McCarthy Asset Management, Inc.

Personalized Wealth Management

May 2020 Monthly Commentary

June 1, 2020

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Stock Market & Portfolio Performance

May 2020: U.S. and international stocks continued to recover from their sharp March sell-off. Meanwhile, bonds rose modestly for the month.

	May 2020	YTD 2020	Description:
Without Dividends:			
S&P 500	4.5%	-5.8%	500 Largest Public U.S. Companies
Russell 2000	6.3%	-16.4%	2000 of the smallest U.S. stocks
MSCI EAFE	4.1%	-15.3%	international stock index
U.S. Aggr Bond	0.5%	5.5%	index of U.S. bonds
With Dividends, after all fees:			
MAM portfolios	3.7%	-5.8%	non-very conservative MAM portfolios
MAM Conserv	3.0%	-4.6%	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.

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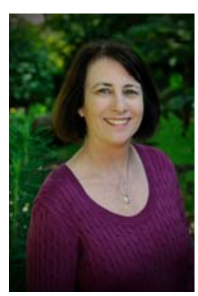

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May Market Update

The stock market continued its recovery from the dramatic losses incurred during March. For the month, the S&P 500 rose 4.5% and is now down just 5.8% for the first five months of 2020. This has happened while the unemployment rate reached its highest since the Great Depression and manufacturing has dropped the most since 2008. Furthermore, the Leading Economic Index plunged the most ever on record and corporate earnings estimates have been revised down at a record rate. Why then, has the stock market rallied in the last nine weeks? There are a few reasons:

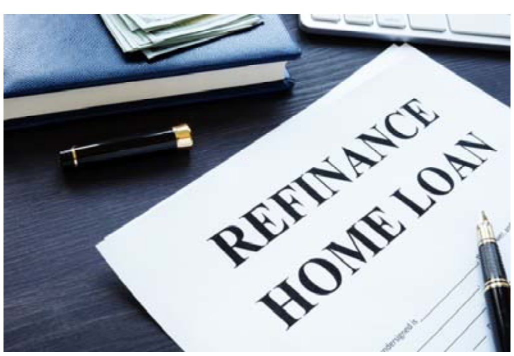
- At the March lows, stocks were pricing in the kind of economic collapse we are currently in the midst of. The subsequent rally was less about economic optimism, and more about the massive injection of liquidity from both the Federal Reserve and Congress.

- While there is no comparable history to the current crisis, historically, stocks rebound in advance of the low point in economic activity. In fact, history shows that the stock market has had some of its best performance while unemployment was peaking, and, on average, has bottomed four months before the end of a recession.

- It's also important to realize that the stock market's recent gains haven't been broad-based. Investors have piled into sectors that are generally well-insulated from coronavirus-related pressure, which have also attracted momentum-seeking investors. Many of these stocks are big name, large-cap growth stocks which have had a significant impact on the recovery in the S&P 500. In contrast, the Russell 2000 Index, which is the most widely-quoted measure of the overall performance of small cap and mid-cap stocks, is still down 16.4% for the year as of May 31st.

Our Outlook: May could mark the end of the shortest but deepest recession in a century. Growth is likely to return in the 3rd quarter as more people go back to work. However, the economic reopening could be slower and more uneven than optimists expect. A sustained economic recovery will probably not occur until we get a vaccine, or develop medical treatment that is effective against the virus. Until that happens, it is difficult to envision people traveling, a recovery in global trade, and businesses willing to invest or hire aggressively. We continue to feel that the stock market could be at risk for another short-term correction. As such, we are likely to remain somewhat cautious with portfolio positioning for the foreseeable future.

Good Time to Refinance a Mortgage



One of the economic impacts of efforts to fight COVID-19 is the Federal Reserve (the Fed) cutting short-term interest rates close to 0%. While the Fed can influence short-term rates, mortgage rates are more impacted by longer-term rates, such as that of the 10-year U.S. Treasury bond. This is because the average life of a mortgage is approximately 7 years. Fortunately for mortgage holders, the rate on the 10-year U.S. Treasury bond has fallen significantly this year. At the end of May, the rate was 0.65%, down from 1.92% at the start of 2020.

As a result, mortgage rates are once again at attractive levels. A number of years ago, I used to regularly write articles about falling mortgage rates. Back then, rates were much higher, and they were consistently falling. In those articles, I would list the rates that Fremont Bank was offering on its "no-cost" refinances. As a result, a number of clients utilized Fremont Bank, often doing multiple refinances as rates continued to decrease.

Good Time to Refinance a Mortgage– con't

Per Fremont Bank's website, as of May 29th, their "no-cost" rate on a loan up to $510,000, was 3.125% for a 15-year fixed-rate loan and 3.375% for a 30-year fixed-rate loan. The annual percentage rate (APR) quoted on these loans was the same as the stated rate, reflecting that the borrower doesn't incur costs, other than an appraisal fee, to do the refinance. Fremont Bank is only able to offer mortgages in California and Nevada. If you live in another state, I am sure there are other lenders who offer attractive mortgage rates. Furthermore, there may be lenders in California offering rates better than Fremont Bank.

I find "no-cost" refinances appealing because if rates fall just a little further, it may make sense to do another refinance. If you decide to refinance, I have a few recommendations:

- Pay off the new loan at least as quickly as your existing loan. For instance, if you are 5 years into a 30-year mortgage, pay off the new loan over no more than 25 years.
- Try to pay off your mortgage by the time you retire. So, for example, a 50-year old who wants to retire at age 65, should opt for a 15-year mortgage.
- Mortgage rates could fall even further in the next couple of months given the sharp decline in the rate on the 10-year U.S. Treasury.

Miscellaneous Items Related to the COVID-19 Crisis

Unemployment Benefits are Taxable: With over 25 million Americans now collecting unemployment, it is important to realize that at least for federal tax purposes, the benefits are taxable as ordinary income. While there is an option for recipients to have 10% withheld for federal taxes, most people opt to not have this withholding done. This may result in a significant amount of taxes owed for 2020 federal returns, particularly given that the CARES Act has increased unemployment benefits by an extra $600 per week through July 31st. To avoid being under withheld, we recommend making federal estimated tax payments. Federal estimated payments for the first two quarters of 2020 are due July 15, 2020.

Required Minimum Distributions Optional for 2020: As discussed in our March and April Monthly Commentary, IRA, Inherited IRA and other pension plan RMDs for 2020 are now optional. If you are subject to taking an RMD, and don't need the funds, we recommend that you opt out of taking it for 2020.

Are College Housing Refunds Subject to Tax? With the onset of COVID-19, many colleges began cancelling on-campus classes and closing student dormitories, sending many parents or students partial refunds for room and board. If these expenses were paid with funds distributed from a Section 529 plan, there may be a taxable event. Luckily, there are options available to avoid tax and penalties.

Any refunded Section 529 distributions typically have 60 days from receipt to be deposited back into the 529 plan to be treated as a nontaxable recontribution. As a COVID-19 relief effort, the IRS has extended this timeline. If the 60-day period falls after April 1, 2020, and before July 15, 2020, the recontribution can be made any time before the later of July 15, 2020, or 60 days from receipt, to avoid tax and imposition of the early withdrawal penalty.

There are also other options to utilize the returned cash without having tax or penalties incurred. As long as the amounts are used for qualified educational expenses, these distributions are not subject to tax. In addition, beginning with distributions made after 2018, the SECURE Act treats up to $10,000 of student loan principal and interest payments as Section 529 qualified educational expenses.

Estate Planning for the 2020's
By Lauree Murphy

COVID-19 has given us a new perspective on the fragility of life. Planning for death is not a subject most people want to think about. Even those who have been proactive with their trust and estate planning should review and monitor periodically. In the current environment, with very few people subject to estate tax, planning may be viewed by many as irrelevant. On top of tax planning, there are other reasons to do estate planning, including appointing guardians for young children, providing for those with special needs, putting a person you trust in charge of handling your affairs when you die or if you are no longer capable, and making sure your healthcare wishes are met. Additionally, for the reasons discussed below **NOW** is an important time to create or review your estate planning documents.

Economic Risk- With the economic stimulus package and loan programs initiated during the COVID-19 crisis, the Federal Government has spent trillions of dollars. This will bring pressure to raise revenue to keep the country solvent. Tax increases are likely in the near future. Estate taxes have become an insignificant source of revenue. Currently, due to the generous estate tax exemptions, only about 1,800 estates are subject to estate taxes each year. Estate taxes are certainly one of the items that Congress will consider adjusting to generate additional revenue.

Political Risk- The Tax Cuts and Jobs Act signed into law at the end of 2017, significantly increased the estate tax exemptions. In 2020, the estate tax exemption is $11.58 million per person. For married couples, that amount is doubled, raising the total estate tax exemption to $23.16 million. The current estate tax exemption rates are due to expire 12/31/25. If no action is taken by Congress, the rates will revert back to 2017 values with inflation adjustments. It's estimated that the inflation adjusted exemption in 2026 would be about $6 million per person. With an election coming in November, if there is a shift in political control, changes in the estate tax law may come as early as 2021. A plan put forward by Senator Sanders, called "The 99.8% Act," proposes lowering the exemption to $3.5 million per person. This is a dramatic and significant decrease from the current law.

Portability- In 2011, portability was introduced. Portability means that if the first spouse dies and does not utilize his/her estate tax exemption, then that exemption can be carried over to the survivor by making a portability election. This in effect doubles the estate tax exemption for couples. In order to take advantage of portability, when the first spouse dies, an estate tax Form 706 must be filed. The form is simpler if you are only filing to get portability. The Deceased Spouses Unused Exclusion (DSUE) Schedule is used to list the assets. Formal appraisals are not always needed. Making the election while the exemption is high will leave the surviving spouse with a big exemption, even if a law change later reduces the exemption amount.

Bypass Trusts- Trusts drawn up before 2018 often used a formula clause to create a credit shelter or bypass trust, equal to the full value of the estate tax exemption. The intent is to shelter tax at the first death on the property in the bypass trust and prevent it from being taxed at the second death. That worked fine when the exemption was lower. However, with today's high exemption rate, too much may end up in the bypass trust. Furthermore, the bypass trust may no longer be needed due to the ability to claim portability.

There is still a need for the bypass trust in some estate plans. There may be assets that are expected to appreciate significantly between the time they are valued for the DSUE when the first spouse dies and years later when the surviving spouse dies. If those assets were held in the bypass trust, it does not matter if they appreciate, as those assets are not taxed at the second death.

Planning for Future Law Changes- With tax laws changing frequently, it makes more sense to have a trust document written with some flexibility. Therefore, it is important to write alternatives into the plan. For example, if the exclusion is X dollars then take action Y, while if the exclusion is lower than X dollars, then take action Z.

While California does not have an estate tax, a number of other states do. If you live in a state that does have an estate tax, you should take those laws into consideration when drafting your plan.

Gifting Opportunity to Take Advantage of Before 2021- Lifetime gift exemptions and the estate tax exemption are tied together. Gifts that are made now are allowed the current high exemption rate $11.58 million per person. If the exemptions are later lowered by a law change, gifts made prior to the law change will not be clawed back. This provides an excellent opportunity to make large gifts this year for those with a very significant amount of assets.

Estate Planning for the 2020's
By Lauree murphy– con't

Giving away assets that have a low basis to those in lower tax brackets can be a great way to reduce taxes. This can be a very good way to support children with low incomes or elderly parents in low tax brackets. The recipient of the gift receives the donor's basis. If the recipient later sells the asset, that individual may pay little or no tax on that sale depending on his/her tax bracket.

Here is a list of the items that belong in many Estate Plans:

A Revocable Living Trust with Pour-over Wills- This will help reduce your estate settlement costs, reduce the time required to settle your estate, and avoid probate to ensure that your financial affairs do not become part of the public records. A Will allows you to choose your own executor and make specific bequests. A Will is also where you designate a guardian for minor children. In your Will, you may want to consider giving your executor the right to access your digital accounts. It is prudent to maintain a separate list of digital accounts, log in names and passwords. Additionally, it is recommended to keep updated copies of this list with your estate planning documents.

Durable Powers of Attorney- This will allow a designated person to act on your behalf should you become disabled or incapacitated.

Advance Medical Directives- These Advance Directives are designed to allow you to control your own medical care, and to some extent, control your quality of life, even when you are subsequently no longer able to verbally express your own consent due to incapacity.

HIPPA Release Form- The Health Insurance Portability and Accountability Act (HIPAA) protects patient's medical records and other information. No one can access your personal medical information without having a signed notarized document allowing access. Prepare in advance by filling out an Authorization to Disclose Protected Medical Information form, also referred to as a HIPAA release form. It must be signed and notarized. Individuals who are listed on the form can then receive information about your medical condition. An attorney can help with this, or you may check with your doctor or medical institution to obtain the form they use.

Sincerely,

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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

Tax Reminders:

- July 15th is the deadline for filing 2019 individual income tax returns and making 2019 IRA, SEP-IRA, Roth IRA and Education Savings Account contributions.
- July 15th is also the deadline for first and second quarter 2020 Federal and State estimated payments.