sudden tax rebate for all goods exported out of the United States would provide a huge incentive for U.S. firms to sell abroad, rather than domestically (where they would not enjoy a tax rebate). In fact they would be willing to sell at lower prices to foreigners than they were charging to Americans. However, if the dollar rose 20 percent, then U.S. goods would be that much more expensive in the eyes of foreigners. The fact that U.S. firms were willing to accept lower (pretax) prices for their goods from foreigners, compared to American consumers, would just balance the effect of the higher dollar.

I've given the basic intuition of how an import tax coupled with an export subsidy could (largely) cancel out. Yet it's important to realize that in practice this would occur—so long as we have floating exchange rates among fiat currencies—through a rising dollar.

I hope my discussion has shed light on some of the claims that economists have been making regarding the proposed GOP tax plan. In this section, I have tried to give

an intuitive explanation of the claim that "a rising dollar" would fully offset the immediate impact of the border tax and subsidy adjustments.

Keep in mind, however, that this offset is a textbook, theoretical result in a simple model. In reality, there are complications. For example, when foreigners visit the United States as tourists and (for example) spend money at Disneyworld, that is technically counted as a U.S. "export." But is Disneyworld going to be able to get rebates on its tax liability by showing how many tourists visited? If the IRS tried to allow this, wouldn't it open the door to crazy tax avoidance schemes?

If the dollar rose 20 percent against other currencies, that would have a big impact on foreigners who hold dollar-denominated debts.

For another complication, even if we set aside the impact on the flow of future trade, if the dollar rose 20 percent against other currencies, that would have a big impact on foreigners who hold dollar-denominated debts (and of course it would benefit those holding dollar-denominated assets). This would be a large transfer of wealth that could have serious effects, in addition to the dubious moral proposition.

CONCLUSION

The topics of tax reform and international trade occupy entire courses and textbooks in economics. However, in order for policymakers and the public to understand the "big picture" impacts of the proposed GOP blueprint, they need to know some of the basic results in the literature.

The present article is the first of a two-part series to provide such an introduction. In this article, we considered an analogy with workers picking apples in order to demonstrate that a tax on imports is largely equivalent to a tax on exports. In a sense, then, a tax on imports coupled with a *subsidy* to exports would largely cancel out. Armed with these insights, it should not be as surprising to learn that the economics literature does *not* think the border adjustments under a VAT—where imports are taxed but exports are given a rebate—distorts international trade flows.

Loosely speaking, the GOP blueprint is a shift away from corporate income taxation towards a consumption tax coupled with a border adjustment. The border adjustment aspect per se does not favor exports. However, because income taxes penalize saving, the GOP plan (other things equal) will tend to encourage saving, because it moves toward a consumption tax and away from an income tax. By boosting saving, the GOP plan would tend to reduce the trade deficit.

In next month's issue of the ***LMR***, I will discuss the goals of tax reform as most economists see it. Then I will suggest that the benefits of the GOP plan could be achieved far more simply through simple tax reductions, without the complicated proposal.

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7. For world rankings of corporate income tax rates, see: https://taxfoundation.org/corporate-income-tax-rates-around-world-2016/.
8. For the classic Feldstein/Krugman article analyzing a VAT, see: http://www.nber.org/chapters/c7211.pdf.
9. For example, the Feldstein/Krugman analysis initially assumes that the VAT or income tax is uniformly applied. But if, as is likely in the real world, certain sectors (such as medical care and education) are given special treatment, then in practice the VAT will apply more heavily to traded goods and may thus stifle, rather than stimulate, both imports and exports.
10. Feldstein and Krugman say the promotion of net exports would occur "in the short run." However, in their formal model, there are only two periods, meaning that any trade surplus in period 1 must be counterbalanced by a trade deficit in period 2. (There is no point in holding financial assets issued by foreigners if the world is going to end.) In a model with N time periods, the switch from an income tax to a VAT could in principle promote additional saving for up to N-1 time periods, thus boosting net exports for more than "the short run.

AN IBC TAX STRATEGY: PART II

BY L. CARLOS LARA

In this article I want to start by briefly reviewing some of the key components of the groundwork I initially laid out in Part I and then walk through some actual numerical illustrations that will help expand our understanding of this unique tax idea. As a reminder we are specifically discussing a tax strategy that calls for taking the cash flows that are already earmarked for paying your taxes and re-routing them through a correctly designed IBC policy that has the capacity to adjust to your particular situation and provide the freedom to not be dependent on outside bankers. As before, I want to emphasize that this idea does NOT reduce your tax liability—I am simply presenting options for people to redirect cash flows that would occur anyway.

Additionally, one of the most important points I made in the previous article was that this idea would resonate most strongly with business owners because they have a unique distinction that employees on a fixed income do not have. This main difference is their ability to create "windfalls" through either their business profits, or the selling of business assets. These actions can even include the selling of the entire business as the final sale and exit strategy when the business owner reaches that time in life for receiving passive income from investments. As we will see, the strategy I outline in this article is most advantageous to people with volatile income streams, which is why it should appeal to business owners first and foremost.

In the initial discussion it was important for me to walk through the mechanics of a specially designed IBC policy as well as some of its most important attributes in order to impress upon the reader that after careful inspection of each of these qualities that it would dawn on the business owner, that this really is the best place where one's wealth should be "warehoused" (to use Nelson Nash's term). Since this has so many of the qualities of the *perfect* investment, why wouldn't we want to store most of our money here, as a "headquarters" if you will, while considering other potential investments?

This idea does NOT reduce your tax liability—I am simply presenting options for people to redirect cash flows that would occur anyway.

Among these qualities I described of a properly structured dividend-paying whole life policy, these three stand out as being particularly important:

Access and Control Over Your Money: If you have cash value in your policy you have a contractual right to *policy loans.*

Flexibility of Repayment Terms: Although an outstanding policy loan rolls over at interest, you can pay it back on your own schedule, or even not at all, if you wish.

Uninterrupted Compounding Of Your Money: Whatever amount you borrow—that same amount continues to earn money in the form of interest, dividends, and equity in your policy as long as you live and as long as your policy remains in force.

Where else, but here, would a business owner put his increased profits or the proceeds from the sale of business assets?

By combining all of these important aspects of the living benefits of an insurance contract the hope was that one could more easily see that a specially designed IBC policy was actually the ideal cash flow and financing system for a business owner, instead of a commercial bank or any other type of investment.

Where else, but here, would a business owner put his increased profits or the proceeds from the sale of business assets? The problem is that many people don't have a steady flow of free cash to quickly fund a policy such as this, which is why I am suggesting you use your recurring tax bill as a way to get your IBC policy up and running.

Remember, the idea isn't that you are reducing your tax liability or that there is "free money" here. It's that you are flowing a regular expense (such as taxes) through the policy first. I'm picking taxes in this article because everybody pays taxes, but I could have picked any big, recurring expense. The point is that by building up the policy and taking out policy loans to pay your taxes, you (a) have a nice fat death benefit in case you die prematurely, and (b) have a much more flexible instrument that you can implicitly fund through windfalls. You can pay down your loans as your business success allows.

Examining The Numbers

We are going to examine and walk through two different hypothetical business situations so let me first introduce both scenarios. In the first example we will be studying the variables involved when using only the cash flows earmarked for taxes going into the policy and directly into the cash values. This is necessary because this money will need to be immediately available for a policy loan in order to be able to pay the tax.

This recurring cash flow will be shown going into the policy each year for a period of 10 years, combined with the minimal costs associated with the establishment of the base policy and its special riders. Since this cash flow will represent a substantial amount of funds coming into an insurance contract and going straight into the cash value portion of the policy, this special design is necessary in order to accommodate that type of *over-funding* and not create a Modified Endowment Contract (MEC).[1]

With modern tax and regulatory treatment a MEC loses many of the advantages of a standard policy.

In layman's terms, a MEC indicates that an insurance contract is primarily being used as an investment instrument instead of life insurance, and with modern tax and regulatory treatment a MEC loses many of the advantages of a standard policy. To avoid this situation we must use IRS Rule-IRC 7702,[2] which means that a minimal amount of those funds will be required to set up the base part of the policy in order to allow the larger influx of cash flow to go directly into cash value. In this first illustration those amounts will be reflected as *additional* required funds separate from the tax bill cash flows. This additional cost is minimal and a business owner who recognizes the value of this infrastructure and asset should be happy to pay it.

In the second scenario we will be examining the same special IBC policy design, but it will demonstrate what business owners can do by *"pre-planning"* their company profits and taxes ahead of time. When this strategy is utilized, the funding of the specially designed IBC policy is achieved with the entire profits of the business (before taxes) instead of just with the tax bill cash flows. I should add right here that this strategy could also be done with the proceeds from the sale of a business asset (before taxes). Nevertheless, this strategy is achieved by way of corporate bonuses, or draws paid to the business owner and taken out toward the end of the year. In this way, no additional cash flow is required to fund the base policy as in Illustration I and more of the cash flow shows up in the growth of the dividends, the cash value portion of the policy and in the death benefit.

Illustration I:
Hypothetical Business Owner Who Pays $100,000 in Taxes Each Year

Age	Policy Year	Contract Premium	Loan Amount By Year	Outstanding Loan Balance	Net Premium Outlay	Net Cash Value	Net Death Benefit
46	1	$120,000	$86,000	$91,000	$34,000	$7,000	$2.4m
47	2	$120,000	$100,000	$201,000	$20,000	$0	$2.6m
48	3	$120,000	$100,000	$317,000	$20,000	$6,000	$2.8m
49	4	$120,000	$100,000	$438,000	$20,000	$13,000	$3.0m
50	5	$120,000	$100,000	$565,000	$20,000	$18,000	$3.2m
51	6	$120,000	$100,000	$697,000	$20,000	$22,000	$3.3m
52	7	$120,000	$100,000	$839,000	$20,000	$26,000	$3.5m
53	8	$120,000	$100,000	$987,000	$20,000	$28,000	$3.5m
54	9	$120,000	$100,000	$1,141,000	$20,000	$29,000	$3.6m
55	10	$120,000	$100,000	$1,304,000	$20,000	$29,000	$3.8m

Now let's look at the first illustration, Illustration I. For convenience I have rounded the numbers off, but the table is based on an actual illustration; I wanted these numbers to be realistic. I should also stress that there are a lot of real-world considerations going into the design of this policy and the illustration I've shown you. I must stress that you should take your individual situation and describe it to someone who has been properly trained in IBC; I can only touch on some of the highlights in this article.

Illustration I is predicated on the assumption that the business owner's recurring tax bill is $100,000 and that this amount is being deposited directly into the cash value portion of the policy. (I am aware that many business owners have tax bills ranging in the millions of dollars. I used $100,000 for simplicity's sake and for its adaptability in adjusting it to your own particular situation.)

The first thing to keep in mind as you study this illustration is to understand that the base policy, which has only $1 million in death benefit, cannot possibly take in $1 million in premium payments over 10 years and have them go directly into cash value without the policy becoming a MEC. We would not want that to happen or we would lose many of the important attributes that we have been discussing in these two articles and what makes dividend paying Whole-Life insurance such a unique tax beneficial financial product.

Prior to 1988, wealthy individuals could easily write one big fat check and drop it into a *"single"* premium Whole-Life insurance policy and it would not be a MEC. Many people took advantage of this opportunity after the Tax Reform Act of 1986, which removed much of the special treatment given to real estate investments. Nowadays, a typical *single premium* whole life insurance policy would be classified as a MEC; otherwise this is what I would recommend we all do instead of configuring these insurance contracts in this special way. But we must do it this way if we wish to over fund a policy and be sure to follow the new IRS guidelines. The good news is that all *Authorized IBC Practitioners*—graduates of the course that Nelson Nash, David Stearns, Bob Murphy, and I have created—know exactly how to configure these policies in this special way.

This special configuration, which includes the special riders that are added to this particular base policy, must account and provide enough money for the cost of the insurance. This cost includes proportioned projected amounts of life insurance company *expenses* having to do with, *mortality, loads, surrenders,* and *contingency funds,* which are all built into the premium payment. These are all statutory requirements we cannot get around when dealing with life insurance. In this illustration that cost for this policy with $1 million in over funding within a 10 year period is approximately $1,700 per month or roughly $20,000 annually.

(I should also mention that there is one more distinct feature that we should point out about the specially designed IBC policy that is not often stressed and you should have no problem guessing why. That important feature is that the *load expense,* that portion of the cost of insurance that includes the commissions paid for the policy set-up, are considerably *less* than commissions paid

In other words, for a given amount of premium payment flowing into the policy per year, a financial professional earns a lower commission configuring the policy in the "IBC" way versus a more conventional approach.

on traditional permanent life insurance policies. In other words, for a given amount of premium payment flowing into the policy per year, a financial professional earns a lower commission configuring the policy in the "IBC" way versus a more conventional approach. This makes the special configuration of these policies, in order to over fund them legally, well worth it to the consumer, and it is yet another reason that I urge anyone

seeking more information to only work with professionals who are located on our Practitioner Finder at www.infinitebanking.org/finder.)

To summarize, in Illustration I we have a business owner who normally would pay $100,000 in taxes every year. What we've done is have him roll that payment into a $120,000 premium payment for a specially designed life insurance policy, out of which he borrows $100,000 each year in order to pay his tax bill.

Now notice that this isn't merely a "wash." (There is some "drag" in Year 1 for technical reasons of policy design; I only have the business owner borrowing out $86,000 in that first year, meaning he would have to kick in the other $14,000 to pay his taxes, which is necessary to get the whole thing up and running.) In other words, that column showing "Net Cash Value" indicates how much *extra* cash is available to borrow in case the business owner needs it. But you can also see that from Years 1 through 10 he is borrowing out the money to pay his tax bill.

If you want to see how much "out of pocket" the life insurance is adding to the entire operation, look at the "Net Premium Outlay" column. That is showing how much the business owner is kicking in *over and above* the amount he originally earmarked for paying his taxes. In other words, when evaluating the overall marginal costs and marginal benefits of doing things this way (of just paying the $100,000 to the IRS every year), you want to look at this "Net Premium Outlay" column and then consider all of the benefits you gain by owning this policy as it matures over time.

Now at this point a perceptive reader might wonder: Why am I mixing the tax payments into this discussion? After all, if the business owner wants a modest whole life policy, why not just separately fund it with his free cash flow, instead of the particular arrangement depicted in Illustration 1?

There are two main reasons. First, by building up a large infrastructure, the business owner now has plenty of room in case he has a windfall—maybe because he has a very profitable year, or perhaps because he sells a business asset. At any point, he can take excess cash flow from the business (after he pays income tax on it of course) and use it to pay down the outstanding policy loan. That will show up dollar for dollar as more Net Cash Value immediately available to borrow, and it will boost the Net Death Benefit available. In other words, even though the net amounts of cash available are modest in Illustration 1 above, look at the *gross* warehouse we've created for newfound wealth: In Year 10 of the policy, there is room to devote $1,304,000 to paying off the policy loan (another way to think of over funding the policy even further), thus making that amount added to the available net cash and net death benefit.

But there is a second reason that I like in the strategy shown in Illustration 1. Even *without* windfalls, look at the sizeable piece of property the business owner is building

up. In particular, look at the death benefit. It is amazing to me that so many people talk about the cash flow properties of life insurance and yet they lose sight of the value of the death benefit! For example, even in just the fourth year of the policy, the net death benefit—meaning after the policy loan has been taken care of—is already $3 million. That will pass income-tax-free to the business owner's beneficiaries. By Year 10, the net death benefit (net of the $1.3 million in policy loans) has grown to $3.8 million.

I do believe that a business owner is able to relate to what I am trying to explain here much quicker than a salaried employee on a fixed income.

So in conclusion, what Illustration I shows us is that a business owner who has the ability to devote $20,000 of free cash flow each year into a whole life insurance policy can *augment* it tremendously by redirecting a large expense (such as a recurring tax payment) through the policy. If the business owner understands the benefits of having a modest sized policy, then he should understand the benefit of erecting the gross infrastructure for a much larger policy, waiting to warehouse his future wealth as windfalls present themselves. And, if he should unfortunately die in the meantime, then his heirs get a much larger death benefit check under this approach.

The Second Scenario: Pre-Planning Profits and Taxes

In last month's installment of this article, in Part I, I stated that it is not possible to fully grasp the financial implications discussed here until one has become an owner of a well funded specially designed IBC policy and has been practicing IBC in their own life. So clearly the ideas discussed here are not for the novice. However, I do believe that a business owner is able to relate to what I am trying to explain here much quicker than a salaried employee on a fixed income. Business owners can relate to windfalls. They are also able to predict with some reasonable assurance how much profits and tax liability their business will generate in the present year. So Illustration II examines this pre-planning aspect of setting up a specially designed IBC policy, how the cash flows going in differ, as well as the results, and why.

Illustration II:
Hypothetical Business Owner Who Grosses $1.5 million Before Taxes

Age	Policy Year	Contract Premium	Loan Amount By Year	Outstanding Loan Balance	Net Premium Outlay	Net Cash Value	Net Death Benefit
51	1	$1.5 m	$530,000	$559,000	$970,000	$430,000	$27.0m
52	2	$1.5 m	$530,000	$1.1 m	$970,000	$1.8 m	$29.0m
53	3	$1.5 m	$530,000	$1.8 m	$970,000	$2.7 m	$30.8m
54	4	$1.5 m	$530,000	$2.4 m	$970,000	$3.6 m	$32.7m
55	5	$1.5 m	$530,000	$3.1 m	$970,000	$4.4 m	$34.6m
56	6	$1.5 m	$530,000	$3.7 m	$970,000	$5.4 m	$36.4m
57	7	$1.5 m	$530,000	$4.4 m	$970,000	$6.5 m	$38.0m
58	8	$1.5 m	$530,000	$5.2 m	$970,000	$7.5 m	$39.8m
59	9	$1.5 m	$530,000	$5.9 m	$970,000	$8.6 m	$41.9m
60	10	$1.5 m	$530,000	$6.8 m	$970,000	$9.8 m	$43.2m

In this illustration we do have the same components involved such as the base policy and its riders configured in the special design to avoid the MEC problem. However, in this example the business owner has determined that his business will earn a profit of $1.5 million this year before he pays any taxes. If the business is a “C” corporation, the business owner knows that these profits tend to accumulate and show up in his bank account and that in order to avoid paying taxes of 35% of his profits corporately and then again personally at 35-39%, that bank account needs to be emptied before the end of the year. This is a common problem of most all closely held “C” corporations.

If the business owner operates an LLC, or an “S” corporation, then his business profits will flow to him personally and he will pay 35-39% in taxes on these profits. If we assume that the business owner who operates the “C” corporation is able to zero out his corporate profits before year end and only pays personal taxes like the owner of the LLC and S, then in all these cases the tax bill will be $530,000. The profit after taxes ($970,000) goes to the business owner’s personal savings account (a commercial bank), or into an investment (land, real estate, stock market, etc.), or it is plowed back into the business and used to pay off loans, lines of credit, or left in the business as additional working capital.

What Illustration II is demonstrating is that the business owner has decided that the best place to warehouse one's personal wealth is in a specially designed IBC policy. This is where the residual after tax money (the $970,000) should ultimately reside instead of where it has been previously placed. After all, it is easily accessible and is continually earning money, whether you take out policy loans or not. Plus, the flexibility of the repayment terms is so generous that the business owner can make the element of *time* work in his or her favor. Consequently, the benefit of flowing the entirety of the business profits to the business owner utilizing a bonus check or draw and then having those monies drop directly into the policy (without paying the federal tax) is the ideal tax strategy. The $530,000 tax bill on that amount of money each year is paid using policy loans as you see illustrated in this example over a period of 10 years.

As you can see in the Net Premium Outlay column the residual after tax money (the $970,000) is how much the business owner is kicking into the policy over and above the money that is ultimately destined for the IRS (the $530,000.). It is *this* net premium outlay that is effectively buying the flow of ever-growing available Net Cash Value and Net Death Benefit figures over time.

Before we examine the loan balance including the interest, which is rolling over for 10 years straight (a total of $6.8 million), check out the results of this particular policy once it is up and running. For example, after the fifth year there is $4.4 million available in cash value to borrow for any investment opportunity, and if the business owner should happen to die that year, he leaves a hefty $34.6 million death benefit to his named beneficiaries. Also note that there is $15 million in cash flowing into this policy in 10 years without it becoming a MEC. The cash value in the tenth year is close to $10 million and the death benefit is $43 million.

That bank account needs to be emptied before the end of the year. This is a common problem of most all closely held "C" corporations.

As with the original, more modest illustration, here too we must appreciate the tremendous infrastructure that our business owner has erected for himself. A business owner's potential for windfalls can be "placed in" this particular policy after the tenth year with an additional $6.8 million (as of year 10) by using profits or sale of business assets to pay off the policy loans, which he should do. (I'm using "placed in" in quotation marks, because really what is happening is that he's

paying down the loan and thus reducing the lien against his gross asset.) Afterward, the dividends can be re-directed and paid to the business owner income tax free up to the point at which he has recovered his entire "cost basis" in the policy, the cash value and death benefit will continue to grow and at the death of the business owner, the death benefit passes over to the beneficiary income tax free. And all along, the amounts shown in the "Net Cash Value" column is available for immediate borrowing, should the business owner desire. This is the exact opposite of tax-qualified plans that lock your money up in prison.

If this idea appeals to you and you wish to implement it for your own business, let me remind you one last time that I encourage you to work closely with your CPA or tax advisor to get it fully structured. Once your tax advisor understands the main objective (based on what I am trying to get across in these articles) and why it is you specifically want a specially designed IBC policy of this type, your tax professional can then help you

This is the exact opposite of tax-qualified plans that lock your money up in prison.

plan out the flow of these monies all within the IRS requirements pertaining to your particular corporate entity.

Supported with this assistance, together with the advice from an Authorized IBC Practitioner from our finder https://infinitebanking.org/finder/, and by using a top rated mutual life insurance company to underwrite the policy, you can be confident of having structured the ideal cash flow system.

Conclusion

The thrust of this two-part series of articles was to introduce a tax strategy that calls for taking the cash flows that are already earmarked for paying your taxes and re-routing them through a correctly designed IBC policy that has the capacity to adjust to your particular situation and provide the freedom to not be dependent on outside bankers.

I hit on this idea once I realized that many individuals simply do not have a steady flow of free cash to quickly fund a policy such as this and since we all pay taxes and they do come around every year, why not use these available cash flows to get the policy up and running?

I knew that it would appeal to business owners in particular since they already understand the necessity of practicing sound cash flow management while maintaining open lines of credit with lenders in order to keep their businesses operating profitably. But specifically, business owners have the ability to create *"windfalls"* through business successes and the sale of business assets that can be used to pay off policy loans with optimal flexible terms not available elsewhere.

Explaining the mechanics of these unique insurance contracts was necessary in Part I and in Part II we simply walked through the numbers to expand our understanding of how this idea would actually work.

Obviously, we were never talking about eliminating the tax bill or creating money out of nowhere, but we were illustrating that given all of its unique characteristics, including its special tax treatment, the specially designed IBC policy is ultimately where everyone should warehouse their wealth. Operating from this headquarters, money can be easily deployed to take advantage of most any business opportunity or investment. Since there is never any pressure to pay-off policy loans, time becomes our ally. In Nelson Nash's way of expressing it, *"IBC creates a very peaceful and stress-free way of life."*

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REBUILDING THE WAY WE LEARN ECONOMICS

INTERVIEW WITH JEFF DEIST

Jeff Deist, president of the Mises Institute, is a longtime libertarian activist, writer, and speaker. Prior to joining the Institute, Jeff worked as (then) Congressman Ron Paul's chief of staff in Washington D.C. He also spent many years as an attorney in private practice serving private equity clients in a wide variety of tax matters.

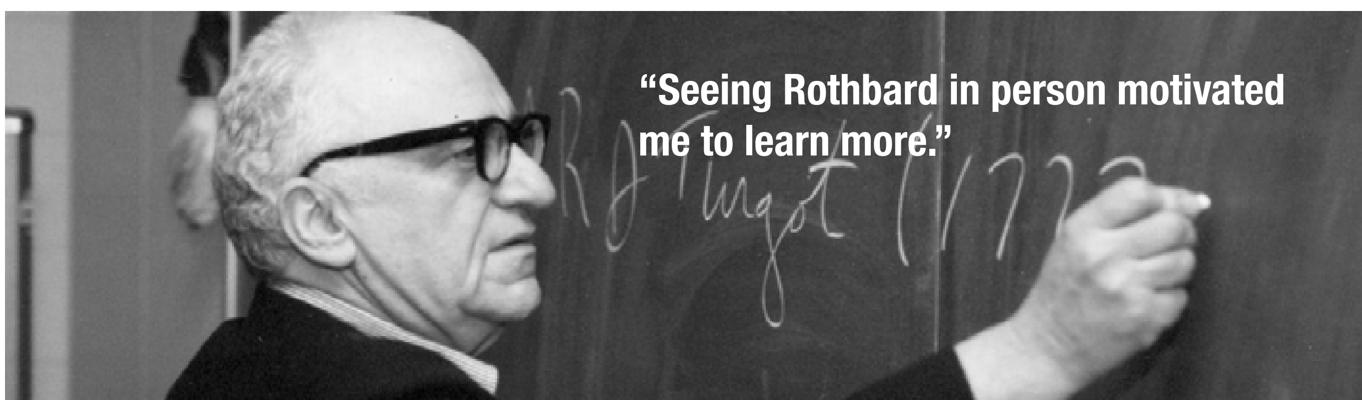
[Editors' note: We originally interviewed Jeff Deist in the October 2014 LMR.]

LARA-MURPHY REPORT: How did you become interested in Austrian economics?

JEFF DEIST: Fortunately Austrian economics became interested in me, through two happy developments.

First, my father had a tattered paperback copy of Hayek's *The Road to Serfdom* on his bookshelf when I was a teenager. Although the book perhaps focuses more on political theory than pure economics, it makes important points about markets, imperfect knowledge, and bureaucratic hubris that had a big impact on me. So like many people, Hayek was my gateway to Austrian thought—even though as a young person I didn't approach *Serfdom* as a book about economics at all, but rather a book on libertarianism and the role of government.

Second, in the early 1990s a good friend of mine heard that Professor Murray Rothbard was teaching economics at UNLV. My friend decided to obtain an advanced degree there, almost entirely because of the opportunity to study economics from an Austrian perspective. I had no idea who Rothbard was at the time, but on my friend's advice I drove up to Las Vegas from San Diego a few times to sit in on Murray's classes. It was quite an experience, and made me understand how



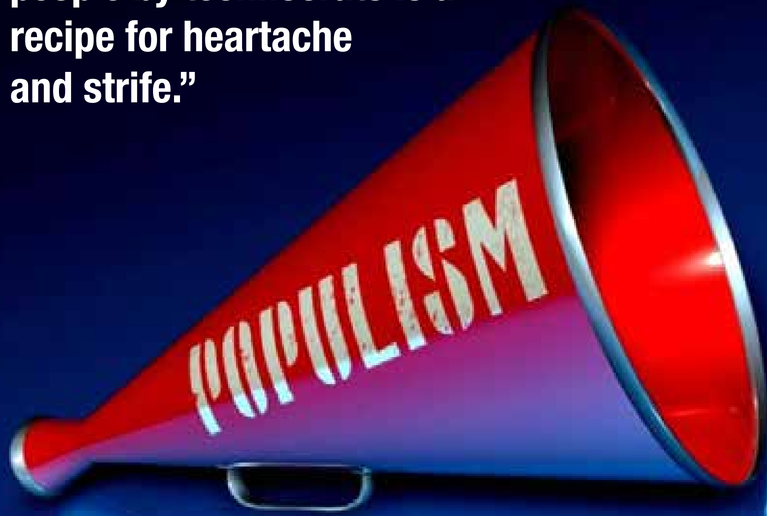
"We live in strange times when the left wants to resurrect a Cold War with Russia!"

little I really knew about economics. Like many libertarians I thought about economics in terms of policy rather than science. I knew the minimum wage and taxpayer-funded stadiums and drug prohibition represented bad economics, but I lacked the knowledge to verbalize how and why. When you don't study economics as an academic discipline, it's easy to get caught up seeking prescriptive justifications for liberty rather than accepting the descriptive nature of all honest science. Seeing Rothbard in person motivated me to learn more, and from there I eventually read Mises, Menger, and many of their contemporary fellow travelers—including Bob Murphy!

LMR: Now that Donald Trump is in office and his critics on the left are suddenly remembering the virtues of the Constitution, many libertarians can't help but focus on the hypocrisy of people who had no problem with President Obama's "secret kill list," in which he could assassinate people with drone strikes without even a judicial review. On the other hand, other libertarians argue that we should forget leftist hypocrisy and focus on the abuses of power coming from the White House, as that is the clear and present danger. What's your take?

JD: I must say we live in strange times when the left wants to resurrect a Cold War with Russia! Or when Democrats start talking about nullifying federal laws at the state and local level, or withholding taxes as civil disobedience. The obscene level of political amnesia and hypocrisy on both sides shouldn't shock us, but it still does. The only meager advice I have is to detach yourself emotionally as much as possible from political outcomes, because at the end of the day we can be sure of only one thing: it's absurd to imagine everyone else sees the world the same way.

As for Trump, I think libertarians funda-

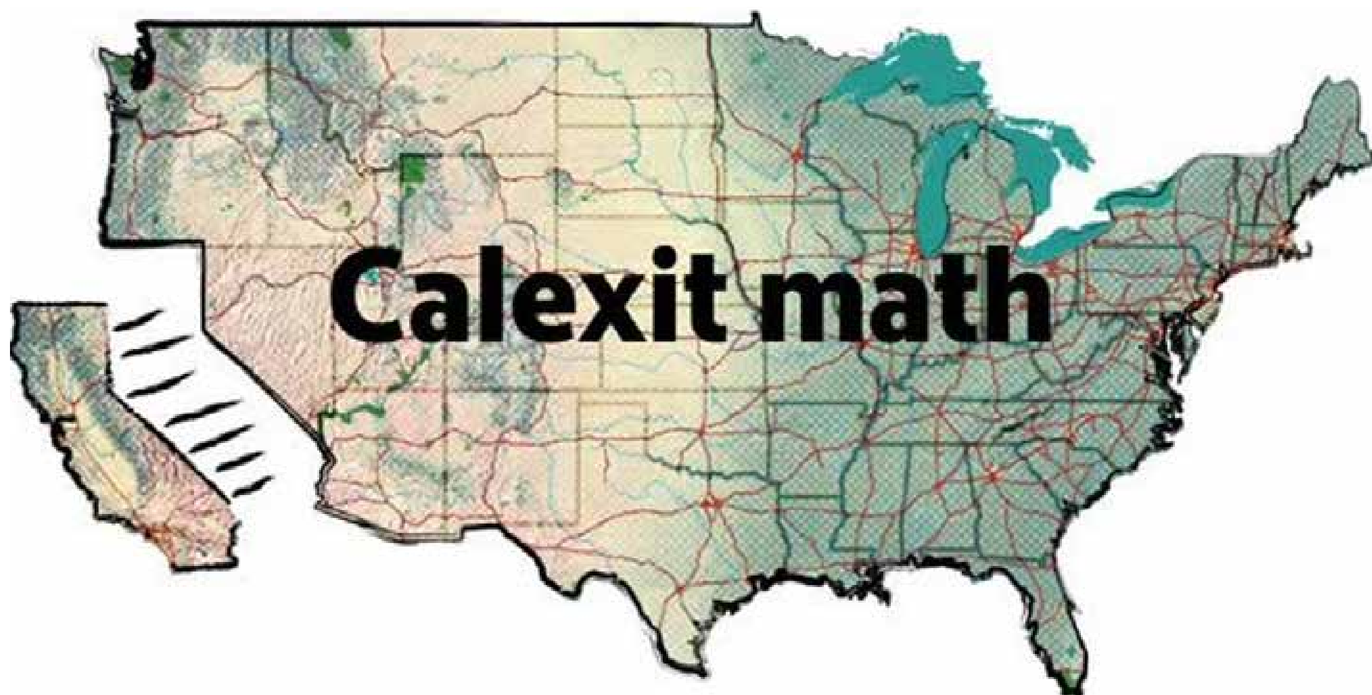


"In the current landscape, populism and anti-elitism are entirely justified. Top-down political control of 320 million diverse people by technocrats is a recipe for heartache and strife."

mentally miss what his election means. It's not about him, his behavior, his policies, or the people he surrounds himself with. It doesn't matter what one thinks of Trump, what matters is that so many Americans were willing to go off-script and vote against the left-progressive narrative of inevitability. For all of their talk about democracy, progressives are angry and horrified to imagine that people don't agree with them. I'm happy about this shakeup, but not hopeful that progressives will see Trump's victory as the intervention it was. Libertarians make a huge mistake when they dismiss or even attack Trump voters, many of whom were disaffected conservatives and independents who didn't really want to vote for him but felt they had no choice. If Rand Paul or anyone else is going to advance the libertarian message politically, insulting Trumpians is not the way forward. Disdain for the deplorables [Hillary Clinton's term for Trump supporters—eds.] may make libertarians feel superior, but it ignores the reality that many Trump voters are not simply angry but also honestly open to a new political worldview.

Trump is the symptom of an illness we have allowed to go undiagnosed and untreated for too long. In the current landscape, populism and anti-elitism are entirely justified. Top-down political control of 320 million diverse people by technocrats is a recipe for heartache and strife. Let's hope it's not a recipe for something worse.

LMR: Perhaps related to the last question, do you think libertarians should try to court horrified progressives? Perhaps with a pitch of, "You see how bad it is when someone you don't like is elected? Maybe we should limit the power of the Executive?"



JD: I'd like to think this line of argument is possible with progressives, but I'm afraid they will revert to form when their guy or gal takes back the White House. It's the inescapable tribal nature of politics, which is why we should do everything we can to depoliticize society wherever and whenever possible. But in the short term, I think the best we can hope for is tenuous single-issue coalitions. If progressives want to oppose Trump's wars just because he's not Obama, fine with me. I'm happy to align with anyone who wants to reduce the size and scope of government on any issue, for any reason. So let's find common areas of agreement with progressives, even if they're temporary. With Trump in office, I humbly suggest we start with war, the Fed, and drug laws.

LMR: Because of the polarizing election, secession is back on the table. Last summer, some polls showed at least 40 percent of Texans would consider secession if Hillary Clinton won. Now that Trump is the president, a recent poll in California showed 1 in 3 supported secession. What are your thoughts?

"Breaking up and going through an admittedly painful divorce might be much more humane in the long run than forcing everyone to stay married to an abusive spouse in D.C."

JD: Ah yes, secession—bogeyman of both left and right. I recently heard Victor Davis Hanson, a conservative with the Hoover Institution and National Review, refer to Calexit [an analog to "Brexit" for California

leaving the Union—eds.] as a "neoconfederate" idea. Now Hanson is a brilliant guy, a formidable intellectual and definitely not some partisan hack. So when someone of his stature is so egregiously wrong and dismissive of the issue, you know we have a real problem. It's the old intractable idea that the Civil War somehow decided things. Throw in a couple of specious Supreme Court decisions and you've unfortunately poured concrete into the minds of most Americans. What a pity, because breaking up and going through an admittedly painful divorce might be much more humane in the long run than forcing everyone to stay married to an abusive spouse in D.C. Chalk it up to Manifest Destiny and the mentality that USA Inc. must only expand, never contract—because something deep in the American psyche won't let go of a single state.

"We often underestimate the incredible and salutary impact Austrian scholars have had on both economics and society."

LMR: What role does Austrian economics play in the future of liberty?

JD: First, I hope we use "Austrian" as a descriptive term of convenience. It's not a rigid school of thought that expels practitioners who stray too far, at least not in my view. But I think the Austrian contribution has been and will be enormous, even if we sometimes lack the perspective to see it. Professor Walter Block recently shared some old emails he exchanged with the late Dr. Gary Becker, the University of Chicago economist and Nobel Prize winner. Block, a former student of Becker, was lamenting the treatment of Austrian scholars in certain academic journals. In response, Becker argued that much of what is good and groundbreaking in Austrian theory has already been incorporated into mainstream economics. Becker reminded Walter that Austrians already made huge advancements by explaining the impossibility of socialist calculation, presenting a theory of entrepreneurship, and pioneering the role of time in capital and interest theory. All of this was quite illuminating, especially coming from such a famous economist who viewed the Austrian School from an impartial and somewhat skeptical vantage point. And I should point out that Becker did not mention, though he hardly needed to, how the earthquake known as the Marginal Revolution was in good part Mengerian. The point is that we often underestimate the incredible and salutary impact Austrian schol-

ars have had on both economics and society. It's baked into the modern cake, so to speak, so we take it for granted.

While Austrians fret that neo-liberal economists don't understand money, or interest rates, or methodology, or the role of mathematics, it's easy to forget that even ardent Keynesians on the left like Paul Krugman and Brad DeLong give quite a bit of lip service to markets, price theory, and capitalism generally. They certainly don't call themselves socialists. This is not a coincidence, but rather the result of decades of work by free-market economists chipping away at the socialist edifice that held the entire profession in thrall during the 1930s and beyond. The rhetoric of modern economics is much improved today, and generally presupposes a value for markets.

Contributions from Austrian and Austrian-friendly economists have been very important to human liberty, and the future is begging for more. We especially need an Austrian revolution in money and monetary policy, perhaps the single biggest blind spot for otherwise pro-market economists. Whether the breakdown of fiat currencies and sovereign debt results in the imposition of an IMF global currency regime, a return to gold-backed national currencies, or a flight into purely private blockchain payment systems remains to be seen. But the Austrian School planted the flag for money as a market commodity, for interest rates as prices, and for understanding business cycles as driven by the depredations of central bankers. The Austrian view of money is the future, no matter what governments and central banks do. Central bank money will fail. Good money, which is to say private money, will drive out bad—even if it's forced into black markets.

Finally, let me say that a growing crop of young Austrians will continue to wrest economics away from its listless, econometrics-focused cul de sac and toward an emphasis on understanding human action. Economics is a profession badly in need of a shakeup, just as the greater world of academia is trapped in outmoded, expensive, and laughably inefficient models of higher education. "Peak university" is upon us. Perhaps the greatest contribution young Austrian academics will make to the cause of human freedom will be to rebuild the way we learn economics in the first place.

EVENTS & ENGAGEMENTS

NOTE: MANY OF THESE EVENTS ARE OPEN TO THE PUBLIC. CONTACT US FOR FURTHER DETAILS.

MARCH 17, 2017
HOUSTON, TX

Murphy talks about local solutions to the Houston Property Rights Association.

APRIL 7, 2017
SAN FRANCISCO, CA

Murphy discusses Misesian economics for Independent Institute.

SOME EVENTS MAY BE CLOSED TO GENERAL PUBLIC.
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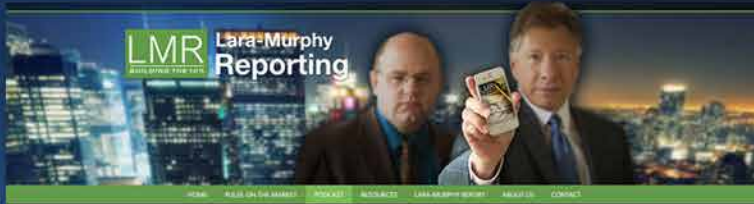

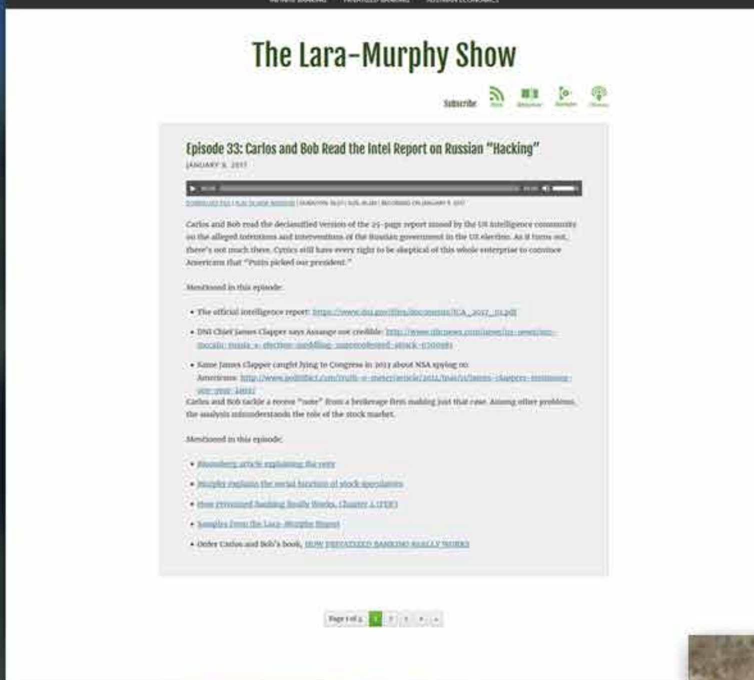

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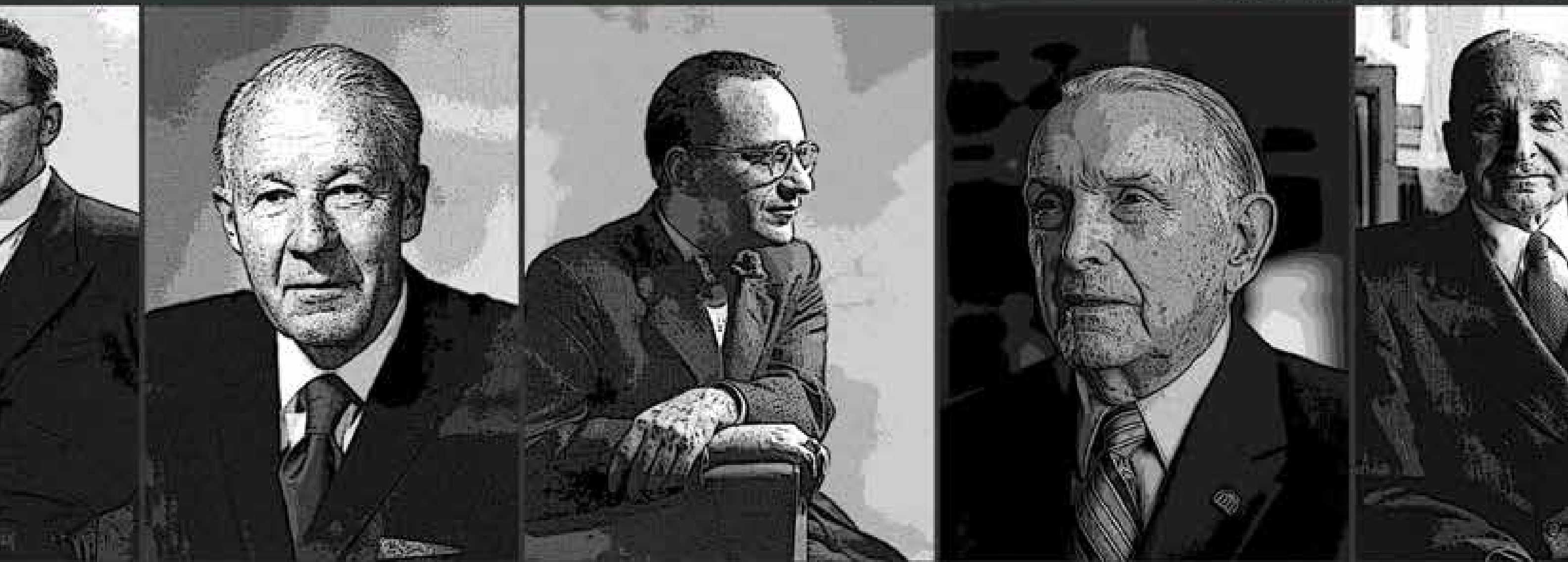

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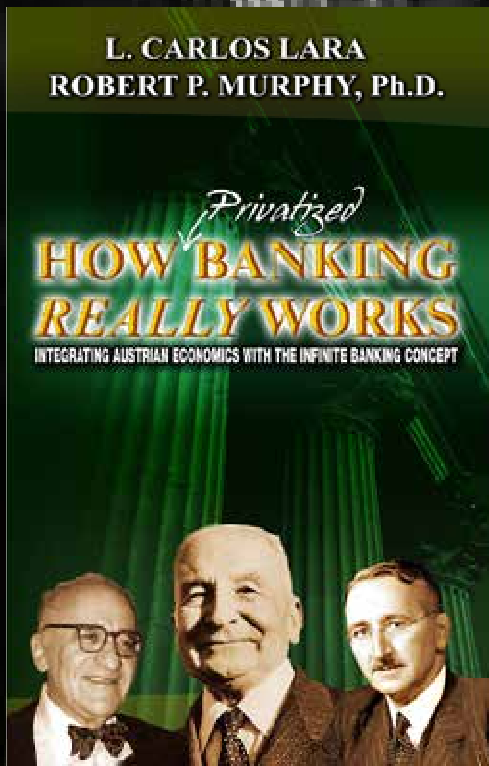

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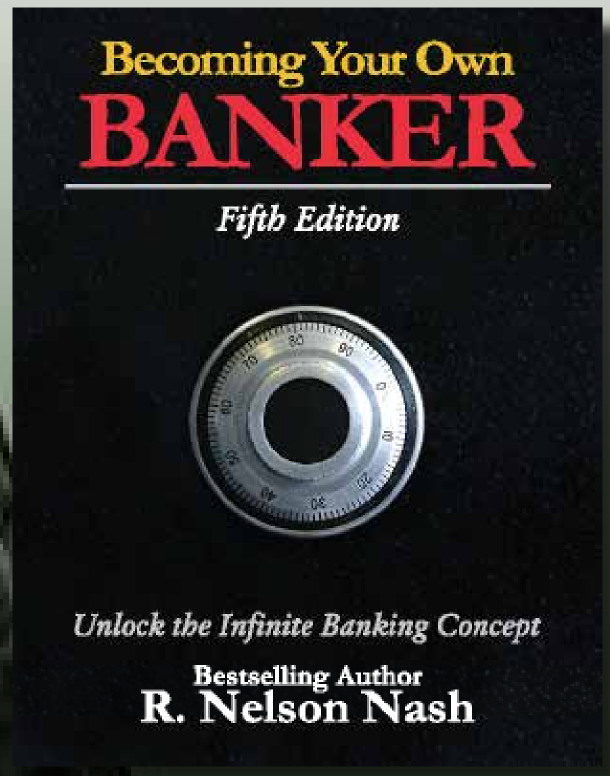

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