NORTHSTAR
FINANCIAL PLANNERS INC.

JULY 2018

FINANCIAL PLANNING NOTES

CLIENT NEWSLETTER

"The key to making money in stocks is not to get scared out of them."

—Peter Lynch

IN THIS ISSUE:

STRESS TESTING YOUR INSURANCE

Let's talk about insurance. If you made it past that first sentence without nodding off, that's a great start! For wealthy Americans, the Tax Cuts and Jobs Act can have significant implications on their insurance needs.

For years, the estate tax "exemption" has been around $5.5 million, meaning if your estate is worth less than that (not including assets passed to a surviving spouse), there will be no estate tax on the assets you leave to your beneficiaries. With the new tax law, the exemption doubles, to about $11.2 million. Note those limits are per taxpayer, so for spouses, the exemption limit is effectively doubled.

How many taxpayers are above the exemption limit? Not many. According to the US Congress Joint Committee on Taxation, only 2 out of 1,000 estates were subject to the estate tax before the law. It's highly likely with the new law that number is now below 1 in 1,000.

But for people with assets between $5 million and $11 million, the law is big news. Many people with estates that size carry life insurance policies with the intent that the proceeds from those policies will pay any estate tax due upon their passing. With the new higher limits, that insurance may no longer be needed. If you've built up a high cash balance in a permanent insurance policy, you could be looking at a double windfall – you no longer need to pay premiums for the policy and the cash balance is now available for other purposes.

Even if your estate is likely to exceed the new higher limit, the effective tax rate on your estate may now be much less than before the law went into effect. Here's an illustration:

George was single, had a total taxable estate valued at $15 million and died in 2017. Less the $5.5 million exemption, taxes were owed on $9.5 million, at a rate of 40%, or a total tax bill of about **$3.8 million**.

Sally had exactly the same amount of assets, but held on until 2018. When she died, only $3.8 million of her estate was subject to the tax, which comes to about **$1.5 million** in taxes.

Under the new tax law, an estate that would have paid about 25% in estate taxes would now pay about 10%. And even better, if you were planning to use life insurance to pay the tax bill, you'd need $2.3 million less in coverage.

If you have a permanent insurance policy, this would be a great opportunity to "stress test" your coverage, to determine if you have the right amount or if you need it at all.

To help our clients in making that determination, we'd do the following:

Assess the Policy

When life insurance is sold, the policy holder is given estimates of what the cash value and death benefit will be over time. Those estimates may or may not come to fruition. Some policies overperform and some underperform. If it has overperformed, you may have built up all the cash value you need, or more, and if it's underperformed, you may not have enough coverage.

Sitting with the client, we would contact the insurance company and ask for an "inforce illustration," which is basically an update of those original estimates of cash value and death benefit. This will help us determine how the policy is performing and if the coverage is adequate.

Optimize Premium Payments

The most common and easy-to-understand way to pay premiums is just to write out a check each month, quarter or year, or have the premium amount automatically withdrawn from a bank account. You know, like you pay all your other bills.

But life insurance is unique in that there are other ways to pay the premium, particularly after you've built up a large cash balance. For example, you could tap that cash balance to pay the premium. That would lower the cash value of the policy, but if you have more cash value than you need, it might make more sense to stop paying the premiums out of pocket. We can analyze the alternatives to come up with the best solution.

Optimize the Policy

The bottom line is figuring out whether you have the right coverage. Do we keep the policy as it is, get rid of it, or restructure it?

Keeping the policy in place may be the best option if coverage is still required for the original purpose and the coverage amount is still the correct amount (or close enough). You might also decide, even if you don't need the coverage for the estate tax, to consider the benefit amount to be an extra tax-free inheritance for your children or other beneficiaries, so you'd decide to keep it in place.

If you decide the coverage is not needed for the original purpose or for any other, you can go ahead and sell or cash out the policy. Keep in mind there will be taxes owed on gains, which is the amount you receive in excess of the premiums you've paid.

A third option is to create a new (or restructured) policy that better suits your needs. You could reduce the amount of death benefit if you need less, and create a "paid up" policy so that you never have to make another premium payment. We could also inquire about using some or all of that cash value to add on a product like a long-term care benefit. There are many options to tap the cash value without triggering a "taxable event," which is to say you wouldn't owe any taxes on the use of that money.

Regardless of giant revisions to the U.S. tax code, it is a good idea to revisit your insurance every few years to make sure you have the proper coverage in place. If you haven't had an insurance "stress test" in a while, or have family members you think would benefit from one, give your financial professional a call.

—Steve

Sources: *Ten Facts You Should Know About The Federal Estate Tax* by Chye-Ching Huang and Chloe Cho, Center on Budget and Policy Priorities, October 30, 2017

Too Much Of A Good Thing? What To Do If You're Overinsured by Russ Alan Prince and John J. Bowen, June, 2018

STRESS TESTING YOUR FINANCIAL PLAN

Ultra-high net worth families regularly stress test their plans to help ensure those plans are both state-of-the-art as well as in line with their needs and wants. Here's why you should join them in that effort – even if you're not nearly as wealthy.

Asking "What If?"

Stress testing financial plans can be a very smart way to help assure that the plan will deliver as promised. Financial plans that might look great on paper often prove to be much less impactful once they are implemented. It is not uncommon for there to be unintended consequences that can even derail one's agenda.

At heart, stress testing is when you ask, "What if …?" about a variety of areas of a financial plan you have or are considering. When it comes to estate planning, for instance, a wealthy individual might ask questions like:

- What will actually happen to my assets when I pass on?
- How will my family be affected, precisely?
- Who will be tracking the hard assets such as artwork and jewelry to make sure they go to the designated heirs – as opposed to vanishing?
- Who is going to make sure my estate plan is being executed as it's supposed to be?

To be effective and informative, stress testing should be done in a systematic manner. While there are some variations, the basic process starts by determining your goals. Your goals, any problems to be addressed and opportunities to benefit should be the driving forces behind the financial and legal solutions you employ.

Once you clearly understand your goals, you can evaluate the specific existing or proposed financial services or products. There are numerous ways to dissect and critically assess financial services and products:

Work the assumptions. A plethora of assumptions underlie all services and products. In stress testing, these assumptions are modified to determine how the solutions will work when a given scenario changes.

Evaluate alignment with goals and objectives. A solution might prove to work extremely well, but still not achieve the desired results. It's essential to help ensure that the services and products will accomplish your goals.

Calculate cost structure. The intent here is to identify the best and most cost-effective solution possible. When calculating cost structures, all the expenses should be specified – including long-term results.

Based on the stress test's evaluation of the existing or proposed solutions, you might consider alternative products or services. It may be very useful to do side-by-side comparisons between the solutions being considered or currently used and such alternatives, asking questions like:

- How do the assumptions compare?
- How do the alternative rate when it comes to potentially achieving my goals?
- Which solutions are more cost-effective?

The end result of the process: recommendations. Based on those recommendations, there are different courses of action to consider taking:

1. **Stay the course.** If the stress testing found the solutions being used or proposed to be on target and of high quality, the recommended action is to stay the course.
2. **Choose different solutions.** If the stress testing finds what may be described as a system failure – the financial products being used are not going to achieve the desired results and might even blow up, for instance – the right move is to take a different course of action.
3. **Choose a different professional.** If the solutions are appropriate but the professionals involved are really not up to the task of implementing them (or they charge too much money), it will usually make sense to switch to someone in whom you have a higher degree of confidence.
4. **Modify the approach with the original professional.** If the solutions can be made more powerful with only slight modifications, the best route is often to stick with the original professionals and have them make the minor changes needed.
5. **Continue stress testing**. There are occasions when the individual or family chooses a professional to conduct a stress test and that professional is not up to the task. This comes out often clearly in the process or results of the stress testing. The only viable course of action is to select a different professional to conduct the stress testing.

Although stress tests are commonly used among the ultra-wealthy, they should be a part of most people's due diligence process when vetting financial plans, financial products and financial services. Frequently, stress tests uncover flaws in financial plans as well as better ways to achieve desired outcomes. For those reasons, stress tests will likely benefit a great number of people – especially business owners and their families, who generally have so much of their future financial security riding on one asset: their business.

Certainly there is a cost to stress testing, asset protection and income tax plans. That cost will depend greatly on the complexity of the testing involved and your situation. However, a stress test fee can be a whole lot cheaper than the costs – financially but also emotionally and psychologically – of a plan or solution that is fundamentally flawed or in conflict with your goals.

—Allen

TRANSITIONS

We are sad to announce that advisor Mia Kitner, who has been with us for more than four years, has left the firm. She and her family are moving on to bigger and higher things in Denver, Colorado.

We wish Mia, Jason, Sophia and the entire Kitner family the very best in the Mile-High City.

And on the heels of Mia's departure, we welcome Richard Lottier to the Northstar Family. Richard joined us as Client Service Specialist in May, 2018 and is currently working toward one day becoming an Investment Advisor Representative. Richard is driven by his desire to help others succeed. He graduated Cum Laude from Florida Gulf Coast University with a Major in Sociology and a minor in Interdisciplinary Studies. He is a native Floridian, living in

WHO WE ARE

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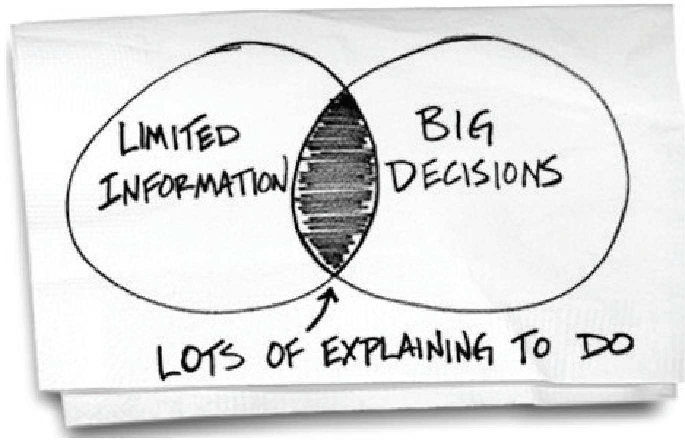
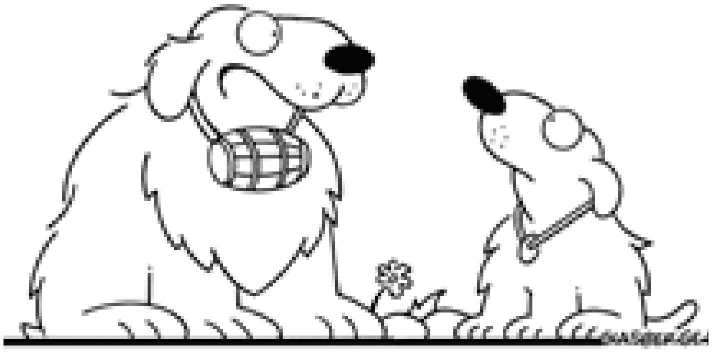
South Florida his entire life. He has worked in the Customer Service Industry for over 10 years in a variety of different fields.

Richard enjoys lifting weights and all things sports. He has participated in team sports since the age of 4 and has learned a lot about teamwork and respect along the way. He has been a loyal Miami Hurricanes fanatic since the time he could walk. He also enjoys spending time with family and friends when he is not playing video games.

FROM CARL RICHARDS' NAPKIN BLOG



FINAL THOUGHT



"I once rescued a man who was buried under an avalanche of debt!"