

Retirement Planning and Investing: A Primer for Surgeons

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“Often when you think you’re at the end of something, you’re at the beginning of something else.”

- Fred Rogers—Mr. Roger’s Neighborhood

The journey to becoming a surgeon is often a long and arduous adventure full of hard work, sacrifice, and a large number of ramen noodles. And while the beginning stages of any physician’s career are often characterized by shoestring budgets and student loans, the earning potential for a career in medicine places physicians in a unique financial situation. This potential future financial stability, however, must be considered in the context of a person’s whole career and aspiration. A thoughtful financial strategy, set up early, can help physicians achieve these life goals and plan for events such as purchasing a house, saving for college, and eventually retirement on their own terms.

This resource aims to provide readers with a general overview of investment strategies and modalities, the terminology to help decipher the number scramble that is retirement plans, and a guide to how to get started with your own financial planning.

I. UNDERSTANDING ASSETS

An asset is any resource with an economic value that is owned or controlled by an individual that is expected to retain or provide future value. Assets can be as simple as cash holdings or as complex as the dividends earned from stock investments. Assets are generally categorized into four types:

1. **Cash-** while this category includes physical currency it also encompasses savings/checking accounts, CDs, money market accounts, and treasury bills. These types of assets are traditionally very stable in their value with little to no potential for appreciation or growth above their stated value. This asset class tends to be very liquid, meaning they are easily able to be converted to cash.
2. **Fixed Income-** these assets are investments that pay the investor a fixed interest rate of return. Traditional examples include bonds where the investor purchases a debt of a company or government and, in exchange, the investor receives regular fixed payments for the length of the bond. At the end of the bond length (bond maturity) the initial investment is returned to the investor. The rate of return is based on the risk of the investment with a lower rate of return when purchasing US government bonds and a higher rate of returns when purchasing riskier corporate bonds. The benefit of these types of assets includes capital preservation with the benefit of a stable, albeit often small income stream.

3. **Equities-** this category of an asset includes traditional investing modalities such as stocks and mutual funds. The easiest way to think of equities is a purchasing a piece of a company. By purchasing stock in a company your equity can grow in value as the value of the company grows or decrease in value if the company were to start failing. Equities come in a variety of different types with some equities being the high risk-meaning high potential for loss, but also high potential for gain versus low risk- which has a relatively stable, but less significant growth potential. Investment in equities is usually for the purpose of capital appreciating or increasing the value of your investment.
4. **Alternatives-** these assets are resources that have an economic value, but do not fall into the traditional above three classes. These include resources such as real estate, art/antiques, or gold/silver. Alternatives are also utilized for capital appreciation, but also allow for diversification of your investments.

Different asset classes are utilized for different investment purposes. The goal of capital preservation versus capital appreciation depends upon your individual financial status, life goals, and work/retirement planning.

II. COMMON RETIREMENT PLANS

Retirement plans are accounts that individuals deposit funds during their paid work years for the purposes of utilizing and withdrawing from once they retire from paid work. Retirement plans come in a variety of different types each with its own pros and cons. A review of common retirement plans is described below but is far from an exhaustive list of the various options.

1. **Employer-sponsored plans-** in the past, employers used to help provide for their employees' retirements through pensions which would pay out a certain amount of money each month after a team member retired. Employers have progressively moved away from pensions and now traditionally offer employer-sponsored retirement accounts. These accounts allow employees to set aside money for retirement with the added benefit of reducing their yearly taxable income, growing tax-deferred, and often with an employer matching up to a certain percent of your contributions.

Common plans include a **401k** and **403b** which are largely the same type of retirement accounts, varying only in the type of employer that offers them. 401k accounts are offered by for-profit organizations whereas 403b accounts are offered by non-profit organizations.

2. **Individual Retirement Accounts (IRAs)-** IRA is retirement accounts that are opened by an individual to save for life after paid work. These accounts function similarly to the 401k and 403b accounts except these accounts are not offered through one's employer. Instead, these are privately opened accounts often through a bank, investment company, or personal broker.

When discussing retirement accounts that have tax incentives, two general types of contribution strategies exist- traditional and Roth. With a traditional contribution strategy when you contribute funds each year, that amount is deducted from your total yearly taxable income. This essentially means that you do not pay taxes on the money that you contributed to the IRA. When it comes time to withdraw that money during retirement, however, you pay taxes on the money then. With a Roth IRA, you pay taxes on the money when you contribute it to the retirement account but can withdrawal it in the future without paying taxes.

There are positives and negatives to both a Roth and a traditional account. Interestingly, there may be a benefit to a Roth IRA over a traditional IRA in regard to the timing of taxation for clinical trainees. In comparison to a traditional account where one's tax rate is determined by the amount that is withdrawn, Roth IRA account contributions are post-tax and the tax paid on the eventual IRA contributions is based on the year that the money is earned. As many physicians, currently in training, have an income expectation that is significantly greater than their trainee salary and physicians in retirement are likely to keep an annual withdrawal from their IRA that is greater than their trainee salary, one's tax burden may be significantly greater upon account withdrawal than if the taxes were to be paid prior to deposit.

Importantly, all these decisions must also be made in the context of one's educational loans. For individuals in an income-based repayment plan, such as PAYE or REPAYE, monthly payments are calculated based upon your taxable income. As such contributions to a traditional IRA/401k/403b decrease your taxable income and thereby minimize student loan payments.

With employer-sponsored plans, when you leave that institution (such as moving for fellowship or starting your first attending position) you have the option to "roll over" your 401k/403b into an IRA. This essentially amounts to taking the money out of your old employer's retirement plans and putting it into a retirement account of your choosing. Some people opt to roll over these accounts because it can allow you greater control over your retirement funds and some banks/investing companies offer added benefits and perks for moving accounts. You do not have to roll over your 401k/403b when you leave your old employer, and some accounts can have benefits that may make it more desirable to leave your funds in the initial account.

Each year the IRS publishes a contribution limit which is the maximum amount of money you are legally allowed to put away for retirement into a 401k/403b account. Each account has its own set limit in addition to a total maximum limit for all your retirement accounts combined. Maximizing your contributions to these various retirement accounts allows you to reap the benefit of the tax-deferred and tax exemption status offered by these accounts. If you "max out" the yearly retirement contributions you may need to pursue alternative strategies for investment/savings plans if you wish to save above the contribution limit for retirement, but these plans often come without the tax benefits of traditional retirement savings accounts.

The benefit of designated retirement accounts such as 401ks and 403bs comes from the tax benefits offered through the IRS. These benefits are offered to help encourage individuals to save for their later years and to not tap into these savings. As a result, the IRS sets the age limit of 59 ½ as the age at which you can start withdrawing from your retirement accounts without early withdrawal penalties. It is permissible to withdraw from your retirement account early, but that comes with a 10% penalty. In addition to the 59 ½ age limit, Roth retirement accounts also require the account to have been open for at least 5 years before penalty-free withdrawals are allowed. If you decide to retire after the age of 59 ½, you are still able to continue contributing to your retirement accounts. You are also not required to take withdrawals from your retirement accounts after you retire if your financial situation affords you that flexibility. At the age of 72, however, the IRS requires you to start withdrawing a minimal amount from each of your retirement accounts termed the required minimum distribution.

III. RETIREMENT PLANNING

Planning for retirement can seem like a daunting task at first glance but creating a thoughtful plan can help set you up for long term financial stability. A solid retirement plan should help you determine your goals, perform a realistic assessment of your current and future financial situation, and establish benchmarks for tracking your progress. The quick start guide below can help you with taking the first steps of creating your own retirement plan.

1. Determine what retirement means to you- what things are you going to do during retirement? Do you want to travel? Buy a second home/relocate? Start a business? Outlining what you want your retirement to look like can help you predict what costs you will have in the future and the amount of savings you will need. It can be helpful to discuss these goals with your spouse/partner to help coordinate your planning.
2. Analyze and quantify your needs for retirement-the actual amount of money you need to retire depends upon several factors including the age at which you retire and the type of lifestyle you want to maintain after you retire. Several online calculators exist to help you create an estimate of your retirement needs based upon your desired level of lifestyle with an adjustment for yearly inflation. Retirement budgets should include funds for at least housing/living expenses, transportation, health care, food and entertainment. The amount of money need for each category is dependent upon one's individual lifestyle.
3. Uncover your shortfalls- once you have an idea of what you want your retirement to look like and how much you will need to save, the next step is to look for potential setbacks or shortcomings that might affect your ability to achieve these goals. Expenses such as an illness, a sick family member, weddings, or college costs can significantly affect your long-term savings if you lack appropriate contingency plans.

It is also important to critically assess your current and potential future financial state to see if you will be able to achieve these goals with your current financial trajectory. Do you have a large quantity of credit card debt? What about student loan costs? Accounting for these shortfalls is a crucial part of developing a comprehensive plan.

4. Create an action plan- utilizing all the planning you have completed up until this point you can start to create a financial plan to help achieve your long-term goals. Savings accounts, investment portfolios, individual retirement accounts, health savings accounts and emergency funds are all savings strategies that can be utilized to help create a stable financial plan for the present and future. Individual needs will vary based upon income, life/family situation, and future goals. Multiple books and how-to-guides have similarly been published on this very topic and can be a useful place to start. An investment/retirement planner may be a helpful resource in helping create the most effective action plan for you and your family.
5. Periodically track your progress- your financial plan is an active and ever-changing target. It is important to periodically re-assess your action plans to ensure you are still on track to achieve your financial goals. It is especially important to re-evaluate your plan whenever you make changes in your goals, experience personal financial changes, or whenever there are large shifts in the market. Staying on top of your financial plan and monitoring your progress can help make sure you are able to achieve the retirement you want.

IV. INVESTMENT STRATEGIES

What is investing? Simply put investing is the process of allocating resources/capital with the expectation of generating a profit. Investing comes in many different forms from stock or real estate purchases, business financing, or bonds. Something as simple as placing your money into a savings account, while it may not seem like an “investment,” usually has a yearly interest rate which generates a profit.

In this example, investing your capital into savings accounts is an extremely safe investment with little risk associated, but consequently little reward. The risk/reward balance is a key principle in investment strategies. The goal of investing is to capitalize on potential future growth. By putting money/resources in now, you hope that in the future your investment will retain its initial value and have in fact increased in value. This comes with a certain level of risk that your investment will decrease in value if for example a company goes bankrupt. Different investments have different risk/reward ratios, typically those with higher risk also have higher reward potential. Thinking back to our different asset classes it is possible to categorize those assets into different risk/reward groups with stable assets such as cash having low risk/low reward ratios and equities/alternatives being on the higher risk/reward end of the spectrum.

When deciding where to invest your capital it is important to assess your level of risk tolerance. Risk tolerance is the degree of variability in investment returns that you are willing to accept. If

you have low-risk tolerance or low willingness to potentially lose your investment, stable assets such as cash and bonds tend to fill that strategy. This is compared to individuals with high-risk tolerance who may have more high-risk portfolios with a larger portion of equities and alternatives. Your level of risk tolerance is something you need to assess given your own personal financial situation and can change over the course of your life. When you are younger and have longer potential working years, higher-risk portfolios can allow for greater capital appreciation with the backup of still having earning potential if those investments were to fall through. This is compared to those approaching retirement who may prefer a more conservative portfolio with a focus on capital preservation as they lack the time to build back a nest egg if their investments were to fail.

Numerous books, blogs, and videos have been published detailing various investment strategies, but care should be taken to utilize information from reliable resources. Personal wealth managers and investment bankers are some other useful resources for helping get started with investment and retirement planning. The decision of if, when, how, and where to invest should be part of a personalized plan that accounts for your own life goals, current and future financial needs, and with a clear understanding of the risks and benefits of each option.

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