Personal Finance Management for New Oncologists: Part 1

If you are just starting your practice, you're likely facing money management decisions that you've never encountered before. Your income has increased, but your student loans now have to be paid back, and chances are you've relocated and have new housing expenses and a new social circle. The choices about how to use your newfound discretionary income can be overwhelming.

This article and one to follow in the March issue of *Journal of Oncology Practice* offer some money management fundamentals, with advice for young physicians in particular.

Getting Started: From Analysis to Attitude

To find out how much discretionary income you have, and to get a handle on where your money is going, start a spending record. Keep track, even if it is just for 2 or 3 months, of how much of your paycheck is going toward essential living expenses and how you are spending your discretionary income. The goal is to identify areas to cut back on, so that you can carve out an amount that you are actually managing—applying to defined financial goals.

Keeping track of the paperwork is part of the challenge in managing finances, but a task that will pay you back. Create files—and know where they are—for all of your finance-related paperwork: loan agreements, credit card statements, bank statements, insurance policies, employment contracts, and so forth. You'll need these records when tax time rolls around, and having them accessible will put you in a good position to begin financial planning.

Using a software program to maintain and analyze your financial information can be very helpful, but it's not essential. "People who are savvy enough could use Microsoft Money—it's great if they want to and have the discipline to sit down and do it," says financial planner Mary McGrath, CPA, CFP. "But I try to stress that they don't need to micromanage—they need to see the big picture." The big picture, according to McGrath, is controlling spending so that discretionary income goes toward well-thought-out goals. McGrath, an executive vice president with Cozad Asset Management in Champagne, Illinois, has more than 20 years experience in financial planning for physicians and other professionals.

A simple spreadsheet program can be used to list and add up your financial data, create a budget, and maintain information needed for taxes and other purposes. If you are interested in doing more in-depth analyses, the two most popular software programs for money management are Intuit's Quicken (Intuit Inc, Mountain View, CA) and Microsoft Money (Microsoft Corporation, Redmond, WA).

Once you have a record of where your income is going, review the discretionary spending to see where you can reduce expenditures. Easier said than done, to be sure, but determining financial priorities and sticking with them is the key to successful money management. Establishing sound money management habits now will serve you well for a lifetime. Many financial planners report that many physicians do not regularly contribute to savings goals, despite their good income.

Young physicians have a special pitfall to avoid: trying to match the lifestyle of their older colleagues. "Focus on where you are in your own financial situation, and don't try to keep up with the Joneses," McGrath says. The big house, a boat, and the resort vacation are especially tempting when others you know have them. Remember that physicians who have been practicing for years are in a completely different financial position.

Reaching agreement with your spouse on financial priorities is also essential to successful money management. "A couple needs to come to an agreement on the big things like paying off debt and how much money to put toward the kids' education," McGrath says. "If they don't both buy into the plan, they will fail." She adds that both parties will need to make some compromises.

McGrath also recommends that both husband and wife have some agreed-on amount of "mad money" to spend as they wish, and about which neither questions the other.

First Priority: An Emergency Reserve

Financial advisers agree that the first priority for saving should be a fund to cover emergencies. Even if you have credit card balances that you would like to reduce or even pay off, experts recommend building an emergency savings fund first. It seems counterintuitive to many people to put money in savings when you could apply it to a credit card balance that carries interest charges. But money applied toward the debt is no longer available to you. A cash reserve is needed if you are unable to work or if a bill comes in that you can't pay from your monthly income. Adding it to your credit card would just worsen your debt situation.

How much should you keep in an emergency fund? A longstanding rule of thumb is to have enough to live on for 3 to 6 months, which can tide you over if you are unable work for some reason. A number of variables affect how much money you need. For example, if your spouse has an income, or if you have disability insurance and paid sick leave through your practice, a smaller savings reserve is reasonable. Be aware, though, that disability insurance payments usually do not begin for 3 to 6 months after an accident or onset of a

disabling illness. McGrath suggests keeping a minimum of around \$25,000 in an emergency fund.

Maintain your emergency fund in a money market account, so it is immediately available. Don't worry about the interest rate going up or down, McGrath advises, because the goal is to have ready access. Although money invested in a mutual fund or a stock, for example, would be available within a few days time, you might need it when it's not a good time to sell. Other investment vehicles, such as a certificate of deposit, require a minimum investment period and carry penalties for early redemption.

Save some money every month toward your emergency fund. The best way to be sure this happens is to set up an automatic payroll deduction. If your practice's payroll department can't handle this, have your bank or money market fund set up an automatic transfer each month. "Automatic deduction is the only way to be sure it gets done," says McGrath.

Eliminate Credit Card Debt

Once you have your emergency cash reserve in place, tackle the balances on your credit cards. According to McGrath, many individuals seek her advice on where they should invest, but when she reviews their financial situation she finds they are carrying credit card balances. "I tell them to eliminate the debt first," she says.

Paying off credit card bills instead of buying new things or going somewhere special is hard, no question about it. Temptations abound—upscale restaurants, a new laptop, a weekend getaway, a luxury car. And it's easy to rationalize such splurges—you've waited so long, and you work hard. McGrath is familiar with—and sympathetic toward—the mindset of physicians just starting practices. "They've been going to school forever—all they've been doing is accumulating debt, and all they want to do is buy the big house and the big car. But such spending makes it just that much longer before they can get themselves out of the hole."

Because of the high interest rates charged by credit cards, the goal is to completely eliminate credit card balances. Then, as you charge new purchases, pay off the entire balance every month. If you have more than one credit card, work first on paying off the one with the highest interest rate. If possible, transfer the balances on higher interest rate cards to a card with a lower rate.

Be wary of scams that offer debt negotiation programs. Such programs are not the same as debt management programs sometimes offered by legitimate credit counselors. A debt negotiation company may claim that it can greatly reduce your debt by negotiating partial payments, and it will charge a fee for doing so.

Student Loan Consolidation

If you have a number of student loans with varying interest rates and due dates, consider consolidating them.

Consolidation gives you just one monthly payment instead of several, and an interest rate that is locked in for the life of the loan. This makes sense if you have education loans with interest rates higher than the federally mandated rate, which is set each year on July 1. But consolidation may not be the best thing for you. If you consolidate loans and extend the repayment period, you could end up paying more total interest over time.

Assess your student loan situation to determine which of your loans are eligible for consolidation and whether it's to your advantage to do so. The Department of Education's Web site (www.loanconsolidation.ed.gov) is a good place to start. It explains your options and offers an online calculator that will show you what your interest rate and monthly payments will be for the loans you wish to consolidate.

If you and your spouse both have student loans, you are probably better off not to consolidate them into one loan. If they are consolidated, if one of you dies or becomes permanently disabled, the spouse has to pay the balance, whereas the balance for one individual's consolidated loan is forgiven in the case of death or disability. In addition, a consolidated debt cannot be divided up in the case of divorce, so both parties continue to be responsible for the entire balance.

By law, federal loans can't be consolidated with private ones, so if you have both kinds of loans and want to consolidate, you'll need two separate consolidation loans. Financial advisors suggest that you consolidate federal loans before private ones, because you can then secure a more favorable interest rate for your private loan consolidation.

As a first step, call the lender that services your private loans to find out if it offers consolidation services (some do not). Be sure to ask to speak with a loan officer in the consolidation department—individuals have sometimes been given inaccurate information because other loan officials may not be familiar with consolidation options. If the lending institution doesn't offer consolidation, you can shop around for a lender to consolidate with—most major banks offer consolidation services.

Setting Financial Goals

Once you have established an emergency reserve and paid off your credit cards, you can redirect the money you were putting toward those priorities into savings for specific purposes. How you invest your money should be determined in large part by when you plan to use it. In other words, set the goals first, then decide on the investment vehicles. For example, investment strategies will differ for the funds to be used for retirement, a bigger house, a college fund, or an annual vacation.

If you have young children, starting a college fund might be one of your first savings goals. You will need money for their education before you need funds for retirement, so starting a

college fund first makes sense. In addition, tax-exempt investment plans are available for college funds, thereby giving you some nontaxable income.

One good option for college savings is known as a section 529 plan, named after the part of the Internal Revenue Service code that regulates them. Section 529 plans are offered and regulated through states (currently all states except Tennessee, Washington, and Wyoming offer them), and each state has its own rules about the types of plans offered, how the funds may be used, contribution deadlines and limits, tax deductibility of your initial contributions, and the ability to transfer the account to another beneficiary.

McGrath points out that you do not have to use your own state's section 529 plan and recommends looking for the best section 529 plan for your goals, no matter which state sponsors it.

Life Insurance and Disability Insurance

Be sure you and your spouse both have adequate life insurance. Life insurance comes in two basic types: term policies and cash value policies. Death benefits paid to the beneficiary of either type of policy are not subject to federal income taxes.

For young physicians just starting out, McGrath suggests getting the cheapest term life insurance available to them. Term insurance is the least expensive type and pays a benefit only if you die within the policy period. The policy stays in force as long as you pay the premiums. If you don't renew the policy or if you stop paying premiums, there is no refund; the policy simply ends, and you are no longer insured. As you get older, other guidelines for buying life insurance may come into play, such as investing in an insurance policy as a way to reduce your estate taxes.

Your financial advisor or an insurance representative can help you determine how much total coverage you need. If you are working with an insurance representative, find one who is interested in serving you and your family for the long run. Using the rationale that independent agents have broader experience and may be less biased, financial experts often recommend that you use an independent agent or a broker rather than someone who works for a single insurance company. In any case, when buying insurance you should be wary of any undue pressure to buy a specific product.

Having adequate disability insurance is also very important, especially when you are young. In fact, your chance of becoming disabled at a young age is much higher than your chance of dying. A good goal for disability insurance coverage is a policy that will replace approximately 60% to 70% of your gross income.

McGrath's experience has made her a "BIG believer" in disability insurance. "Unfortunately, I've seen cases where it was needed and not enough coverage was there when the disability

occurred." Noting that disability policies have limits on coverage available, McGrath recommends that physicians get all of the disability insurance a company will give them. She acknowledges that premiums are very expensive but stresses that coverage is very important for the family if needed.

If your practice group provides disability coverage, you may still want to investigate purchasing your own policy, because you may want a policy that has a different disability definition or a higher cap on benefits. The definition of disability, which determines when you will start receiving benefits, is a very important feature of a disability policy.

If disability insurance is one of your employment benefits and you decide to purchase your own policy, you may be able to negotiate a change in your compensation arrangements with your employer. Find out if you can give up disability insurance as a fringe benefit and instead receive, as income, the amount equal to the premium that the group would have paid. Be aware, however, that premiums for individual policies are much higher than those for group policies.

Estate Planning

Many young physicians think they don't need a will because they have few assets or even a negative net worth. But if you die without a will, state law determines the distribution of your estate and can drag out the process. Most important if you are a parent, a will establishes a guardian to raise your children. For couples, each spouse has a separate will, and each will has provisions for guardianship of children if you should both die at the same time.

You should also be sure you have a living will and designate a health care power of attorney and general power of attorney. In addition, you should review the beneficiaries on your insurance policies to be sure they reflect your wishes.

For drawing up your will and related estate documents, you may want to use a lawyer who specializes in estate planning, rather than the attorney you have used to review your employment contract or shareholder agreement.

Executing a will is not a one-time act. You should review it periodically to be sure it continues to reflect your wishes as well as any relevant changes in your life, such as marriage, divorce, or birth of children.

Finally, create a single list of your financial information so that your spouse or heirs can find what they need. List important documents and where they are kept, account numbers, and the contact information for your attorney, financial advisor, and insurance agent.

Using a Personal Financial Planner

Some physicians have the time and inclination to learn about financial management and develop plans for themselves. But keeping up with changing financial markets, investment

vehicles, and tax implications is time consuming. Even though physicians can do all the research and planning themselves, most believe that their time is better spent in productive practice hours and spending time with their family.

In addition to allowing you to use your time on other things, using a professional financial planner has the following advantages over the go-it-alone approach.

- **Experience.** A planner has perspective on a realistic schedule and amount of savings to achieve your goals. Planners have been down this road before with other clients and know what works.
- **Insight Into Financial Complexities.** A planner understands how the financial moves you might consider are interrelated, especially in light of tax implications.
- **Level Headedness and Objectivity.** A financial planner can bring a voice of reason to bear when you are deciding about saving and spending priorities. He or she can also provide perspective when you may be considering impulsive decisions, such as investing in something that doesn't fit your established priorities or selling low when the market dips.
- **Mediation.** If you and your life partner have different attitudes toward money management, an outside party who knows your financial situation can help develop a budget and a plan that you both can live with. A planner's objectivity and financial expertise can be a big help in identifying differences in approaches and offering resolutions.

In choosing a financial planner, look for someone who has a number of years of experience and has worked with physicians. Ask other physicians for a referral, and schedule a face-to-face meeting before going forward. Rapport and trust are essential—a financial advisor not only knows about your debts and total money picture but also knows your personal values, perspective on life, and dreams.

Once you decide to use a planner's services, what should you expect? Your first meeting with a planner should be free of charge and should not focus on only one aspect of your finances, such as insurance or investments. If you decide to go forward, the planner will ask you to provide financial

information about your income, loans, credit cards, and insurance. McGrath says she prefers that clients simply provide the documents, such as their tax return, monthly statements, and insurance policies. She uses the documents to analyze their financial situation. "They don't have to spend a lot of time filling in a form or doing a big homework project," she says.

The planner will talk to you about your goals and recommend a financial plan tailored to meet your priorities, values, and risk tolerance. In addition to recommendations about investment strategies, the plan will include advice on related areas, such as making a will, changing your tax withholding amount, or purchasing insurance.

A financial planner should also conduct an annual review to find out what has changed in your life—a change in income, a new house, or a new baby, for example—and work with you to update your strategies as needed. A good advisor will take time to educate you and be sure you understand the rationale for recommendations.

How much will this cost? Financial planners charge either by a set fee or by commissions they earn on funds or individual stocks they invest for you. The National Association of Personal Financial Advisors supports the fee-only approach. The rationale for this recommendation is that someone who makes a commission has a conflict of interest in recommending investments.

Fee-only advisors can set fees in different ways. They may charge an annual percentage of any money you invest with them, charge a flat or hourly fee, or charge a fee that combines those two approaches. In the beginning it's likely you will be charged a flat rate or an hourly rate for their services, since you probably won't have assets to invest. For those who use a financial planner to manage their assets, a typical charge is 1% of the assets they manage that total between \$500,000 and \$1 million. Amounts below \$500,000 involve a fee of more than 1%, and the percentage decreases for amounts higher than \$1 million.

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In the next issue of Journal of Oncology Practice, Strategies for Career Success will address investment principles, types of investments, and protecting your assets.

Further Resources

Education Funds. College Savings Plans Network (www.collegesavings.org) or Saving for College (www.savingforcollege.com).

Financial Advisors. National Association of Personal Financial Advisors (www.napfa.org).

Loan Consolidation. US Department of Education: (www.loanconsolidation.ed.gov).

Savings Strategies. America Saves (www.americasaves.org).