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Our quarterly newsletter

FOCUS FINANCIAL®
RED ROCK GROUP

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Q1 2023 MARKET REVIEW

Coming off the heels of a dismal year in 2022, markets rebounded in a big way in January. The S&P 500 finished with a gain of just over 6% and the NASDAQ notched its best January performance since 2001.

Driving the rally was the declining rate of inflation, which indicated that the Federal Reserve (Fed) could be close to ending its monetary tightening program. However, optimism over the Fed ending rate hikes was quickly squashed with a hotter-than-expected jobs report and a stronger-than-expected increase in the Fed's preferred measure of inflation, which raised concerns that further rate increases may lie ahead.

In March, markets received a shock as Silicon Valley Bank and Signature Bank became the 2nd and 3rd largest bank failures in U.S. history. Ultimately, while volatility may persist in the near-term as confidence in the banking sector takes time to fully return, we see opportunities forming in both the equity and fixed income spaces in the months ahead.

Almost exactly one year after the start of the Federal Reserve's most aggressive ratehiking campaign in four decades, the recent bank troubles could potentially mark a turning point in monetary policy. A potential pause in the Fed hiking cycle could spur both equity and bond markets.

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UNDERSTANDING FDIC INSURANCE AND SIPC

With recent headlines about two failed U.S. banks and their ripple effect throughout the banking sector, we want to summarize the latest information on this evolving event. We assure you we are monitoring the situation closely. However, it's important to note that such events can cause short-term market volatility.

On March 10, 2023, Silicon Valley Bank (SVB), the 16th-largest bank in the U.S., headquartered in Santa Clara, California, failed. SVB's customers include small to mid-sized technology companies and private bank customers, some of which are individuals.

On Monday, March 13, 2023, The FDIC transferred all deposits—both insured and uninsured—and substantially all assets of the former Silicon Valley Bank of Santa Clara, California, to a newly created, full-service FDIC-operated 'bridge bank' in an action designed to protect all depositors of SVB. As a result, depositors will now have full access to their money. In addition, customers will be made whole on their deposits through FDIC insurance fees that FDIC -member banks pay to have their customers' deposits insured up to $250,000.

FDIC Insurance and what it covers

The Federal Deposit Insurance Corporation (FDIC) was created during the depression of the 1930s to help rebuild Americans' trust in the banking system. During this period, many banks failed, and depositors lost assets.

FDIC insurance covers the following deposit products:

- Checking accounts
- Savings accounts
- Money Market Deposit Accounts (MMDAs)
- Certificates of Deposit (CDs)
- Negotiable Order of Withdrawal (NOW) accounts

FDIC insurance DOES NOT cover non-deposit products such as:

- Stocks
- Bonds
- Mutual funds
- Annuities
- Insurance products
- Crypto assets

This is an important distinction since FDIC coverage does not protect investments.

For investments, it's essential to understand how SIPC protection works.

The Securities Investor Protection Corporation (SIPC) offers limited protection to investors. SIPC works to restore investors' assets when a member brokerage firm fails financially. Brokerage firm failures are rare. However, if it happens, SIPC protects the securities, mutual funds, bonds, and cash in your brokerage account up to $500,000.

SIPC protects your investments if:

- Your brokerage firm is a SIPC member (we are).
- You have securities at your brokerage firm.
- You have cash at your brokerage firm to buy securities.

SIPC does NOT protect if:

- The firm is not a SIPC member.
- Against market loss.
- Promises of investment performance were made.
- Your investment is a commodities or futures contract.

Recent market volatility serves as a reminder of the importance of maintaining a diversified investment portfolio that considers a client's risk profile and time horizon. We've taken these factors into account when establishing and maintaining your portfolio. However, should you have concerns, please call our office anytime.

WHAT IS A BACKDOOR ROTH CONVERSION?

We often get questions like, “How can I balance my tax obligations with my financial goals?” and one possible option is a Roth IRA. Roth IRAs are tax-advantaged retirement savings accounts that can be quite useful if you expect your tax obligations will rise as you get older. Because withdrawals from a Roth are tax-free, it’s an especially attractive option for high-earning households. Unfortunately, the US tax code prohibits individuals or households from contributing to a Roth IRA if they earn over a certain annual income. But there IS a workaround (creatively known as a “backdoor Roth conversion” among tax and financial professionals).

How does a backdoor Roth conversion work?

Problem: You can’t open/fund a Roth IRA because you earn over the income limit (specified in the low-to-mid-six figures, depending on your filing status).

Solution: Because traditional IRAs have no income limit, you would open a traditional IRA and then (here's the tricky part) instead of funding it with a normal deductible contribution, you would fund it with a nondeductible contribution (meaning you won't claim the deduction on your taxes). You then convert the traditional IRA into a Roth IRA.

That's the idea in a nutshell, but be aware that it can be complicated, especially when you start to account for tax situations specific to your household.

What are the pros?
The converted funds now held in the Roth IRA give you access to your funds tax free after age 59.5 with no required minimum distribution. You can even pass it to your heirs (and unlike a traditional IRA, your heirs owe no taxes on an inherited Roth IRA). Also, under current regulations, there is no limit to the amount of money you can convert from a tax-deferred account to a Roth IRA.

What are the cons?
Because you haven't yet paid taxes on the money in a traditional retirement account, when you convert it to the Roth IRA the IRS views that as taxable income. So, you owe taxes on the amount you convert in the year you execute the conversion. For example, suppose you're in the 24% tax bracket and converted $100,000. That means you could owe $24,000 on top of your expected annual tax obligation.
There are other factors that can make a backdoor conversation complicated or messy, especially if the account you'll be converting contains funds from different sources. And remember, if you convert from a Traditional IRA, you have to wait five years before you can withdraw funds penalty free.

ARE YOUR PASSWORDS STRONG ENOUGH?

With the surge of online services and the increase in smartphone and tablet usage, password security is critical. The use of passwords remains the primary authentication protocol for online accounts, so keeping passwords secure is vital to protecting your accounts.

A common frustration is that complex password requirements make it difficult to create passwords that are tricky/unusual yet also easy enough to remember. This complaint is universal and has actually led to easier breaches for cybercriminals. Why? People who are burned out from password overload are more likely to either memorize one password and use it across multiple accounts, or utilize passwords that are simple and easy to remember (and therefore are easy to crack). Password123, anyone?

How can you ensure your passwords are strong and secure, so the barrier to entering your online accounts is at maximum density? Follow these three tips:

1. Use two-factor authentication. Many businesses that store your personal information now offer you an extra layer of security by either texting a one-time code, asking you multiple security questions, or requesting your fingerprint recognition to confirm that it's truly YOU trying to access the account. There's a huge security benefit to using these high-tech features.

2. Use "passphrases" instead of passwords. Instead of using a one-word password, string together a few words with symbols in place of letters to create a "passphrase" relevant to each account, such as "Thi$I$MyFir$tHomeloanAccount". Not only do these phrases fulfill the newer, complex password requirements, but they can be much easier to remember and harder to crack.

3. Use a password manager, not a sticky note. Instead of surrendering to using simple passwords or writing them all down, use a password manager. Think of it as a vault that holds all your passwords, and only you have the master key. So you only need to remember one strong and unique password while the manager remembers the rest for you. LastPass, Dashlane, and 1Password are a few of the highest-rated options; just be sure to do your research to find the best option for you.

Choosing and using the best passwords and keeping them secure is one more way for you to significantly reduce your online risk.

HOW LONG SHOULD I KEEP MY TAX RECORDS?

Here's how long you should maintain records, plus exceptions to the three-year rule.

Keep tax records for three years if:

- No fraud was committed and all income was reported.
- You filed a claim for a credit or refund after your return was filed.

Keep tax records for four years if:

- You maintain employment tax records. Keep these for at least four years after the date the tax comes due or is paid, whichever is later.

Keep tax records for six years if:

- You could have underreported your income by 25%. If this is the case, the IRS can review your taxes from up to six years ago.

Keep tax records for seven years if:

- You filed a claim for a loss from worthless securities (including loser stocks or bonds) or a bad debt.

Keep tax records indefinitely if:

- You purchased property, so you can show the amount that you originally paid for it.
- You do not file a return each year.
- You filed a fraudulent return.

STORING YOUR TAX RECORDS DIGITALLY

People have decluttered their offices and are storing their documents digitally. Many institutions also issue digital copies of tax forms, further reducing your tax paper trail.

In addition to reducing paper, storing your tax records and receipts online or in the cloud can be convenient—but make sure your online storage provider encrypts your data so a cybercriminal can't easily steal your Social Security number or other information that can easily identify you. You can protect your files and folders by adding a password.

When it is feasible, scan documents, store and back them up. Dispose of the paper copy at will, as long as it's not an original deed, title, valuation or original investment paperwork. Keep those (e-)documents secure.

The IRS keeps a record of your tax returns from previous years. You can request a transcript online, by phone or by mail. The tax agency will ask for proof of identification, including your Social Security number.

If you use a CPA, don't rely on your accountant to keep records for you. Taxpayers should maintain copies of tax returns and related documents themselves.

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