McCarthy Asset Management, Inc.
Personalized Wealth Management

November 2017 Monthly Commentary

Dec. 1, 2017

Inside this issue:

Stock Market & Portfolio Performance

November 2017: U.S. stocks posted solid gains for the month, while international stocks were up more modestly and bonds fell slightly.

	Nov 2017	YTD 2017	Description:
Without Dividends:			
S&P 500	2.8%	18.3%	500 Largest Public U.S. Companies
Russell 2000	2.7%	13.8%	2000 of the smallest U.S. stocks
MSCI EAFE	1.0%	20.0%	international stock index
U.S. Aggr Bond	-0.1%	3.1%	index of U.S. bonds
With Dividends, after all fees:			
MAM portfolios	2.6%	14.8%	non-very conservative MAM portfolios
MAM Conserv	1.2%	8.2%	portfolios with 50%+ bond allocation

The returns showed above are unaudited. Past performance is not indicative of future results. Returns for McCarthy Asset Management Portfolios ("MAM Portfolios") are net of management fees and transaction costs, and reflect the reinvestment of dividends. Results represent a composite of clients using a similar investment strategy, individual results will vary.

Returns for the indices are provided solely as a general indication of current market conditions. MAM Portfolios are not invested in a style substantially similar to any index. Indices do not reflect the deduction of management fees or transaction costs or the reinvestment of dividends. Performance for the indices would be lower if these costs were reflected.

Advisor Team

McCarthy Asset Management, Inc.

Three Lagoon Drive Suite # 155
Redwood Shores, CA 94065
USA

STEVE McCARTHY
CPA, CFP®,
Owner and Principal
650 610-9540 x 303
steve@mamportfolios.com

LAUREE MURPHY, CFP®, EA
Financial Planner
Tax Specialist
650 610-9540 x 304
lauree@mamportfolios.com

ANTHONY BERTOLACCI , EA
Director of Compliance
Tax Accountant
650 610-9540 x 302
anthony@mamportfolios.com

MARILYN BLANCARTE, PACE
Executive Assistant
650 610-9540 x 305
marilyn@mamportfolios.com

Possible Significant Tax Law Changes

On November 16, 2017, the House of Representatives approved its sweeping tax reform package—the Tax Cuts and Jobs Act (HR 1). The Senate is now in the process of preparing its own tax reform package which, if passed, would then need to be reconciled with the House bill before a final bill can be sent to the White House for signature. As such, it may be the latter part of December or even January before we know for sure which details survived and which are modified.

Even though the effective date of any tax changes won't be until 2018 or later, year-end planning for 2017 takes on added significance given the potential major changes of these tax bills. Both the House GOP bill and Senate GOP plan would impact virtually every individual and business on a level not seen in over 30 years. As with most tax bills, however, there will be "winners" and "losers." Both versions call for lowering the individual and corporate tax rates, repealing countless tax credits and deductions, eliminating the alternative minimum tax (AMT), and more.

Here are the more significant changes that would affect individual taxpayers (the business and corporate tax law changes are not addressed in the article).

Individual Tax Rates:

- Currently, the tax rates are 10, 15, 25, 28, 33, 35 and 39.6%, with the maximum rate reached for single filers for income above $426,700 and married filers above $480,050.
- The House version has rates of 12, 25, 35 and 39.6%, with the maximum rate for single filers for income above $500,000 and married filers above $1 million.
- The Senate version has rates of 10, 12, 22.5, 25, 32.5, 35 and 38.5%, with the maximum rate for single filers for income above $500,000 and married filers above $1 million.

Standard Deduction: Currently $13,000 ($6,500 if single) would nearly double to $24,400 for the House bill and $24,000 for the Senate bill.

Personal Exemptions: Currently $4,150, subject to a phase-out for higher income taxpayers, would be eliminated under both the House & Senate bills.

Itemized Deductions:

- State tax deduction would be eliminated under both the House & Senate bills.
- Property taxes would be capped at $10,000 under the House bill and eliminated under the Senate bill.
- Home mortgage interest: Currently, interest on debt up to $1 million can be deducted. The Senate bill would retain that, but the House bill would reduce the eligible mortgage debt to $500,000 for mortgage debt incurred after November 2, 2017. Both the House and Senate bills eliminate the deduction for interest on home equity debt.
- Medical expenses would no longer be allowed under the House bill, while the Senate bill preserves the deduction.

Possible Significant Tax Law Changes– Con't

- Miscellaneous itemized deductions, including unreimbursed employee expenses, would no longer be deductible under either tax bill.

Top Capital Gains/Qualified Dividend rate, which is currently 20% (plus a 3.8% surtax for higher income taxpayers), would not change under either the House or Senate bills.

Alternate Minimum Tax (AMT) would be repealed under both the House and Senate bills. For most taxpayers currently subject to AMT, this would not be a significant benefit as the elimination of the state tax and property tax deductions would eliminate AMT for them anyway.

Estate Tax: The exemption for estate tax would be double under both bills to $11.2 million. In addition, the House bill would eliminate estate tax beginning in 2025.

Sale of Principal Residence Exclusion:

- Under current law, up to $250,000 of gain ($500,000 if filing jointly) on the sale of a principal residence is excluded from tax. Among the requirements is that the home must be owned and used as your principal residence for two out of the last five years. This rule can be used once every two years and the exemption is available regardless of income.

- For sales after 2017, both the House and Senate bills would restrict the eligibility to homes used as your principal residence for five out of the last eight years. In addition, the House bill would phase out the excluded gain by one dollar for every dollar by which the taxpayer's modified adjusted gross income exceeds $250,000 ($500,000 for joint filers).

2017 Year-end Tax Planning for Individuals:

- Assuming you are not subject to AMT, **prepay any state income tax and property tax** due by December 31, 2017.

- **Delaying income to 2018** may or may not make sense. While the tax brackets will likely be lower if the tax bills become law, the loss of the state income tax deduction may more than offset the benefit of the lower rates.

- **Accelerate Charitable Contributions?** Under the proposed tax law changes, fewer taxpayers will continue to itemize their personal deductions. For those who will be able to itemize in 2017 but not in 2018, they should prepay charitable contributions by December 31, 2017.

- **Accelerate Medical Expenses?** The House bill repeals the deduction for medical expenses. For those that incur sufficient medical expenses to claim a deduction, it may make sense to prepay expenses by December 31, 2017.

- **Prepay Miscellaneous Itemized Deductions**, including unreimbursed business expenses, by December 31, 2017.

- If you are thinking of **selling your principal residence**, it may make sense to do so prior to December 31, 2017.

Possible Significant Tax Law Changes– Con't

- **Plug-in Cars:** Purchase your Tesla, Chevy Bolt or similar plug-in vehicle before year-end. The House bill repeals a credit of as much as $7,500.

- **Employee stock options:** Workers with Incentive Stock Options (ISOs) may benefit if they wait to exercise them until 2018. Exercising and holding ISOs can trigger alternative minimum tax, which both bills would repeal.

- **Alimony:** For payers of alimony, sign divorce or separation agreements that include alimony before the end of 2017. In the House bill, alimony ceases to be deductible by the payer for agreements signed after December 31, 2017.

Potential Implications of these Tax Law Changes:

- Real estate prices may be negatively impacted, especially for more expensive homes.

- Higher income taxpayers have a greater incentive to move to a state with low or no state income tax.

Schwab to Add "Trusted Contact Information"

In February of this year, the SEC approved FINRA's proposed amendment to the Customer Account Information rule and created the new Financial Exploitation of Specified Adults rule, both of which take effect February 5, 2018. Schwab believes these rules can help financial advisors and Schwab protect potentially vulnerable clients from financial exploitation. As a result:

- Beginning in February 2018, Schwab is adding a form to its new account applications to collect Trusted Contact information for all new clients.

- A Trusted Contact is someone who Schwab may contact about the client and the client's accounts—for example, a family member or friend. Once a client identifies a Trusted Contact, that individual's contact information will be added to all of the client's accounts.

- What powers will a Trusted Contact have? They really will have no powers over an account. They can't view or make changes to the account. In fact, they won't even know they have been designated as a Trusted Contact unless the client tells them. The purpose of the Trusted Contact is for Schwab to have someone to contact if they feel that a client is being financially abused. I imagine having a Trusted Contact named on an account could also be useful for us if we suspect there is financial abuse occurring.

- For current account holders, Schwab will be including an insert in the December account statements explaining how clients can add this information to their existing accounts via a new form. If you are interested in adding a Trusted Contact, we can fill out the form and send it to you for signature, or you will be able to do so directly via the Schwab Alliance website.

Please let Marilyn know if you would like to add a "Trusted Contact" to your account(s). She will then be able to assist you with this once it becomes operational in the New Year.

Investor Returns– Bad Timing Costs Investors

Morningstar, the investment research firm, has created a metric they call "investor returns" which shows that investors' behavior often hurts their investment performance. Since 2006, Morningstar has calculated "**investor returns**" for mutual funds and exchange-traded funds to capture **how the average investor fared in a given mutual fund over a period of time**.

A fund's published total return reflects a buy and hold strategy. This may not be relevant to some as not all investors buy and hold. Investors move their money in and out of funds as they search for the best return, causing the net assets of funds to rise and fall over time. In contrast to a fund's total return, which reflects a buy and hold approach, **investor return accounts for all cash flows into and out of the fund to measure how the average investor in that fund performed over time**. In other words, it shows how well or poorly investors traded the fund. In a classic example, a fund receives a great inflow of assets right <u>after</u> a period of good performance. Investor returns capture these flows and place more weight on the months when the fund had higher assets.

Unfortunately, the norm is for investor return to be less than total return. Morningstar's data shows investors in diversified U.S. stock funds have missed nearly 1.8% of the average fund's annualized total returns over the past decade because of bad trading. While 1.8% underperformance may not sound like much, over a long period of time, it can make a big difference.

In reality, even excellently managed funds experience periods of underperformance. This could cause some investors to sell their shares after a period of relatively poor performance. Unfortunately, these investors won't participate if the fund then has a period of outperformance. In selecting mutual funds for portfolios, we like to focus on a fund's performance through a full market cycle. For instance, a fund like AMG Yacktman has underperformed the S&P 500 the last five years. This is not surprising, though, as this fund tends to underperform during up markets. Over the last 10 and 15 years, which include full market cycles, the Fund is in the top 1% and 4%, respectively, of its peer group. Given that we are probably in the later stages of the bull market that started in 2009, I think this is a good fund to own despite its recent underperformance.

Sincerely,

Stephen P McCarthy, CPA, CFP®,

McCarthy Asset Management, Inc.

Three Lagoon Drive Suite # 155
Redwood Shores, CA 94065
USA

Phone: 650-610-9540
Fax: 610-9541
E-mail: Steve@mamportfolios.com

Our Services

McCarthy Asset Management, Inc. (MAM) is an independent, privately owned Registered Investment Advisor firm. We provide clients with the peace of mind that comes from knowing professionals are managing their financial affairs. The services we offer include:

Investment Management Services:

- **MAM creates and manages customized investment portfolios based on each client's investment objectives, timeframe and risk tolerance.**

Financial Planning Services:

- **The Net Worth Analysis (NWA) tracks the accumulation of Invested Assets for pre-retirees and the retention of Invested Assets for retirees. Updated annually.**
- **"Retirement Analysis" a comprehensive analysis of your retirement goals, which produces easy-to-read, interactive working plan, stored in the cloud. Updated as needed for life events.**
- **Social Security Planning is an analysis of the best strategy for when and how to start claiming Social Security benefits.**

Tax Services: Clients have the option of utilizing the income tax services provided through the firm Stephen P. McCarthy, CPA. These services are offered at an hourly rate and may include:

- **Tax Return Preparation**
- **Income Tax Projections**
- **Tax Minimization Ideas**
- **Tax Authority Representation**

Other Services: MAM has retained outside experts, whose services are available at no cost to our clients:

- **Long Term Care Planning– Allen Hamm of Superior LTC Planning Services, Inc.**
- **Medicare Advisory Program (MAP) - Eileen Hamm**

Reminders/Updates

1) **Property Tax payments** are due December 10, 2017.
2) **Roth IRA Conversions:** Please contact us ASAP if you would like to discuss. The deadline for 2017 conversions is December 31, 2017

.