Good Fiscal Habits to Create Financial Security

The best tools to help a doctor create financial security are good planning, hard work and time. A pediatric dentist deserves a comfortable retirement after a long career of dedicating herself to helping children battle dental disease. When good fiscal management skills start early on, debt reduction and a comfortable retirement can easily be achieved over a career of 30 years. However, many doctors graduate with very large student loans, think their ability to save for retirement is far off and do not give much thought to building up savings accounts until later in their careers. This is a huge mistake because they are not taking advantage of the powerful tool of time where one can benefit from dollar cost averaging and compound interest. Dollar cost averaging is investing a fixed amount each month regardless of the stock market's level. This reduces the risk of investing a large lump sum when the market may be high and then has a correction. Compound interest is interest added to the principal of a deposit so that the added interest also earns interest from then on. Many studies have shown that doctors who contribute monthly to savings accounts end up with significantly larger retirement accounts versus doctors who contribute a once a year lump sum or delay their saving until later in their career.

Rules of Good Fiscal Management

- **Understand money is not there to buy stuff.** Money buys freedom, security and the ability to have more choices because there is a financial cushion to fall back on. When you are in the debt reduction and building savings phase of life, look at each potential purchase and ask yourself, "Do I really NEED this? Or, would it be wiser to use those funds to further my financial goals by reducing debt or increasing savings?" Think of the total value those funds could grow to if they were invested for the next 20 plus years instead of being put into stuff that will not bring financial security.
- **Begin saving early on.** Even if it is only a small sum each month. Establish the habit of writing a check or setting up an automatic draft deposit on a monthly basis that goes directly into a saving or investment account. The monthly savings amount can be increased over time as practice profits increase.
- **Always live below your means.** Paying off debt and building savings will feel better, give peace of mind and be more rewarding versus accumulating a lot of stuff that depreciates, becomes out of date and does not contribute to your net worth. In Thomas Stanley's excellent book, "The Millionaire Next Door", he shares that most millionaire households do not have the extravagant lifestyles that most people would assume. This finding is backed up by surveys indicating how little these millionaire households have spent on such things as cars, watches, suits, and other luxury products and services.
- **Have budgets for your personal and practice expenses.** Set up a company in QuickBooks for your personal expenses so they can be analyzed each month to see if budgets are followed and expenses can be reduced to create additional savings.
- **Increase your life-style in small proportions** as your income rises so additional income can be used to reduce debt and build savings.
- **Put unexpected income into a savings account; bonuses, tax refunds, money gifts, inheritance, etc.** These funds were not planned on anyway and this is a good way to boost savings beyond your normal monthly savings plan.
- **Start a corporate retirement account as soon as financially possible if you own your own practice.** Have your CPA advise you on the type of plan that is best and when to start it.
- **Start an IRA or Roth if you do not own a practice.** An IRA or Roth can also be contributed to in addition to a corporate practice retirement plan.
- Always contribute the maximum amount each year to any retirement account, especially if you are an employee and the company will match your contributions.
- **Realize that to meet retirement needs you will also need to save money outside of your retirement accounts.** Many doctors think that if they are fully funding their corporate retirement accounts each year, they are saving enough for retirement. This will not be enough. For example, 25 years of saving $50,000 per year that grows conservatively at five percent

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each year will total $2,386,549. A widely referenced rule of thumb for retirement withdrawal is the four percent rule. Retirees who withdraw four percent of their initial retirement portfolio balance and then adjust that dollar amount for inflation each year can expect their savings to last approximately 30 years. Four percent of $2,386,549 is $95,462. I doubt that in 25 years from now, after inflation on cost of living expenses, $95,462 a year will be enough money for a couple to live comfortably even if Social Security is available. That is why it is necessary to also have a personal retirement savings account outside of the corporate retirement account. A doctor should eventually be contributing more to their personal retirement account each year (20-25 percent of their total income) than their corporate retirement account.

Mistakes We See Doctors Make

- Not having a long-term financial plan for reducing debt and saving for children's college and retirement.
- Not starting a monthly savings plan.
- Not having and monitoring a practice and personal budget.
- Not having a practice business plan that sets practice goals and monitors goals on a monthly basis; new patient total, average doctor daily production, average recare daily production, collection ratio, accounts receivable total, monthly doctor and recare days worked.
- Living beyond their means; buying too much on credit, too many toys, extravagant life-style, clothing, jewelry, services, vacations, houses.
- Thinking a strong stock market or strong practice cash flow will always go on and setting up their lifestyle accordingly. We have seen doctors go through dramatic changes in cash flow due to the following and then have trouble supporting the lifestyle they have set up:
  - Change in insurance reimbursement. Medicaid has notified doctors that their future reimbursements will be reduced anywhere from five to 20 percent in 30 days.
  - New patient numbers decrease due to more private practices and corporate dentistry moving into the doctor's area causing production to decrease.
- Take draws and not set part of the draw aside for taxes.
- Poor financial advisement results in the doctor unable to pay their estimated tax payments, pay the IRS on April 15 and fund their corporate retirement plan even though the practice had been cash flowing well. This occurs because these payments are typically large and the doctor's CPA has not adequately forecasted these future payments and advised the doctor so funds could be set aside. Unfortunately we have seen doctors have to borrow on their line of credit to make some of these payments and avoid penalties.

Create Five Separate Savings Accounts for Major Expenses

- **Federal and State Estimated Tax Payments.** Any time a draw or bonus is taken from the practice (money outside of a normal paycheck where taxes are withheld) ask your CPA how much of the total draw you should set aside to be able to pay the estimated federal and state tax payments and deposit that amount into this account. When estimated tax payments are due on April 15, July 15, September 15 and January 1, the funds will be available to pay this bill in full.
- **Federal and State Tax Payments due with the April 15 tax return**. As practice profits start to rise, a doctor will arrive at April 15, and find that there could be a substantial tax bill due even though they had paid all of their four estimated quarterly tax payments in full. It is wise to review practice profits at least quarterly with your CPA to see if additional funds will be needed to pay taxes on April 15.
- **Unexpected Large Expenses.** House down payment, auto, medical deductible, working spouse does not work for a period of time, supplement living expenses in economic downturns.
- **Children's College.** Time and compounding interest are your best friends if you start early saving for college costs. Even if your initial monthly deposits are modest when your child is born, the habit of a monthly saving deposit is established and amounts can be increased as the practice matures. It is a reasonable goal to be able to pay for college costs as they arise when a good savings plan has been in place for several years.
- **Retirement Plan Savings.** This is a tax deferred savings account within the practice corporation.
- **Personal Savings for Retirement.** Additional funds needed for retirement beyond what is set aside in the doctor's corporate retirement account. Any funds put into this account will be treated like personal income and will need the appropriate federal and state tax amounts also deposited into the tax savings account.

Setting up automatic monthly deposits into savings accounts can be the single most important financial decision a doctor can make. Watching your savings grow saves you from the anxiety of what-ifs and creates peace of mind by knowing you have financial security.

"Money should be mastered, not served."

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