Medical EconomicsFinance

10 steps to increase financial security for physicians

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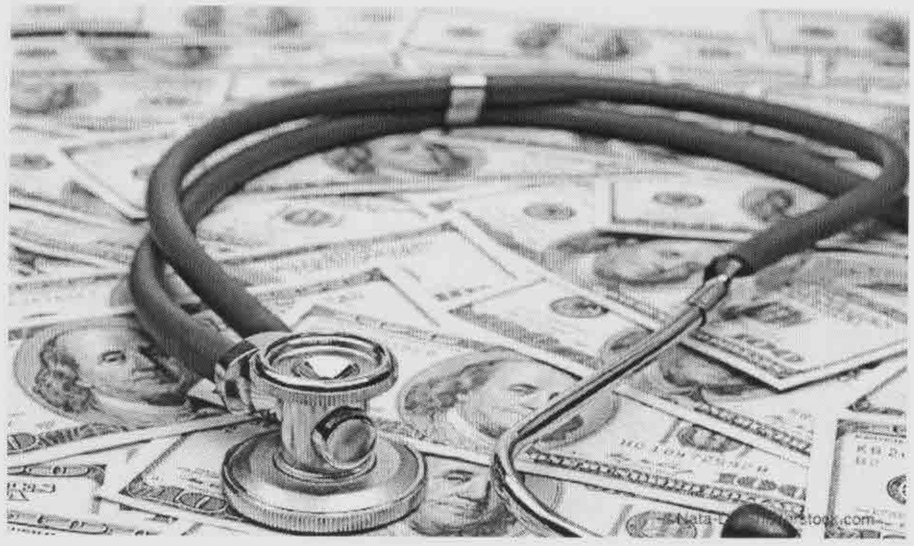
By David J. Schiller, JD



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As a contract and a tax attorney since 1984, I have reviewed many asset summaries of physicians late in their careers. Although most have historically strong incomes of $200,000 to $400,000 per year, their accumulated wealth varies tremendously. Some physicians in their 60s have a home, a small retirement plan and little else. Others have cash equivalents of $5 million or more, no debt, real estate and other assets. In my experience, this usually does not relate primarily to income differences but rather to both spending control and financial knowledge.

If you are interested in having the opportunity to eventually retire and not have to worry about finding an "early bird" special at your favorite restaurant, consider the following ten great ideas.

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10. For your children, would you rather pay astronomic tuition bills for four to eight years of college and graduate school or 16 years to 20 years that includes private school? When you have children approaching school age, choose an A+ school district and send them to public school. I promise they will still get into good colleges. Savings: $600,000 per child.

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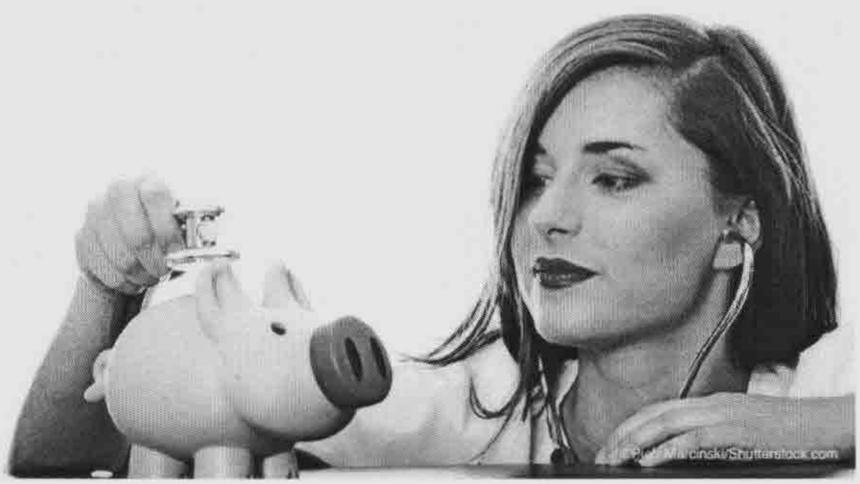
9. Immediately start funding a Roth IRA. The current limit is $5,500 per calendar year. The principal and interest will grow tax-free (not tax-deferred) over decades. At your retirement age, you will have $500,000 tax-free (invested at historic rates of growth).



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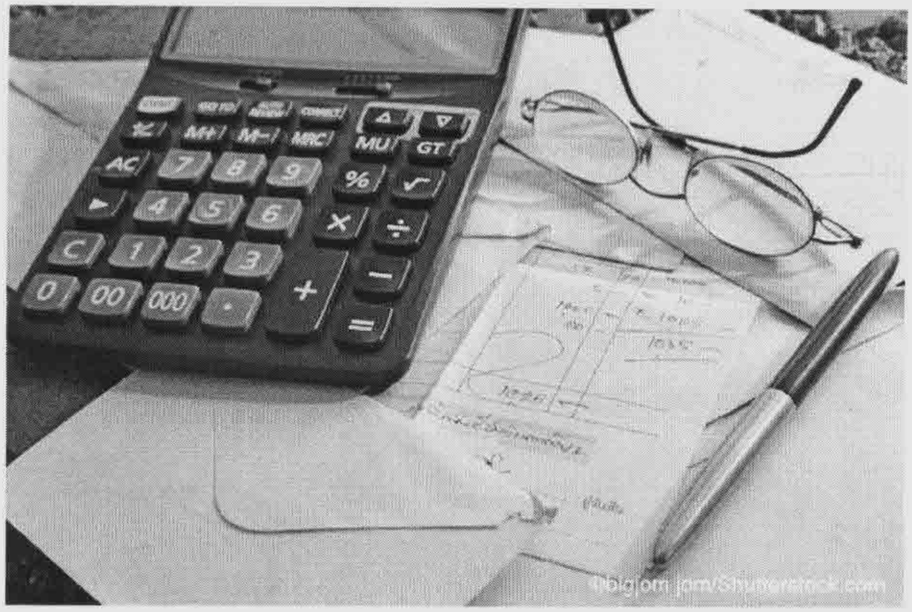
8. Contribute to your employer's Roth 401(K) or regular 401(K). Begin the first day you are eligible, at the rate of at least 5% of your compensation. By age 35, contribute no less than 10% of your compensation up to the legal maximum. In a Roth 401(K), you will have decades of tax-free accumulation. You will enjoy the benefits of employer matching contribution. Do not borrow money from the plan.

If you change jobs, move your retirement plan account into an IRA; do not cash it out. If necessary, you can usually withdraw funds to make a down payment on a home or for an emergency, but plan contributions should be viewed as "tomorrow" money. You can borrow to purchase a home and to finance your children's educations, but cannot borrow to retire.



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7. It is easier to accumulate wealth if you are debt-free. Mortgages, student loans and car payments should be minimized and eliminated as quickly as possible so that available income is available to invest both through retirement plans and on an after-tax basis. Cars should be purchased rather than leased. Leasing is an expensive way of borrowing money because you are, in effect, purchasing only the most expensive depreciating years of the car's useful life, the initial few years.

You should not have credit card debt at any time as credit card debt means you are spending money before you earn it.

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6. Interest income on your investments is taxed at ordinary income rates, perhaps 30% or more, but dividends issued from stock or stock mutual funds are taxed at lower, long-term capital gains rates. Similarly, when you sell a stock or a stock mutual fund, the appreciation is taxed at long-term capital gains rates under most circumstances. As you are able to invest, make sure that you are using tax-advantaged investment vehicles.

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5. When investing in the stock market, consider no-load mutual funds such as those offered by Vanguard, that do not require an investment adviser. (A "load" is the fee of sales commission paid out of your investment to the salesperson that sold the investment to you.) The greatest chance you have of underperforming the market relates to the expenses associated with investment, more so than the particular investments selected. Since almost all advisers underperform the market, you should consider investing on your own, minimizing costs and watching your funds grow. As a younger physician with many high-income years in front of you, a good portion of your investments should be in equities so as to enjoy their appreciation over decades. With today's miniscule bank interest rates, there is no reasonable alternative.

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4. If you or your spouse or partner has an issue with overspending, it is imperative that you develop a budget, first allocating funds to long-term savings such as a retirement plan, next to short-term savings, then to unavoidable recurring costs such as rent or mortgage, student loans, food and discretionary expenditures. The perfect time to put this in place is when you go from the salary of a resident or fellow into a full-time job and your income jumps substantially. Read the book, "The Millionaire Next Door," by Thomas Stanley and William Danko to

learn how to gain control over your spending. If you start to spend your entire salary, you will never be in a position to retire.

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3. Whether or not you currently have children, you can fund a 529 plan to enjoy tax-free growth and plan for education expenses of children or future children. If you do not have children yet, you can name yourself or a relative as the beneficiary and then change it after children are born. Trying to fund college educations out of current income is difficult and it is better to prefund education rather than to pay back student loans over many years.

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2. If you are married or have children or both, it is imperative to have a will so that your wishes are implemented upon your passing. Many tax advantages are available when bequeathing assets to your heirs that don't require complicated trusts. It is important that you maintain up-to-date wills so your affairs are in order.

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1. Your most valuable financial asset is your income stream over the coming years. Protect it with adequate private disability and life insurance policies. Policies provided by your employer typically end upon termination of employment and having a portable policy is important.

Taking these steps will help you to maximize your financial position over your work life and through retirement. The best time to get on the right track is yesterday; the second best time is today. Staying in shape financially is easier than making mistakes and then attempting to fix them.

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