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Markets Can and Do Go Down.

How Will You Handle It When It Happens?

by William H. Smith, CFP®

Over the last couple of months I've had several conversations with a prospective client (Mr. P.C.) who had been referred to us. We had several preliminary discussions on the value of a disciplined investment approach. I provided him books and articles that made the compelling case for not trying to time the market, but rather highlighted the advantages of asset allocation. I generally tried to reinforce the fundamental concept that investment success is determined by *investor behavior, not investment performance.*

In late August I got a call from Mr. P.C. who informed me he had completely liquidated his tax deferred account. This account was invested in a well-diversified global fund with which I am very familiar. He stated that he would be ready to become a new client of Trust Company when "the time was right." Our conversation went something like this.

Trust Company: So you've liquidated everything in your portfolio? Please share with me how you came to that decision.

Mr. P.C.: Well, the market's going down and that fund keeps going down. Everyone knows we're going to have a recession. I'll sit on the sidelines and just see what the market does for a few months.

Trust Company: Mr. P.C., that sounds like market-timing to me. Remember, we've talked about this!

Mr. P.C.: I'm not timing the market, I just want to wait and see.

Trust Company: Wait and see what?

Mr. P.C.: Everyone knows we're headed for recession. I'll just see what happens.



NOTABLE QUOTE

"The fact that people will be full of greed, fear, or folly is predictable. The sequence is not predictable."

Warren Buffett

The Trust Company of the South is a fee-only independent trust company and financial planning firm focused on serving the needs of affluent individuals, families, and non-profit institutions.

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Update Your Health Care Directives!

by John Slayton, JD, LL.M.-TAX, CFP®

The 2005 Terry Schiavo case in Florida has caused a lively discussion regarding the clarity of North Carolina's "living will" and "health care power of attorney" (HCPOA) statutes. The NC Bar Association and Medical Society recently undertook to upgrade and align the two laws. This summer, the NC Legislature adopted H.B. 634 and, effective November 1, the living will and HCPOA statutes have been clarified and new more user-friendly statutory forms are available. End-of-life issues are never easy or painless, but these changes should provide more understandable means to exercise your self-determination rights and clearer ways to express your end-of-life wishes.

H.B. 634 makes significant changes to two fundamental NC statutes:

- >> The NC living will statute, adopted in 1979 in response to the Karen Ann Quinlan case in New Jersey, specifies the procedures for withholding medical treatment in end-of-life situations, when there is no advance directive in place.
- >> The NC health care agent and HCPOA statute was adopted in 1991 in response to the Nancy Cruzan case in Missouri.

Many people have executed both a living will and a HCPOA. Historically, if a health care agent gave an authorized instruction that appeared to be at odds with an instruction in a living will, heated debate often ensued as to which instruction prevailed. People who execute both instruments may have intended for the designated health care agent to have the final say, but health care personnel often argued the living will controlled. Careful review of the two statutes and instruments did not adequately clarify which instruction should prevail. This often resulted in additional distress during singularly emotional situations.

The new law:

- >> Allows you to *choose* whether the authority of a health care agent or the wishes stated in a living will "trumps"

in the event of a conflict. You select an option on the form.

- >> Allows you to *require* your living will be honored regarding withholding medical treatment, rather than leaving the option with the attending physician.
- >> Brings *clarity* and *consistency* in terminology in both documents to doctors, patients and family members. Clarifies new terms for what and when life-prolonging treatment may be withheld.
- >> Delivers more *user-friendly* and *understandable* non-exclusive statutory forms, with more flexibility and direction in exercising choices.
- >> Clarifies procedures for withholding life-prolonging measures when no living will or HCPOA applies.

What You Should Do Now

- >> *If you have signed old statutory forms, they remain valid, according to their terms. They are subject to the previous ambiguities in their interaction, however, so you might want the clearer new forms.*
- >> *If you have been considering updating your estate planning documents, availability of these new user-friendly forms might provide adequate reason to go ahead and start the process.*
- >> *Because the vast majority of living wills and many HCPOAs are executed without the assistance of lawyers, often when checking into a health care facility, you should pay more attention when you are completing them and be sure you understand the forms and the choices you are making. Understand what artificial nutrition and hydration involves... it can be invasive. To help you comprehend the impact of what you are signing and to maximize self-determination, the new forms include more meaningful choices and they provide you with more guidance as to how to complete them.*

Contact your estate planning attorney or give us a call to discuss how to proceed!

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Trust Company: You seem to have some pretty good information. When is the recession coming? How long is it going to last? Assuming a recession does come and stock prices do go down, how far down will the market have to go before you are ready to get back in?

Mr. P.C.: I'm not sure, depends on the recession.

Trust Company: How long will you wait for the recession to occur?

Mr. P.C.: I don't know.

Trust Company: Let me make sure I understand. You've taken action (liquidated your account) based on an event you are predicting will occur, but you can't tell me how long before it will occur or what magnitude of impact it will have to have before you allow Trust Company to implement our investment strategy?

SILENCE

That conversation took place on August 23rd. Mr. P.C. could not provide either a degree (amount) or duration (time) at which point he would be prepared to re-enter the market.

Mr. P.C. is right; there will be a recession.....someday. We don't pretend to know when it will occur, how long it will last, and what it might do to the equity markets. In reality, a successful investment strategy is completely independent of the accuracy of a forecast. I regret I was unable to enlighten Mr. P.C. on the shortsightedness and the emotional nature of his decision.

Here are three simple strategies to help you prepare for the next market decline (the key to which is realizing the ship really isn't sinking)!

>> **Regain (or Reframe) Long-Term Perspective** – The best way I've found to do this is to look back at decades. Take the period 1960 – 1970. Think of all the reasons one might have had at any point during that decade to worry about the future. We had the Cuban Missile Crisis, JFK's assassination, the Vietnam War, and the Civil Rights turmoil. One could find lots of reason to abandon equities. But from 1960 to 1970 the S&P 500 went from 55 to 92. Each decade has similar trials and tribulations; Watergate, Arab oil embargo, double digit inflation and disco in the 1970s (okay disco may not have been a threat to the free world, but it was pretty bad!). By looking back, it allows one to look forward with proper perspective and optimism.

>> **Understand How Your Brain Works** – The urge to act to avoid market declines can actually be traced to our evolution as a species. Our reflexive brain is very good at avoiding saber tooth tigers and other threats, but serves us very poorly as investors. As Jason Zweig points out in his new book, *Your Money and Your Brain*, researchers from the fields of medicine and psychology have found that human brains react nearly 3 times stronger to loss than to gain. Slow down, allow the reflective brain to work and you'll likely be a better investor.

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BOOK REVIEW



Your Money and Your Brain

by Jason Zweig

In today's marketplace, there is a constant barrage of "how to" books on investing and personal finance. Mr. Jason Zweig's book, *Your Money and Your Brain*, is a unique and refreshing change of pace in that it focuses on the emotional elements that drive us (investors) to make the decisions that we make regarding our money. Mr. Zweig is a senior writer for Money magazine and has been a columnist for Time magazine. He is also the editor of the revised edition of Benjamin Graham's *The Intelligent Investor*, the classic text that Warren Buffett has described as "by far the best book about investing ever written."

Mr. Zweig refers to a study known as "neuroeconomics," which focuses on several key concepts that affect the investment decision making process; greed, fear, risk and overconfidence. The book provides numerous examples of common mistakes individuals make and also provides excellent perspective on how managing your emotions will help you manage your money more effectively. In addition, one

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Behind the Scenes at Trust Company of the South

- >> **Wallace Williams** and her husband, Greg, chaired the “Light the Night” walk for leukemia and lymphoma research that was recently held in Greensboro, North Carolina. The fundraiser was quite successful and The Trust Company of the South was the major contributor of the event.
- >> **Becky Faucette** recently celebrated ten years of service with The Trust Company of the South. Congratulations, Becky!
- >> **Brandon Cook’s** band, Solace of the Sun, performed at the Life Rocks Benefit Concert in Greensboro, North Carolina. The concert benefited the Hodges Children’s Cancer Fund.
- >> **Bill Smith** was recently named President of the Burlington Downtown Corporation; an organization established to promote economic development in downtown Burlington, North Carolina.

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- >> **Do the Math** – It may be counterintuitive, but when the price of the overall market drops, so does the risk. Stocks are one of the few things that people seemingly want more of when prices are high and less of when prices are low.

Market declines are common, and should be embraced by disciplined investors much like a “killing frost” that deters speculative buyers while maintaining the long-term health of the financial ecosystem. Having a disciplined investment plan in place *before* adversity strikes reinforces appropriate behavior and helps avoid making emotional decisions when we encounter the inevitable market turbulence.



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BOOK REVIEW, cont'd

of the more comforting findings from Mr. Zweig’s research is that you don’t have to be rich to be happy. If you are truly interested in “knowing thyself” from an investment and personal finance perspective, we would highly recommend this book.

Excerpts from Your Money and Your Brain

>> **Avoid the “sure thing” – Your “seeking system” is especially turned on by the prospect of a big score, and that in turn will hinder your ability to calculate realistic odds for the success of an investment. Be on your guard against any sales rep who tries to lure you with jackpot jargon like “can’t miss,” “double your money,” or “the sky’s the limit.”**

>> **Remember: Lightning seldom strikes twice – If you’ve ever had the taste of a big gain, you’ll likely be tempted to try to get that feeling back. So be especially wary of investing in stocks or mutual funds that remind you of the one you made a killing on long ago; chances are, any similarities to another investment, living or dead, are purely coincidental.**

>> **Think twice - Making a financial decision while you’re inflamed by the prospects of a big gain – or a huge paper loss – is a terrible idea. Calm yourself down (if you don’t have kids to distract you, take a walk around the block or go to the gym) and reconsider when the heat of the moment has passed. – William H. Noble, Principal**