QUARTER
04
2011

QUARTERLY
JOURNAL OF
FINANCIAL
KNOWHOW

Dave Pohl & Associates Financial
informer ©

this issue

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Keeping a cool head during volatile times

Market swings and global economic uncertainty are keeping investors up at night, but there are ways to stay sane in an insane economy. As the markets rollercoaster and uncertainty hangs over the economy in ways we haven't seen since 2008, it's a good time to address how all the turbulence has impacted investors' psyches.

Money and psychology are inextricably linked. It's the reason people often call the markets "skittish" to explain drops with little cause. And fear and panic are the main emotions that drive investor selling, almost always irrationally.

Mind over money

But what most investors don't realize is that in addition to collective market psychology, almost everyone has his or her own individual psychological issues with money. While crashing stocks, ballooning mortgage payments, or the threat of job loss are understandable causes of stress, our more significant problems with money stem from our own internal issues that drive many people to act irrationally when it comes to financial matters -- whether there's a market crisis or not.

The most obvious examples of these issues are the classic money-related pathologies we're all familiar with: gambling addiction, overspending, hoarding, etc. But there are many more subtle everyday examples like the inability to deal with day to day financial tasks, falling for get rich quick schemes, taking on excessive debt, and the inability to attend to important long-term financial issues like retirement or estate planning.

Irrationality with money plays a big role in families, too: the myriad subtle and unintended messages parents give to children regarding money, or relationship problems that can arise over insignificant amounts of money. In a significant number of divorces money is a central issue, and many problems with settling a divorce amicably are money related.

Interestingly, irrationality with money is also evident on an international level, as evidenced by the ongoing financial crisis, during which many global financial institutions (and even countries) and regulatory agencies made decisions that, in hindsight, were clearly problematic and avoidable.

So if it's true that we all have money issues, how do we correct them? The first step is to identify what money means to you—what it *really* means to you.

According to Webster's Dictionary, money is:

1: something generally accepted as a medium of exchange, a measure of value, or a means of payment: as a: officially coined or stamped metal currency

2: wealth reckoned in terms of money b: an amount of money

3: a form or denomination of coin or paper

But these definition, while accurate, don't quite get at what money actually means to many people. An easy way to begin to understand your own relationship with money is to answer the following question:

money = (fill in the blank)

It is amazing how large and varied the list of answers is. Some of the most common are: control, love, power, security, safety, independence, freedom, social acceptance, and sexual appeal. Another easy test is to identify how money is being used, and you'll have a sense of what it means. For example, money can be used to show love, to punish, to foster dependence, to manipulate, to humiliate, and to create alliances.

But whatever the answers, none of the above-mentioned definitions are the same as the dictionary definition; so the next obvious question is, where do these meanings come from? The reality is that most of these additional associations with money develop during childhood.

Children learn about money from a variety of sources, but as is the case with many psychological issues, parents have the greatest impact; specifically, it's the parent's indirect messages that are often the most powerful. As we know, children are sponges, taking in the myriad interactions parents have around money everyday, many of which we don't even pay attention to. Every time we lie about our child's age to get the cheaper movie ticket, or argue with our spouse about the price of a recent purchase, we are sending a message -- often one that's contrary to the conscious message we intend to send.

What parental behaviour, for instance, might lead a child to later equate money with control? Consider the parent who uses an allowance to reward or punish behaviour; like the man who knew he had to behave especially well on Sunday (the day he got his allowance), because if he annoyed his mother on that day she wouldn't give it to him. What about equating money with love? The most common way this gets established is when a parent, perhaps due to guilt over being away from home for business trips, returns home and showers the child with gifts.

"...the person who equates their net worth with their self-worth, and therefore feels terrible about themselves when the Dow starts falling."

These types of interactions on an occasional basis are not necessarily problematic. But when repeated over time, these early experiences can solidify into firmly-held beliefs. And because they're developed through the eyes of a child, they tend to be incomplete or partially true, but yet they become indelible, controlling the way we interact with and use money. Some authors have called these beliefs "money myths" or "money wiring," and "money scripts," because they control our actions just like a script does in a play (this term was first coined by psychologists Brad and Ted Klotz and financial planner Rick Kahler).

One of the most common scripts is "**money is bad**." It's important to note that these beliefs are *sometimes* true, and it's easy to find evidence to support the notion that money is evil. In many divorce proceedings, for instance, money is used for evil purpose, and an awful lot of violence is perpetrated in the name of money. But there is evidence for its opposite as well (the Bill & Melinda Gates Foundation, for example). Someone with the money script "money is bad," however, will see <u>all</u> money as bad, and will therefore avoid things having to do with money. This is the person who sees money as dirty, or who ignores money by not opening their monthly statements, not doing an estate plan, or meeting with a financial advisor.

Another common money script is "**more money will make things better**." If one is in abject poverty, and can barely afford food and shelter, there is no question that more money will make things better. But once we have reached a level of income that takes care of the basic necessities of life, more money does not necessarily make things better, and in fact for some people excess money can actually make things worse. This script can lead to problems like workaholism, or the disillusionment many feel once they have "made it" financially.

A third important script is "**There will never be enough money**." This leads people to hoard out of fear, and is evident in the person who is not willing to take appropriate risks when investing, or keeps everything in cash. Its also evident in those wealthy people whose money is a source of constant stress rather than fulfillment. They simply cannot use their money wisely, because <u>any</u> use of money feels dangerous. It also leads to panic selling, when dips in the stock market feel like the person's money is being taken away.

A final common script is perhaps one of the most pervasive, the script of "**money equals self esteem**." This is the person who equates their net worth with their self-worth, and therefore feels terrible about themselves when the Dow starts falling. This can also lead to the excessive acquisition of material things in order to feel better about oneself.

One final aspect to notice about many of the money scripts is that they can be flipped. For example, the preceding "There will never be enough money," is for some people "There will always be enough money." This script is the source of much of the current mess theglobal economy is in, leading people to believe that real estate values will keep going up, or that they can continue buying things on credit and the money will magically appear from somewhere. These are also the people who take excessive risks when investing.

Now that you have an understanding of money scripts, try to uncover which are relevant to you. What are the overarching beliefs about money that govern your interactions with it, and how might these be influencing your current behaviour and emotional reactions to the crisis?

Once you have a clearer understanding of what money means to you, you are in a better position to weather the inevitable ups and downs of the economy, and to see that often the main source of financial stress is actually not the economy; it's our distorted relationship with money and how it impacts our ability to deal with the crisis. Awareness of money beliefs is the first step; it will allow you to modify those beliefs to fit the current situation, and thereby deal with money more objectively.

To conclude, money is an excellent tool, but only when used appropriately. You wouldn't use a hammer to cut a piece of wood, but we often attempt to use money to achieve things for which it wasn't designed. It can, however, help us to achieve our goals if we use it with care and understanding. When you demystify money, and remove the inappropriate meanings and emotion from it, you are in a better position to use it wisely and purposefully for the betterment of yourself, your family, and your community -- in times of crisis and beyond.

Paying cash, not credit, leads to healthier food choices

Paying with cash instead of plastic at the grocery store leads to more careful spending and healthier food choices, a study in the Journal of Consumer Research finds.

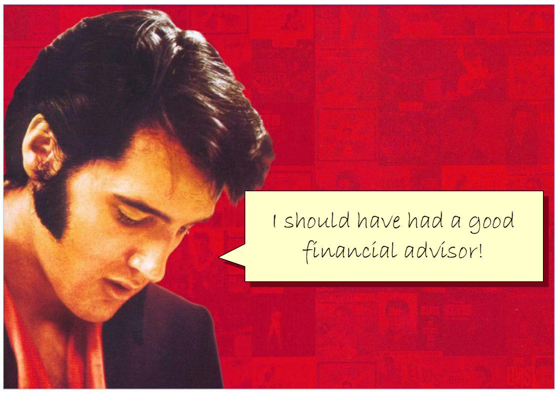
The idea is that shelling out actual money is psychologically more difficult than swiping a credit card, which takes away from the joy of spending. But is that necessarily true and perhaps paying cash leads to making "healthier" buying decisions?

Researchers followed the grocery shopping habits of 1,000 households over six months, tracking what they bought and how they paid for it. The study found that people who used debit or credit cards were significantly more likely to make unplanned, impulsive food choices. Their impulsive purchases also tended to be "vice products," like cookies, cakes and other unhealthy foods.

"The notion that mode of payment can curb impulsive purchase of unhealthy food products is substantially important," wrote authors, Manoj Thomas, Kalpesh Kaushik Desai and Satheeshkumar Seenivasan. "The epidemic increase in obesity suggests that regulating impulsive purchases and consumption of unhealthy food products is a steep challenge for many consumers."

Further study will be needed to determine whether there is an actual cause-and-effect relationship between unhealthy eating or obesity and paying in plastic. If it's any indication at all: 34% of Americans are obese, and in 2009 40% of U.S. grocery purchases were made using a credit or debit card. Makes you think, doesn't it?

Since grocery stores and banks are all for impulsive spending, you'll have to police yourself. It might not hurt to try doling out paper bills the next time you're deciding on a bag of potato chips.



It's a one for the money...

Elvis Presley's estate is reputed to have lost 73% of its wealth to estate taxes and fees. However estate taxes are not only a problem for the rich and famous. The possible impact of Estate Duty and Capital Gains Tax payable on your death should be considered in your financial planning.

"Last Will and Testament - I, the testator, being of sound mind and disposition, do hereby leave, bequeath and bestow upon my friends at the South African Revenue Service, in consideration of their kindness and benevolence to me during my lifetime, a cash amount to the value of 1/5th of my estate." This is seemingly an extract from the Will of a deranged madman, but in effect not necessarily beyond the realms of possibility. Estate duty and capital gains tax can play havoc with your testamentary planning and it's not only the mega-wealthy that have to be concerned.....

Death taxes - an historical perspective

Throughout the ages, governments and rulers have sought to impose new and innovative taxes on their subjects. In the 18th century, English Prime Minister William Pitt the Younger introduced a tax on windows, leading to the creation, by his opponents, of the saying "Daylight Robbery." He also introduced taxes on wig powder, playing cards, servants and dogs. The Russian leader Peter the Great introduced taxes on beards, souls, hats, clothing, food, chimneys and boots, as well as birth, marriage and burial.

However, it is Roman emperor Augustus Caesar who is considered by many to be the most brilliant tax strategist of the Roman Empire. He thought to levy a tax on the one event that even the smartest tax lawyer has not yet formulated a way of avoiding: dying.

Caesar Augustus instituted a death tax to provide retirement funds for his military. The tax was five percent on all inheritances except gifts to children and spouses. This tax was so innovative that the English and Dutch centuries later referred to the inheritance tax of Augustus in developing their own inheritance taxes.

Death taxes – the modern approach

Today many countries levy a form of death tax. A death tax usually takes one of two forms: either an "estate tax" levied on the assets in a deceased estate and payable before the estate passes on to the heirs, or an "inheritance tax" payable by the heirs in an estate.

Many people view inheritance and estate taxes as being the preserve (and concern) of only the mega-wealthy. However, in South Africa this is not necessarily the case. While estate duty applies only to "larger" estates, increasingly "capital gains tax" is likely to have an impact on all estates at some point. So even if you are not reading this article on your private jet, champagne and caviar in hand, continue reading as you might discover that estate duty and capital gains tax are things you should consider in your financial planning.

What is Estate Duty?

In South Africa, our "death tax" is euphemistically called "estate duty". Simplistically, estate duty is a tax levied on an estate after a person dies and is calculated as a percentage (currently 20%) of the value of the net assets in the estate, over and above a certain threshold.

How is Estate Duty calculated?

Estate duty is charged upon the "dutiable amount" of an estate. An "estate" consists of all "property" of the deceased (including immovable and movable property, investments and business interests) wherever in the world this property is situated. For the purpose of the calculation of estate duty, certain assets including the proceeds of life assurance policies, group life payments and lump sums payable by assurers and retirement funds on the death of the deceased are included in the estate. It is important to note that even if one has nominated a beneficiary who will receive payment directly from the institution or fund these payments are still included for the purposes of calculating one's estate duty.

What deductions are allowed in determining an estate?

Estate duty is intended to be levied on a "net" estate and so certain deductions are allowed against the value of the estate before the duty is calculated. Firstly, all the deceased's debts and liabilities are deductible: death-bed expenses, funeral costs, executor's fees, mortgage bonds, overdrafts, outstanding loans and taxes, even any capital gains tax payable by an estate on death (see below) qualify here.

Another important deduction allowed is in respect of the value of any assets or property accruing to a surviving spouse. This "surviving spouse" deduction has in recent years been extended to apply in cases where unmarried "life partners" including same-sex partners, inherit. Thus for the married person who leaves all or the bulk of his or her assets to a surviving spouse, the payment of estate duty on the death of the first-dying is avoided.

On what size estate is the duty imposed?

As estate duty is not intended to be levied on "smaller" estates, all estates qualify for an exemption (called an "abatement") from duty of the first R3.5 million of the net estate. Due to the size of this exemption threshold, people often overlook planning for estate duty. However, if one considers the market value of an immovable property, added to the value of one's business and/or group life, retirement fund and

(Continued on page 4)

One of the most affordable and convenient ways of ensuring that your estate has available funds to pay estate duty and other taxes is by means of a life assurance policy. This policy should be made payable to your estate for the appropriate amount.

Calculating your potential estate duty tax is just one of the services offered by your financial advisor!

"Estate duty can play havoc with your testamentary planning and it's not only the mega-wealthy that have to be concerned..."

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life assurance benefits and other investments, one can quickly and sometimes unexpectedly exceed this threshold.

Until recent years the application of the R3.5m abatement to the estates of married couples was a cause for concern. Previously, if a first-dying spouse left his or her entire estate to the survivor – in which case no duty is levied - then effectively the first-dying spouse's R3.5m abatement was not used. The difficulty was that the first-dying spouse's "unused" abatement was not able to be transferred and used in the survivor's estate when he or she died (i.e. in addition to the survivor's own R3.5m abatement) - a typical case of "use it or lose it".

However, with effect from 2010, the law was amended. Now in calculating the estate duty liability of a widow or widower, the value of any inheritance received from a pre-deceased spouse (up to the abatement amount) can be added to the latter's R3.5m abatement. Only if, despite this concession, a second-dying spouse leaves a net estate exceeding the combined abatement amounts will estate duty be levied.

How much estate duty must be paid?

After allowing for all deductions and the abatement, the result is the "dutiable estate" – it is on this value that estate duty is calculated, currently at a rate of 20%.

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How is capital gains tax levied on death?

Capital gains tax ("CGT") was introduced in SA in 2001. While a taxpayer is alive he or she is taxed on an annual basis on capital gains made on the disposal of various assets such as unit trusts, shares and properties (although the first R1.5m gain made on the sale of a primary residence is exempt from CGT).

Liability for CGT usually only occurs when an asset is disposed of, such as by way of the sale of property or shares, or the repurchase of unit trusts. However, on death a taxpayer is simply "deemed" to have disposed of his or her *entire estate*. This means that even if heirs elect to inherit assets rather than dispose of them, the deceased estate is still potentially liable for CGT! Currently the first R200 000 of total gains thus made by a taxpayer in the year of his or her death is exempt from CGT; the balance of the gain amount will attract tax at an effective rate of up to 10%.

Again, as with estate duty, a concession applies to married couples. Where a deceased taxpayer leaves assets to his or her spouse, a "rollover" of the CGT liability occurs. No CGT is payable by the estate on assets left to a surviving spouse; the "catch" is that when the surviving spouse dies, the capital gains in his or her estate are calculated based on the original acquisition prices paid by *the first-dying spouse*.

When must estate duty and CGT be paid to SARS?

These taxes are payable by the executor of the estate from the assets of the estate, and must be paid before any inheritances can be paid to heirs. The effect on the heirs can be potentially devastating. Not only do these taxes directly diminish the capital an heir will inherit, but in an illiquid estate the executor may be forced to sell valuable assets, such as a home or the family business, sometimes at knockdown prices, to finance the tax burden.

Estate taxes can be a crippling burden on an estate. Unlike Elvis, make sure your wealth doesn't "leave the building"!

Where there's a

To ensure that your estate devolves efficiently and cost-effectively, and with the minimum of inconvenience to your family and heirs, it is crucial that you have an up-to-date Will. It is also crucial that your original Will is stored away safely – copies are not accepted! Here are some of the dangers of dying without a Will ….

1. You have no control over the choice of your executor (or his fees) – your Will should nominate your choice of executor, normally either a professional such as an attorney, bank or trust company, or a family member or friend (who will need to be assisted by a professional). In the absence of a Will your heirs will be required to nominate an executor, causing unnecessary delays and possible conflicts. A Will usually exempts your nominated executor from the requirement to lodge a security bond – basically a guarantee issued by a financial institution to make good any losses suffered by the heirs in the course of the winding up an estate. While the Master of the High Court will usually exempt a deceased's spouse, parent or major child from obtaining a security bond, other family members will find it almost impossible to obtain security bonds. Professional executors will more easily obtain security bonds, but any fees for issuing these are charged to the estate.

2. You have no control over your choice of heirs – if you die without leaving a valid Will, you are said to have died "intestate". In this situation the laws of intestate succession apply. These laws may result in your estate being inherited by persons you would not have chosen as heirs.

3. Inheritances devolving upon minor children may have to be paid into the Guardian's Fund - in the event of intestate succession taking place it is not uncommon for minor children to become entitled to inherit a portion of the estate. The law allows the executor to pay the cash component of a minor's inheritance to the legal guardian of a child heir, but the Master would invariably require the guardian to "provide security" - such as by registering a mortgage bond over the guardian's property. Often the guardian is unable to provide security in which case the monies must be paid over to the Guardian's Fund, administered by the Master of the High Court. Application would have to be made to the Fund for the payment of interest to the child. Your Will would usually waive this requirement for security or provide for the appointment of trustees to administer your minor child's inheritance.

4. You lose control over the appointment of a suitable person as your minor child's guardian - if parents die together, leaving young children behind, a Will would normally provide for the appointment of a guardian to care for the children and administer their assets. Dying intestate results in a situation where your children may be left without a guardian until such time as a family member or friend volunteers to take on the responsibility. This may lead to conflict between prospective guardians or result in the appointment by the Court of a guardian of whom you may not have approved.

5. Your heirs may lose their inheritance in a subsequent divorce – in executing a Will you have the opportunity to direct that any inheritance you leave will not fall into the marital regime of your heir's existing or future marriage. In the absence of a Will making this stipulation, you forfeit the opportunity to provide your heirs with this valuable protection.