[thecompass] spring 2011

THIS ISSUE...

Bricks & Mortar:
Does Your Financial Advisor Provide Both?

by Mike Palmer, CFP®

Several years ago my wife and I built a new home. It was an exciting and challenging experience, one that required multitudes of choices and reliance on professionals with expertise and wisdom that we simply did not possess. I remember visiting our contractor's brick supplier and getting a lesson in the various types of brick. We learned the differences in textures, colors and the importance of mortar. I remember being surprised by the importance of the mortar selection. There are parallels between the role of mortar in home construction and how one distinguishes between financial advisors.

On the surface, it would seem mortar is far less important than brick; after all, I don't recall the third little pig asking about the mortar as he bought bricks to build his wolf-proof home. What few people realize is that mortar makes up about 20% of a bricked surface area. The color of the mortar has a subtle but noticeable impact on the color / appearance of a home. There are also base loads, mixing requirements and time sensitivities that affect how the mortar performs in binding with the brick.

In the financial services profession there are lots of purveyors who supply investment products (bricks) but relatively few who provide the mortar that provides families with a secure financial foundation. Having the capability to understand the myriad elements impacting a family's financial security and identify solutions before problems arise is a distinguishing characteristic of our firm. While many people focus on investments, we believe wealth (what money provides) is a far more important consideration and more impactful on one's financial security. Modifying investor behavior, providing historical perspective, and giving unbiased advice in the context of each client's individual goals are examples of the skills that distinguish advisors that thrive in working with mortar.

Very simply, we view the investing component of what we provide as bricks. Lots of advisors have satisfactory bricks. However, not every financial advisor possesses the mortar - the experience and wisdom to provide comprehensive counsel on financial planning variables that pose the greatest risk to a family's financial security.

NOTABLE QUOTE

"Prediction is very difficult, especially about the future." - Niels Bohr, Nobel-winning physicist

Trust Company of the South...because wealth management is more than managing money

Happy Birthday Obamacare!!

by John Slayton, CFP®

As we celebrate the first anniversary of the passage of the most aggressive health care reform law in generations, let's take a moment to look beyond the myriad legal challenges pending in various states and review some of the cash-saving benefits currently available. Like the famous spaghetti western, *The Good, the Bad and the Ugly,* many of the benefits of health care reform are front-loaded, while the expenses follow in later years, so what should we do now before we have to pay later?

- **Bye-bye "Donut Hole"** – Many readers are familiar with the Medicare Part D prescription-drug program donut hole – the coverage gap after your total (insurance and out-of-pocket) drug costs reach $2,840 for the year, until your out-of-pocket drug costs reach a "catastrophic" level of $4,550 for the year – during which period you must pay all drug expenses. The donut hole starts to close in 2011 and is gone by 2020. This year, after your total drug costs reach $2,840, your pharmacist will automatically apply a 50% discount on name-brand drugs, until you reach the $4,550 out-of-pocket level, after which the government pays the bulk of the cost. Many seniors have learned about the high cost of certain drugs as they navigated through the donut hole in recent years. The government also picks up 7% of the cost of generic drugs in the donut hole this year.
- **Get that Annual Physical** – Many insurance plans that previously did not, must now provide certain preventive-care screenings, without charging deductibles or co-pays. Depending on your age, this may allow blood-pressure, diabetes and cholesterol screenings, colonoscopies and mammograms, flu shots, routine vaccinations and well-baby and child visits. Certain insurance plans that have not made recent substantial changes may be grandfathered, so check your plan. Seniors on Medicare now may receive an annual wellness visit and a personalized prevention plan, and are no longer charged co-pays or deductibles on many screenings.
- **Preexisting Conditions Less Worrisome?** – In 2014, insurers will be prohibited from rejecting people because of their health and pre-existing health issues. Until then, the law has created high-risk insurance pools to help cover people with health issues. Countless employees have been trapped in undesirable employment situations, due to fear of being uninsurable in a new employer's plan. So a Pre-Existing Condition Insurance Plan sounds great. Unfortunately, to qualify you must have been uninsured for at least six months. If you have been uninsured for an extended period, this works. But if you are about to lose coverage, better alternatives might include coverage-extension requirements (18 months under COBRA) or previously existing state high-risk pools without the six-month waiting period. If you are leaving one employer's plan, without another plan to move into, COBRA can be expensive, but generally costs less than an individual policy – particularly if you have health issues. Waiting six months is risky.
- **Health Savings Accounts ("HSAs") and Flexible Spending Accounts ("FSAs")** – no longer allow use of pre-tax deferred dollars to purchase over-the-counter drugs, such as pain relievers, allergy and cold medications and nicotine patches – only prescription drugs and insulin. Work around this limitation by getting a prescription from your doctor for any of these over-the-counter medications that you regularly use, then go ahead and use your HSA to buy them.

Continued on back cover

Beware: Financial Media Ahead

by Mike Palmer, CFP®

As one gets older there usually become fewer absolutes in life. But as with many things in life, there are always exceptions. My exception is mainstream media (especially CNBC) and its coverage of financial crises, real or imagined (mostly the latter). Viewers of CNBC should really be subjected to a financial equivalent of the surgeon general's cigarette warning label. *WARNING: The content you are about to view and the incessant talking heads that are about to pontificate are hazardous to your financial health. The opinions expressed by our guest "experts" have proven to be less accurate than monkeys throwing darts at the Bronx Zoo.*

Over the last fifteen months any number of headlines could have deterred the average person from staying the course and remaining a long-term equity investor. The Deepwater Horizon oil disaster, the near default of Greece sovereign debt, double digit unemployment in the US, a falling dollar, the "flash crash" of May 2010, the Japanese tsunami / nuclear accident, the wave of populist uprisings in the Middle East, gold at nearly $1500 an ounce, gas prices up nearly a dollar per gallon in less than twelve months. The list of "apocalypse du jours" is nearly endless. And it will always be so.

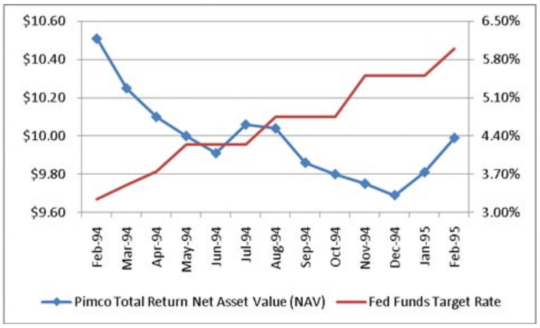
During that time the market (as measured by the S&P 500 index) is up 22%. From March 2009 to April 2011 the index is up 150%, the strongest 24 month period in over thirty years. Those who are weak of heart (or fortitude) have missed it.

The media's purpose (especially the financial media) is antithetical to the aims of the long-term investor. Here are just a few reasons why. The media is in the business of short-term, not long-term. The media deals in news, not information or education. The media's main goal is to keep your attention. They do so with flashing lights, movement (streaming crawls along the bottom of the screen) and bombarding you with a Hollywood Squares of talking heads taking up what little screen space remains. Successful investing is more often than not boring; typically the less activity that occurs within a portfolio the better.

As noted financial columnist Nick Murray wrote recently, "the financial media does not know you (the client), does not care about you and wants only to keep you reading and watching."

The advisor absolutes I know are that market corrections are part and parcel of being a long-term equity investor. These corrections cannot be predicted with any regularity or consistency and therefore I will not try. Fleeing a decline I know to be temporary makes no sense. It is never different this time, irrespective of how many "experts" on CNBC say it is so.

Are Bonds More Risky Than Stocks?



Fixed income investors have enjoyed the most remarkable of tailwinds the last 15+ years that it is hard for many investors to remember that bonds can lose value. The 10 year Treasury yields only a smidge more than the historical inflation rate, yet investors continue to plow money into bonds. According to ICI, over the last 12 months investors have poured more than $152 billion into bond funds while at the same time equity funds have seen *net redemptions* of more than $32 billion. This perverse dynamic is not uncommon. Regrettably most individual investors left to their own devices (and many enabled by financial advisors that do very little advising) fail to see price and value as inversely correlated. The last time the Fed really tightened the money supply was in 1994-95. During that time the fed funds rate increased six times in a 12 month span. As you can see from the chart above, the PIMCO Total Return fund lost about 10% of its value peak to trough.

Trust Company of the South...because wealth management is more than managing money

Behind the Scenes at Trust Company of the South

>> **Mike Palmer** recently attended the DFA National Advisors Study Group meeting in Atlanta.

>> Cameron Shirley, daughter of TCTS employee **Lisa Shirley**, was awarded the Lumen Scholarship at Elon University.

>> **Jay Eich** has been named to the board of the First Tee of Charlotte.

Continued from page 2

Remember that HSAs require that you have a health-insurance policy with at least a $1,200 deductible for individual coverage ($2,400 for family coverage). Permitted HSA withdrawals before age 65 include insurance deductibles and co-payments, prescription drugs, dental care and a portion of long-term-care premiums (depending on age). Note, however, that the penalty for nonmedical expense withdrawals before age 65 has doubled, from 10% to 20% this year – on top of ordinary income tax rates.

• **Keep the Kids Around** – The most popular new rule with my senior-year finance students at Elon University now allows adult children to stay on their parents' health-insurance policies until age 26, rather than kicking them off when they turn 21 or graduate from college. You can even add adult children to your health-insurance policy in the middle of a plan year, if they lose their coverage (such as if they graduate from college). This is a huge benefit to recent graduates, who may not have yet secured full-time employment providing group health insurance benefits, and are therefore confronted with obtaining expensive individual coverage.

The health care reforms provide needed coverage for millions of under-insured Americans. We all know that sooner or later we will have to pay for these changes, so let's make sure we fully utilize the benefits available to us in the interim. *Be careful out there!!*

THE TRUST COMPANY OF THE SOUTH

Raleigh Office

Michael H. Palmer, II CFP®, Principal
919 781.8287
mpalmer@tcts.com

William H. Noble, Principal
919 781.8287
bnoble@tcts.com

Burlington Office

William H. Smith, CFP®
Managing Principal
336 538.1000
wsmith@tcts.com

John H. Slayton, JD, CFP®, Principal
336 538.1000
jslayton@tcts.com

Mitchell H. Paul, CPA, Principal
336 538.1000
mpaul@tcts.com

Charlotte Office

Jay D. Eich, CFP®, CPA, Principal
704 936.4302
jeich@tcts.com

Christopher N. Sutherland, CPA
Principal
704 936.4303
csutherland@tcts.com