Our Alternative and Real Estate Investments

Most of my portfolio is pretty boring. 60% of it is invested in stock index funds and 20% of it in low-cost bond funds. That never really changes, so there is little point in writing frequently about it. However, about twice a year I update readers on my other investments. This 20% is primarily invested in real estate investments, but the main aims of this portion of my portfolio is high returns, low correlation with stocks and bonds, and getting paid for illiquidity. Many of these investments are not available to you, but there are often similar investments that are if you are interested. Bear in mind all of these are completely optional. If your written investment plan avoids them completely, you are probably going to be just fine so long as you fund the plan adequately. Returns discussed in the post are as of February 11th, 2019.

The Vanguard REIT Index Fund

My investing policy statement dictates 5% of my portfolio be invested in this fund. I’ve owned it since November 2006. My annualized dollar-weighted returns since that time are 7.76%, dragged down significantly by 2018 when it returned -7.63%. It
is up almost 13% already in 2019. Remember that with dollar-weighted returns, in a portfolio that is rapidly increasing in size, recent returns have a much larger influence on the annualized returns than you might expect. I’m a little underweight here right now, with only 3.24% of my portfolio invested here, so that probably worked out in my favor in 2018 and against me last month.

Peer to Peer Loans

Remember these? I added these to my portfolio back in 2011 and exited (or rather, started exiting) in late 2016. I used primarily Lending Club but also Prosper. They actually treated me quite well.

- 2012: 12.65%
- 2013: 13.16%
- 2014: 11.34%
- 2015: 9.99%
- 2016: 7.09%

I decided I wanted out because I didn’t like the very concentrated platform risk and it seemed silly to be taking that kind of risk for 8-10% returns when I could invest in hard money loans backed by a forecloseable property instead. It turned out to be far more illiquid at that point than it had been years earlier when I started investing in this asset class. Nevertheless, I was able to liquidate 90%+ of it within a few months and invest it elsewhere as planned. But I still have money there that I won’t see for years. That’s not such a huge deal in my Prosper account. It was never more than a small taxable account, but just before I decided to get out, Prosper decided they weren’t going to let you sell your notes on a third party platform. So as they are paid off, I periodically transfer the money to my checking account. I currently have $107.23 in that account spread across 11 current notes and one late note. I won’t get my last dime back

The Lending Club account was more problematic. I also had a small taxable account there that actually liquidated pretty quickly. But the larger Roth IRA account was a lot harder to liquidate. I sold very few at a premium, a bunch at par, and even more at a small discount. It became obvious I wasn’t going to sell any more unless I was going to give them away, so I decided to just keep trying to sell them at par and wait for them to mature. There were two problems with this approach. The first is that to move cash out of the account requires an IRA rollover, which is a pain and comes with a $25 fee. The second was that once my balance fell below $5K, the self-directed IRA holding the assets started charging a $100 annual fee that had previously been waived/paid by Lending Club. Despite having all of my notes for sale for nearly all of the last two years, I still own 52 current ones and seven late ones, for a total of $1273.74. A $100 annual fee on a $2000 account is the equivalent of a 5% ER, so needless to say my returns the last two years have not been stellar (-5.22% in 2017 when I was selling a lot at a discount and -1.60% in 2018 when I wasn’t), but at least they’ve only been on a relatively small amount of assets. Most of the money was moved out within just a few months. I’m still trying to sell those last 59 notes, but if I can’t, I’m stuck here until October 2021 too. My overall Lending Club annualized return was not bad, 7.96%.
Partnership Office Building

I still own part of my partnership office building. The value is only assessed once a year, so no real change here. The tenant is great! The return has ranged from excellent to poor over the years. Last year it was poor due to a bunch of upgrades. 9.25% annualized overall.

Indianapolis Apartment Building

This was the one bought through RealtyMogul in 2014. It got behind on payments for a while but caught up. Over the years it has sent me $2,030 on my $10,000 investment. The next distribution is due later this month. It was targeting a 7-12% cash on cash return (and a 15% IRR). I’ve seen 4.89%. I should have a payment hit about the time this is published. They tell me the cash on cash return has been 5%, which is about right. The estimated hold was 5-7 years, so we’ll see what the overall return is in another year or two.

My Local Grocery Store

I no longer own my local grocery store. As discussed in this post, this RealtyShares investment went round trip. It called for an 18.2% IRR and I calculate my own at 17.8%. I’m pretty happy with that, even with RealtyShares on their way out of business.
Houston Apartment Building

This is one I bought through Equity Multiple just over a year ago. It offers a 10% preferred return and until recently that was exactly what I had gotten. It’s hard to come to any definitive conclusions until it goes round trip. It’s a 3-year hold so that date is still a couple of years away. They’re aiming for a 15% return. However, I just got a notice this month that demonstrates well what risk showing up looks like in this type of investment.

Over the course of the last few months, we have been working closely with the Sponsor to finalize their 2019 budget which includes a renovation schedule for the remaining units. As mentioned in previous updates [The property is in Houston where there was a hurricane], one of the difficulties that the Sponsor ran into was lack of available subcontractors to effectively work through renovations. As a protective measure, the Sponsor has continued to lease out the Property to tenants on a month-to-month basis in order to generate cash flows and meet debt service.

The plan moving forward will be to renovate 65 units over the next 9-12 months while leasing out finished units at market rates. Eight units are currently under renovation and are scheduled for completion in early March. As part of the new
plan to address labor shortage, the Sponsor has informed us that they have signed employment contracts with electricians, plumbers, and HVAC crews in addition to contracting a larger team to handle carpentry and other renovation work. The Sponsor may add 2-3 more skilled laborers over the next couple weeks to help expedite the entire process and is committed to adhere to the schedule. After many discussions with the Sponsor, we now have a concrete plan in place to complete the unit renovations.

Additionally, we have discussed cash flow distributions with the Sponsor extensively. As noted in previous updates, the initial Interest Reserves have been fully paid out at as of November. Per our Partnership Agreement, cash flow distributions to investors thereafter would be funded by available cash flows of the Property. Based on the current plan, distributions are projected to be partial with the remaining shortfall accrued until additional units are renovated and sufficient cash flows are generated. Delays in unit renovation have no doubt negatively impacted the timing of distributions to investors but all accrued amounts on Preferred Equity will be fully repaid ahead of any distributions to the Sponsor.

While the news on current distributions is disappointing, the Houston market continues to be strong and the prospects for an attractive exit remains optimistic.

As you can see, the return is now dropping below the pro-forma and I doubt it will be made up. Will there still be a positive return? Probably. Will it be 15%? Probably not. Is there anything I can do about it? Absolutely not.

**Origin III Fund**

This was my first real estate equity fund. I prefer funds to picking the properties individually. I like the professional
management, diversification and sometimes additional liquidity. This one is sure taking its time getting fully invested though. It’s been doing capital calls for 16 months now and I’m still only 63% invested. That’s fine, I’d rather they not rush it if they don’t have good deals to buy and I’ve got plenty of other places to invest the money in the meantime. Return so far is only 1.54%. The first distribution is supposed to be in about 6 months. Hopefully, we can get fully invested by then! The goal with this one is to double my money over 7 years or so. We’ll see how it goes.

Fort Worth Apartment Building (37th Parallel)

This was purchased in February 2018. It reliably makes a payment once a quarter. Cash on cash return so far is 3.84% (although that will jump up closer to 6% between now and publication of this post when the 4th quarter payment is made.) I think this one is a 10-year hold. We’ll see how it goes. So far it is at pro-forma or very slightly above.

Realty Shares Lover’s Lane

This was a $5K loan to a home flipper through RealtyShares. They took the optional extension for an additional 4 months but always paid as agreed. I made 8.69% and got all my money back last October.

RealtyShares BarTree

This was another $5K loan to a flipper through RealtyShares that also took the extension. It had always paid as agreed until January when it missed a payment for the first time. I’m looking forward to getting my principal back soon given RealtyShares’s recent issues (basically they’re finishing up their current investments and then going out of business).
This is my last RealtyShares investment. 7.24% annualized return so far. Recent notices demonstrate what risk showing up looks like in this asset class. Remember this is a one year investment beginning June 2017.

June 2018:

The sponsor reports that the property is for sale with three other apartment complexes. Several offers were received, the highest of which is $4.4MM or about $28,000 per unit. The sponsor has decided to exercise its 6-month extension to have more time to complete marketing, negotiate offers, and close the sale. The rationale is that with more time to market the property, the sponsor may close on a better offer. The properties can be purchased individually or in a portfolio. The listing price for this property is $1,306,565.

September 2018:

The property is now under contract. The sale price is $1.25MM and the sale is expected to close within 60 days. Your investment will be returned in full with accrued interest upon closing. RealtyShares will update you when the close is confirmed.

January 2019:

The sale fell through. The borrower offered this property with two others he owned in Texarkana to sell as a package. The borrower felt that a sale at a higher dollar amount would attract a wider buying audience. What they found is that a $5MM purchase price was too large for smaller buyers and too large for larger regional buyers. They are back on the market selling the three properties individually. The property is now on the market for $1.2MM. The loan has been extended until June to allow for the consummation of a sale.
RealtyShares Church’s Chicken

This one gave me my principal back in July, always paid as agreed. I made 9.76%

Fund That Flip Jay Road

This is is a $5K hard money loan through Fund That Flip and has had some issues. It made a late payment back in August, then in October filed for an extension. The rehab has been completed but they were still trying to sell the property. They missed their December payment, which was probably a bad sign. Then they finally sold the property in January and I got paid all the interest I was due plus penalties. Final return? 11.29%.

Fund That Flip Fox Lane

This $5K loan through Fund that Flip also filed an extension, but at least they’re making all their payments. One was a week late, but I’m more concerned that the project on a 1-year loan is only 48% complete after 15 months. Not looking good there. 9.27% so far. At least the late payment and loan extension fees go to the investors.
Fund That Flip 527 East

This one actually completed the project and paid back the loan at the expected time. 10.93%.

AlphaFlow

In late 2017 I got sick of picking these hard money loans myself and decided to outsource it. First stop? AlphaFlow. They basically pick the loans from the various crowdfunding companies and charge me an additional 1% for removing hassle, providing liquidity, and providing diversification. So far, so good. 7.64%. My $22K is spread over 109 notes.

Broadmark II Fund

One of my favorite investments, this is a hard money loan fund that loans to developers in Utah and Colorado. 9.57% so far. They claim returns around 11%, but that’s not what I’m calculating it out as. Part of that may be due to the Colorado taxes being withheld for me, but most of it is just the fact that the reporting comes back a month late and that’s what I use to calculate my return. They changed to REIT status recently, which should qualify this income for the 199A deduction.
Arixa Secured Fund

This is another hard money loan fund, lending in California. I calculate my return at 6.02%. That’s always about a month behind just because of the way they report it to me, but they’re only claiming a 2018 return of 7.7%. I find it interesting that most real estate investments calculate returns differently than XIRR. I guess I shouldn’t be surprised. I asked recently why their returns were lower than Broadmark’s. Fund manager Dan Frankel said this:

*It is all about the risk of their loan portfolio versus ours. Lenders can charge higher rates in states like CO and UT because these states will experience more significant value degradation (on % terms) in a down turn, compared to major job centers in coastal CA. We would charge much higher rates in those states as well.*

Whether you buy that or not, it appears to be yet another great financial reason not to live (or invest) in California I guess. 3.6% sunshine tax. Either way, I do prefer owning dozens of these loans via these funds rather than a handful of loans picked individually, and for about the same amount of management fees either way.

My Next Real Estate Investment

I mentioned this one on the podcast a couple of weeks ago, but I’ll be picking up another hard money loan fund in my portfolio in the next month or so. You are welcome to join me if you like. I’m not yet sure if it will replace AlphaFlow or Arixa eventually but for now it will just be in addition to it. The fund I will be indirectly investing into is the DLP Lending Fund. I won’t be investing directly into it because the minimum investment is a little rich for me ($500K). The fund lends primarily in Pennsylvania, New Jersey, and Florida.
While the PPM allows for a small percentage of the fund to be invested in mezzanine loans, the fund is currently 100% invested in first position real estate investment loans and plans to stay that way. The fund also uses some leverage. There is a 10% preferred return and they aim for 11%+ returns. Since they started in 2014, they have averaged 14.3% returns.

So how am I investing in it if I don’t want to put $500K in? That’s where CityVest comes in. Some of you may recall another fund I mentioned in December in connection with CityVest, one of my site’s sponsors. 40-50 of you invested in that fund, but I wasn’t one of them. CityVest was started by Alan Donenfeld after he recommended his anesthesiologist brother invest in good private real estate funds and then found out his brother, despite being an accredited investor, could not invest in them due to the high minimums. CityVest bands together groups of accredited investors like physicians into an “Access Fund” that then invests in the larger fund. The benefit is a lower minimum investment and usually another price break. The downside is another layer of fees. Here is the deal with the CityVest DLP Access Fund:

**DLP Lending Fund**

- 1% + 80/20 split after the 10% preferred return (First 10% to you, next 2% to manager, then 80/20 above that)
- $500K minimum investment
- 5% exit fee
- 90 day liquidity
- Monthly distributions
CityVest DLP Access Fund

- $500/year fee
- 0.75% annual fee
- $50,000 one-time organization fee split among all investors in the Access Fund
- $50K minimum investment
- 5% Exit fee waived
- No liquidity for 3-4 years
- 100 total investors
- Quarterly distributions

WCI Deal

- First year annual fee reduced to 0.375% from 0.75%
- $25K minimum (instead of $50K)

Now I don’t want to put $500K into this fund. I wouldn’t be able to be sufficiently diversified if I did that. But I do want to minimize the fees that come from going through CityVest. There are three ways to do that.

First, I negotiated a lower annual fee for the first year, in addition to a lower minimum ($25K instead of $50K). You have to go through the WCI links to get that. If you go straight to CityVest, you don’t get it.

Second, I want the fund to “fill,” meaning I want all 100 investor slots that its structure allows to be filled. The more people that invest, the lower my portion of that $50K
one-time fee becomes. I also want people to invest more money rather than less. If all 100 investors only invest $25K, that’s a $2.5M fund and that fee is 2%. If all 100 investors invest $100K, that’s a $10M fund and that fee is 0.5%. I think the fund will end up being about $5M honestly, so a 1% fee.

Third, I want my $500 annual fee to be as small of a percentage of my investment as possible. I can do that by investing more than the minimum $25K. Katie and I decided to invest $100K, so that fee is only 0.5% per year.

So my total fees for year one will be

- 1% DLP fee
- 0.37% CityVest annual fee
- ~1% CityVest organization fee
- 0.5% CityVest administrative fee
- Total 2.87%

My fees for years 2-4 will be the

- 1% DLP fee
- 0.75% CityVest fee
- 0.5% CityVest administrative fee
- Total 2.25%

In addition, the DLP manager will earn 20% of returns, although they will not receive any until the investor receives the 10% preferred return.

If they can manage to do what they have done the last four years, I would expect returns of around 12%. This investment will be very tax-inefficient by its nature (hard money loan interest is taxed as ordinary income- no depreciation), but the fund will be taking care of the state tax returns in Pennsylvania and New Jersey using composite returns.

If you wish to join me in this investment with $25-100K+ of your money, you may do so through [this link](#). Yes, you must be
an accredited investor. Now don’t be stupid and invest some huge percentage of your portfolio in this; diversification still matters. I only have 5% of my portfolio in real estate debt and even that is split among 4 different managers.

In case it isn’t incredibly obvious, I GET PAID IF YOU INVEST WITH CITYVEST THROUGH THE AFFILIATE LINKS ON THIS PAGE. Affiliate marketing is one of the ways this for-profit website makes money. So obviously I have a huge conflict of interest in this regard and I have no legal fiduciary duty to you. You can read more about my conflicts of interest here. You can get started investing with the link below or you can call up Alan Donenfeld at 212-593-1600 and let him know WCI sent you to get the WCI deal. If you want to learn more, there is a webinar on Tuesday and Wednesday this week at 2 pm EST.

**Invest in the CityVest DLP Access Fund Today!**

**Physician on FIRE**

Moving away from the real estate debt, let’s talk about my best investments — the WCI Network. Physician on FIRE continues to send me quarterly checks and I calculate out my ROI at an annualized 289%.

**Passive Income MD**

My best investment, however, is the king of cash flow himself. Nothing better than getting passive income from Passive Income MD. 851% annualized return there. I highly encourage you to continue to support these fine websites.
I invest in real estate in hopes of high returns, low correlation with stocks and bonds, and being paid for liquidity.

Overall, the returns on the 5% of my portfolio invested in real estate debt were 9.13% in 2018. The returns on the 10% of my portfolio invested in equity (heavily boosted by WCI Network returns) were 85%.

Most of my investing money the last few months has been going into stocks to try to rebalance the portfolio. Strong performance from real estate/alternatives combined with poor stock market performance has forced me to do that. But I’m sure I’ll be looking at more real estate investments soon. If you’re interested in real estate investing, take a look at some of my affiliate partners (More details found on this page.)

- CityVest
- CrowdStreet
What do you think? Do you invest in anything besides index funds? How have those alternatives treated you? How have you chosen to invest in real estate? Comment below!

4 Ways to Accelerate the Power of Compound Interest

[This is a guest post from Michael Episcope, co-founder of Origin Investments which provides real estate equity funds to individuals. Origin Investments has been a paid advertiser on this site, however, this is not a sponsored post.]
The secret to growing wealth is not only making wise investments but also putting earnings to work to generate even more earnings. Money grows faster over time. When interest, dividends and capital gains on investments are left to accumulate, they grow exponentially—earning interest on not only the original investments, but also the accumulated earnings.

**Calculate Compound Interest with the Rule of 72**

A useful shortcut to help calculate the rate of compounding at a given interest rate or expected investment return is the rule of 72. By taking the interest rate or the expected return and dividing it by 72, the result is the number of years it will take to double your money. Using this formula, a 9% return will double every 8 years. (72 divided by 9=8)

Even a single percentage point more in annual returns add up to big dollars when you do the math. For example, over 35 years a $1 million investment portfolio generating gains of 6% annually will be worth $7.69 million, while a 7% annual return will generate a portfolio value of $10.68 million. That’s a difference of 39%.

Albert Einstein is said to have called compounding the eighth wonder of the world. Whether or not that’s true, it’s clear
that keeping your money working at all times and making money on your money is the key to getting and staying wealthy. By making a few portfolio tweaks or managing cash more effectively, nearly every investor can find a way to generate another 1% to 2% annually on their portfolios. It requires discipline, but the steps are simple:

4 Ways to Accelerate the Power of Compounding

#1 Focus on asset classes with high expected returns

Portfolio optimization is a tool used by virtually every wealth manager to create risk-adjusted portfolios, but it comes at a cost by trading volatility for return potential. That’s because portfolio maximization doesn’t focus on maximizing long-term wealth, but rather minimizing long-term loss—For that reason, many portfolios are “over-diversified” with asset classes that are included to lower volatility.

David Swensen, CIO of Yale University’s endowment—the world’s second largest according to the New York Times, focuses the school’s investment dollars on alternative asset classes with high return potential. Very little of the Yale portfolio is in bonds or cash. Why? While bonds are a great tool to smooth the
ups and downs of a portfolio, they don’t earn significant returns. And what’s the point of having bonds in a portfolio if you have a 25-35-year investment time horizon? Over that period, odds are you will achieve the long-term historical average of any asset class. So why not invest in an asset class with a high expected return? Instead, Yale’s endowment has assets in both the public and private markets to optimize returns. To be clear, the Yale portfolio is highly diversified across various asset classes, each with the potential to generate sizable returns. It’s this strategy that has helped Swensen achieve annualized rates of return in excess of 12% over the last 30 years. Alternative investments such as real estate and venture capital played a key role in generating these returns.

#2 Scrutinize every fee

Investors pay fees directly to wealth managers or investment accounts, and indirectly to managers of the underlying assets. The fee for wealth managers today is somewhere between 0.3% and 1.0% on assets under management. To find lower management fees, consider re-negotiating or using a robo-advisor. Robo advisors such as Betterment and Wealthfront provide similar asset management services as traditional advisors but for a fraction of the cost.

Moving beyond advisory fees, pay close attention to investment vehicles and how their fees are structured. Passive investing has proven to beat active investing time and time again, but finding the lowest cost provider is essential. Are you in a Vanguard index fund paying 0.1% or a mutual fund paying 0.6%? Switching is simple and easy.

It’s often the hidden fees we don’t see that are the ones that destroy returns the most. The race to low fee or no fee solutions has forced companies like Robinhood to find other ways to fee customers. No one works for free and companies must make money so beware of these marketing tricks. Don’t
penalize a company for putting their fees up front and center. A 1% fee can sometimes be a lot less expensive than free.

#3 Manage cash appropriately

Cash is king, but too much of it can stink up a portfolio’s return potential. Cash in an investment portfolio can drag portfolio returns down substantially because it earns next to nothing. If 20% of a portfolio is in cash, then the other 80% must work even harder to achieve your portfolio return goals. Determine how much cash you need and make sure the rest is invested appropriately, even if it’s just in an overnight money market account earning 1 or 2%. If your cash is sitting in your checking or savings account, chances are that you are earning less than 0.25%.

The biggest mistake investors make when committing to closed-end funds is setting aside their commitment in cash. In many cases, it can take years for the manager to call this capital and that’s a lost opportunity. This commitment needs to stay invested until it’s called. Over the short term, you may realize some downdrafts, but the potential funding shortfall can be easily managed by maintaining a healthy cushion in your liquid portfolio. On the back end, make sure distributions are immediately invested instead of just sitting in your bank account. In the long run, managing money in this way will reap
the greatest portfolio benefits.

#4 Invest for the long-term — Set it and forget it

It’s not about timing the market but how much time you are in the market that matters. Generating a steady 7% return and managing your capital in a tax efficient manner is far better than chasing short term returns or throwing darts at the wall trying to guess the daily ups and downs of the market.

Consider this: from 1998 to 2017 the stock market generated a 7.2% annualized return. If you missed the 20 best days of those 20 years, your return would have been only 1.15%. That’s the difference between having $1,256,950 and $4,016,943. No one knows when those best 20 days will happen, which is why staying invested matters.

No portfolio grows at a steady 7%, but over the long run, the right assets managed appropriately can be optimized for a predictable expected return. The danger in optimizing a portfolio, though, is to focus on minimizing long-term loss rather than maximizing long-term wealth. Wealth managers often diversify away risk so much that they also diversify away the ability to make any real wealth. If you have a 30-year time horizon, why are you investing in bonds? Moving that money into alternatives with high return potential is a far better solution so long as you can identify the right funds.
By combining traditional assets with high potential alternatives, investors can make long-term plans that give them the best options for appreciation. An adviser may have 50 to 100 relationships but you have only one. Stay on top of your portfolio and don’t be afraid to challenge the status quo because it’s your nest egg that’s on the line. The job of the advisor is to not lose you money, but the absence of loss is not gain. Work with them to craft a plan that not only preserves your wealth but also affords you the ability to build wealth. Finding that extra 1-2% in returns is fairly easy if you follow some of the steps outlined above and can pay huge dividends down the line.

Do you agree with these recommendations for increasing investment returns? Why or why not? Comment below!

Private Real Estate Funds – Podcast #93
You may have been expecting podcast #92 this week if you are keeping track, but you will have to wait a week or two for it. Our guest, a military physician, was told at the last minute of a requirement that the military had to sign off on the podcast transcript before it went live. So hopefully that will run next week. Instead this week we are going to talk about private real estate funds. At the beginning of the episode, I give the disclaimer that alternative investments, including real estate, are 100% optional to your portfolio. You don’t have to invest in any of them in order to be financially successful. And there is an easy way to invest in real estate called the Vanguard Real Estate Investment Trust Index Fund. So with those two disclaimers, we talk about my experience investing in real estate. I invested with several crowdfunding real estate companies. When my income increased I moved on to real estate funds, that had higher minimums, and have had good success there. But I’m always looking for other funds, not only to provide diversification, but just to see people who are doing this well. The real difficulty with the funds is the relatively high minimums. I’ve negotiated another opportunity with CityVest for you to invest in a fund with a lower minimum. I share all the details in this episode for those
interested in investing in this asset class.

Podcast #93 Sponsor

This episode is sponsored by Chad Chubb of WealthKeel. Based in Philadelphia, WealthKeel is a financial planning firm that works with physicians across the country. WealthKeel specializes in crafting straightforward, actionable financial plans for Gen X & Gen Y physicians. They navigate through the increasingly complex decisions you have to make with your money, allowing you to free up time and energy to focus on your family, your work, and what you love most.

WealthKeel utilizes a simple flat-fee structure to offer both financial planning and investment management, as well as project specific hourly advice. Chad is a Certified Financial Planner® and fiduciary for physicians and their families. He has been quoted by Medical Economics, the American Medical Association, and CNBC for his work with physicians. Over the years countless WCI readers, both delegators and do-it-yoursefyers, have trusted Chad and his team at WealthKeel for ongoing financial planning and one-time plans. To learn more schedule your free Icebreaker Call or email Chad directly at chadchubb@wealthkeel.com.
Quote of the Day

Our quote of the day today comes from Morgan Housel who said, “Enough people have been bamboozled by the finance industry that a sense of, ‘if it sounds too good to be true, it probably is’ has enveloped even rational promotions of optimism.”

Real Estate

I gave the disclaimer that alternative investments, including real estate, are 100% optional. You do not have to invest in any of them in order to be financially successful. Funded adequately, investing 20% of your gross income in a boring strategy like a Vanguard target retirement or life strategy fund throughout your career will lead you to retire as a multimillionaire, especially when the use of retirement accounts is maximized. Keep that in mind. Everything going forward from this point in the podcast is totally optional as an investor.

Second, there is a very easy way to invest in real estate called the Vanguard REIT Index Fund. This fund buys up all of the publicly traded Real Estate Investment Trusts in the United States. There is a similar fund for international REITs. Like any Vanguard mutual fund, this fund offers a passive investing strategy, very low costs (0.12%), professional management, and daily liquidity. Many investors have chosen to add this fund to their portfolio because its correlation with the overall market is only moderate. It is 0.46. 0 is completely uncorrelated, that’s about what the correlation between stocks and bonds is. Correlation between the overall market and small value right now is .93. So in that respect, 0.46 really does offer some significant diversification benefit.

There is no doubt that publicly traded REITs are influenced by
the whims of the overall market place. It lost over 6% in December for instance. Sometimes, REITs get absolutely hammered. In 2008, that fund lost 78% of its value from peak to trough. This makes a lot of real estate investors nervous. The truth is their real estate values do fluctuate daily, but the volatility is somewhat hidden to them because the value of the asset isn’t marked to market daily like a publicly traded stock or mutual fund. Some real estate investors also want to be paid for illiquidity. By giving some of that up, they hope to get a little extra return with part of their portfolio. Also, since real estate is not nearly as efficient a market as stocks, they also often hope to add value through active management.

My Experience with Real Estate Investing

My experience with alternatives really began back in 2012 with Lending Club. I had good returns, about 12%, but there is nothing backing that asset. As institutional money came in, returns became lower and it seemed silly to be loaning unsecured money for 8% when I could loan it on secured assets and make at least that. Plus the shenanigans and platform risk bothered me.

So I went to crowdfunded real estate companies. I had a great experience. I got all my money back and made good returns. The
minimum investments were pretty low, from $2-20K. But it never felt very diversified and it certainly wasn’t as passive as I would like. I did this both on the equity and the debt side, 10% and 5% respectively.

In an effort to make it more passive and diversified, I tried a firm called AlphaFlow. This is technically an RIA that charges 1% a year. But I was willing to give up 1% in order to be investing in dozens of loans instead of a handful, to not have to pick them out myself, and to provide liquidity. The returns were about what I had been getting, minus the 1% fee.

Then I started making a lot more money. I was already an accredited investor, but all of a sudden the minimums on some of these real estate funds were less of a problem for me. I could come up with $50-$100K per fund. So I branched out a bit, particularly in my hard money lending. I went to a fund called Broadmark. I think I got into it for 75,000. They basically give you a 6% return on those hard money loans and then after that, you split the profits with the fund at 80, 20. You get 80, they get 20. That has been a great investment for me. Over time I have made about 10% or so a year on that and it’s been pretty steady month after month.

I also reached out to another fund put on by Arixa Capital which is a firm that does hard money loans in California. They charge 1.75% per year, which seems really high when you compare it to mutual funds. But you have to bear in mind that you’re not exactly comparing apples to apples. I ended up with returns in the 7% or so range from that.

But I’m always looking for other funds, not only to provide diversification but just to see people who are doing this well. Hard money lending is not particularly complicated. It is basically house flippers that need cash to fix up a house and then sell the house in six or 12 months. These funds are doing the same thing that was being done through the crowdfunded sites online. The developer comes to them and
says, “Hey, I need a loan for six months. The higher interest rate doesn’t bother me, that’s just a cost of doing business, but I need to close the loan quickly.” The hard money lenders can close their loan in three days or a week as long as they meet their underwriting criteria. The benefit for these funds is, yes each loan might be short term, but the fund isn’t short term. So over the long run, if you can charge these guys 10-14% interest on the loans, there is a lot of money there to be made for the investors. The difficulty is, these funds tend to have relatively high minimums.

Investing with CityVest

Alan Donenfeld with CityVest ran into this problem of high minimums to invest in these funds when he approached his brother who is an anesthesiologist. Alan told him he should probably be investing in real estate because it was a great asset class with great returns. His brother looked at the private real estate funds and told him even with a multi-million dollar portfolio he couldn’t get into these funds with million dollar minimums and still be reasonably diversified.

Alan looked into solving this problem for people who were accredited investors, meaning they had an income of $200,000 single, or $300,000 married, or investable assets of a million or more. They qualified for these investments but couldn’t come up with the minimums. CityVest forms access funds, basically putting itself as an intermediary between these big funds with high minimums and the individual accredited investors. By putting themselves in there and forming this access fund, they can lower the minimum investment for the investors. And sometimes negotiate a little bit better terms. Not a lot of doctors can come up with $100,000 at a time to invest in a fund like this, certainly not in the first half of their career, but a lot of docs can invest $25,000 at a time. That was the situation with the CityVest proposition I discussed on the blog last December. Lots of white coat
investors got into that fund with the lower minimum.

Now CityVest has another fund that they are forming and expect to close certainly by the end of March. This is another access fund and the fund that it will invest in is a DLP lending fund. This access fund is going to gather up money, form this fund of several million dollars and then take that money and invest into the DLP fund. It is a good opportunity to get into this sort of asset class. DLP has an excellent track record. It is not that long, they only started in the last quarter of 2014. But their records are very good. It is up over 14% what they have given to their investors so far, doing these hard money loans. There is lots of pressure in this space and so it wouldn’t surprise me if the returns were a little bit lower going forward from here. But this fund does well. It has done well in the past, and every expectation is that it will continue to do well going forward.

Now, this particular fund, the DLP fund is basically an evergreen fund. It is not a fund with a stop date. But the access fund to be formed by CityVest is. The plan is for this fund to run three or maybe four years. It could possibly be extended another year if all the investors agreed to do it. But mostly this is going to be a three to four year investment. There is not going to be any liquidity in those three to four years. You can’t get your money out if you need it. But over that time period, the expectation is that it will provide nice solid returns and exposure to this asset class of hard money lending.
If you go to DLP directly, you have to have a quarter million dollars to invest in the fund. That is a big hurdle to get over for a doctor, especially if you want to have any sort of diversified portfolio. I mean, I only put 5% of my entire portfolio into hard money loans and so if I want to have three or four different funds out of that 5%, well, that takes a very large portfolio to put $250,000 in a single fund.

DLP charges 1% a year to the investors and they charge when you exit the fund, a 5% fee. It is kind of like a back load that way but I think the idea is to incentivize you to leave your money there long term rather than jumping in and out.

So the proposition here from CityVest is that they will put together an access fund that allows up to 100 investors to invest with a minimum of $50,000 instead of $250,000. They also negotiated so that the 5% fee to exit DLP won’t exist for those who come through their access fund.

Of course, anytime you put somebody else in there, there’s going to be some additional fees. CityVest charges three fees. The first one is a one time fee that is spread over all of the investors in the fund. This is a $50,000 fee to basically set up the fund. So depending on how much money is invested in the fund, it depends on how much of a fee that really is. If $5 million gets invested, that’s about 1%. If $10 million gets invested, that’s about .5%.
The second fee is charged each individual investor, it’s $500 a year. That is to cover the costs of running the fund. That works out to be about 2% a year, if you invest $25,000, or if you invest $50,000, that’s about 1% a year, if you invest $100,000 it’s .5% a year. So how high that fee is depends on how much you invest.

Then the last fee is .75% a year paid to CityVest. In exchange for those fees, they give you a lower minimum and they manage to get that 5% exit fee waived for you. That is the proposition CityVest is making.

They came to me looking for more investors. If I refer doctors to them, they will pay me out of the fees they earn from the doctors. Typically with all of my affiliate deals I try to negotiate a good deal for WCI readers and listeners. So with this affiliate deal I wanted value to be added for the investor at each step. If you decide to invest with CityVest and go through the links on the site, here is what I’ve negotiated for you.

1. The minimum investment has been lowered from $50,000 to $25,000 for you.
2. The 0.75% annual fee for the first year will be cut in half.

That is the incentive for you to come through my links rather than go directly to CityVest to invest in the fund. Even after those fees, if this fund makes the 14 and a half percent it has been making, you’re still going to be making 10-12%. It is an excellent return for a hard money lending fund.

The DLP fund lends primarily in Pennsylvania, Florida, and a little bit in New Jersey. The type of houses they are lending money for are a little bit C and B class houses rather than A class houses, cheaper houses basically that allows them to charge a little bit more.

I expect I’m going to invest in this deal as well. I haven’t
decided how much I’m going to put in, obviously, the minimum will be 25,000, but I suspect I’m probably going to be closer to the 50 to $100,000 level just because I want to minimize those fees. That $500 per investor fee, is much lower as a percentage of the return if you invest 100,000 verses 25,000. Also, the incentive of course, is to get as many investors in the fund as possible. I don’t think we’re going to have trouble getting the maximum 100 in there but to have each of those 100 invest as much as possible because the more invested in the fund, the more that initial $50,000 fee is spread out over and lowers that fee relative to the entire investment.

If you would like to join me on this investment or learn more about it, go to CityVest and talk to Alan Donenfeld. Go over the paperwork and ask him any questions you want to about the deal. I’ll be talking about it a little bit more on social media, maybe even on the blog a little bit in the coming weeks, but that’s basically the explanation of the deal. Make sure if you want that special deal to be able to only invest 25,000 and to get half of your first year’s fee waived, you let them know you came from White Coat Investor.

Listener Questions

A Windfall of Money

One listener’s large practice was purchased by a private equity group. He wondered what to do with money from a one time deal like that.

The IRS is going to treat that money as income to you, you have to pay taxes on it in that year. But anytime you make money, it all really goes into the same pot, no matter where the money came from. Whether it came from your investments, your spouse’s income, your income, inheritance, it is all the same. It is just a common behavioral mistake that people make to treat it as some separate amount, just because you had
this windfall coming in, you have to do something different with it and that is not necessarily the case.

Hopefully, everybody listening to this podcast will get some sort of a windfall during the course of their life. You don’t know how much it’s going to be, you don’t know when it’s going to come but chances are, you’re going to receive something that maybe you weren’t expecting. And that’s really my definition of a windfall. But there is really three categories of windfalls:

1. The first one is the one I call spare cash. This is money you weren’t expecting. I would just take that money and kind of fold it into my existing financial plan, whether that is paying off student loans, paying down a mortgage, or maxing out retirement accounts. I just take that money and divide it among my goals in whatever manner I see fit, just like any other money you made, like your monthly paycheck.

2. The second category is enough money to make you financially independent, enough to change your life in a significant way. This is the amount that this doc was talking about in the question. The best thing to do upon getting that level of money, is probably nothing. Do nothing for a few months, or maybe even a year, give it some time and really think about what you’re going to do with your life. If you’re ready to retire already, go ahead and do so. If you want to get out of medicine, and do something else, you can do that too. If you love what you’re doing, maybe you put a chunk toward retirement, give some away and you spend some.

3. The third category is ridiculous money, like lottery winnings, which if you invest it wisely that is more money than you could ever spend given your current lifestyle. At this point, you’re going to need to engage in some pretty serious estate planning. You have a real opportunity to make a change in your community
and in the world. So this is a responsibility that you can’t take lightly. Consider annuitizing some of the money. You hear about all these lottery winners that go broke. You can’t go broke if you ended up annuitizing it such that it’s going to pay you out a certain amount every month from now until the day you die. It is also a great time to get some solid unbiased advice at a fair hourly rate from a CPA and an attorney about estate planning and asset protection. Put a big chunk of it into a safe investment. You no longer need to take as much risk.

It makes me think about what Andrew Tobias recommended in The Only Investment Guide You’ll Ever Need. Here is what he said you should do if you win a million dollars,

“Go out for a very nice dinner, put about one year of normal living expense someplace liquid like a bank or money market fund, and then put roughly equal sums into US Treasury securities, maturing in one, two, three and four years. Then put the bulk of the remaining money into stock index fund split between US and foreign investments. Buy a bigger house if you want one, but not so big that the cost of carrying it will strain you in any way. Maybe even consider buying a small rental property but don’t buy a boat. Make sure your will is in order and then relax and forget the whole thing.”

I agree. I think it is important to spend some of it. Don’t go crazy, buying some massive yacht or something, but spend a little bit of the money. And then give some of it away, maybe some to your family but mostly to real charities that are going to do some good in the world. I think that helps you keep money in the proper place in your life. And of course, remember that one of the benefits of having enough money is that you don’t have to maximize everything out. You can use this to worry less about money because you have more now, whether that comes from winning the lottery or selling your
practice. Bear in mind one difference with selling your practice, particularly to some of these corporate management groups, is that it often comes with a lower future income. You’re trading a lump sum now for a lower income later. Keep that in mind, if you’re going to be making less money going forward, you have to plan your lifestyle going forward on less money and put a lot of the windfall toward retirement.

**Becoming a Stay at Home Parent**

The wife of a pediatric anesthesiologist coming out of fellowship asked what are some of the things that they should be thinking about and considering to see if they can afford for her to quit her job and become a stay at home mom? He is going for PSLF in five years and they have two kids with a full-time nanny.

I think this is actually a really common concern, particularly in the traditional scenario where the guy is the doctor. He has been plugging through medical school, residency, and fellowship being supported by his wife, maybe with or without children.

This doctor is going from a fellow salary to an attending pediatric anesthesiologist salary. There is no doubt in my mind that if they keep their lifestyle under control, she can certainly quit, walk away and never work again. He’s going to have enough income to take care of business, to save up enough for retirement, to pay off any debt, and to pay for the house.

Here are a few things to consider though.

1. Your income is not going to be as high as it would be if you continue to work. It is going to be a little bit slower to reach your financial goals. But the income drop might not be all that much, depending on how much she is making. They will no longer need to pay for the nanny and pay less in taxes.
2. If you are no longer working, you are going to probably want to have a little more life and disability insurance on the breadwinner. And some life insurance on the person who is being a stay at home parent because what they’re doing has real value and you can calculate the economic value of it by looking at what a nanny and housekeeper costs and additional meals out.

3. The most important long term issue here is the effect on her career. When you take significant time out of the workplace, chances are your long term earnings are going to be lower and it will be harder to get back into the workplace. You will probably not be as far along in your career as somebody who spent more time in that career rather than taking time off to raise a family and it might be impossible to get employed at all. If you’re sure you’ll never go back to work, no big deal. If you think you might, you may want to look into part-time work, to keep your skills up.

Teaching Children to be Financially Literate and Charitable

One listener asked for advice on how to teach children to be financially literate, unspoiled, and charitable. A tall order! It is difficult.

I think the financially literate part is the easy part. It is relatively easy to teach your kids about money once you understand it yourself. We start very young. I make my kids listen to Dave Ramsey on the radio sometimes when we’re driving around in the evening to their activities. They all scream and cry about it. But in the end, some of those lessons are being absorbed and they’re learning to pay attention to finances. They’re learning about the dangers of debt. You just have to talk to your kids about money. You would be surprised, it is not that complicated. A lot of it can be learned at relatively young ages. You can even give them books written
specifically for kids.

All of my kids have had some sort of entrepreneurial pursuit, it might be a lemonade stand or shoveling driveways for somebody else. You also have opportunities at times when they’re trying to raise money for something to have them earn a certain percentage of it themselves. For example, in June, Whitney and I are going to Honduras on a medical mission. She wanted to go along and I told her she had to raise a certain amount of the money to be able to go. She is coming up with all kinds of ways to raise money. I think it is good to teach them a little bit about entrepreneurship that way.

The other two questions, unspoiled and charitable, are a lot more difficult. Let’s take the charitable one first. We give away a lot of money and we want to pass that value on to our children. Once a year we have a family meeting and decide what charities we’re going to support with our money that year. Each person in the family gets an equal say. We go around and battle it out. You have to argue for your favorite charity. I wasn’t able to talk anybody else in the family into donating to the access fund this year, which is a charity that basically helps keep climbing areas open. But we ended up donating to other charities instead.

I think actually involving the children in the family finances in a way that’s appropriate is also a great way to teach them to be charitable. Not only money though, also with time. You can take them out and do service projects and those sorts of things with them.

It also helps, particularly when traveling, to point out that not everyone has the advantages and opportunities that they have, which kind of segues us into the unspoiled section. This is the big challenge I think when you start making decent money, particularly way more money than either of you grew up with. I don’t think I have all the answers on this one for sure. But I think some things that you can do are to limit
what they have. Just because you can afford to send them to school in a Range Rover doesn’t mean you should. Just because you can afford to buy them a $6,000 purse doesn’t mean you should, just because you can afford an iPhone, maybe they should have a flip phone until they reach a certain age.

Artificially limiting how much money they see in their lifestyle is beneficial to them. It also helps to talk to them about the times in your life when you really didn’t have that much money. I’m constantly reminding my kids that when they turn 18 and get their own car and their own house and their own job that they can do whatever they want and until then they have to follow my rules. That is kind of a constant reminder to them that at a certain point in their life, they’re going to be responsible for themselves and have to live on their own income.

I think it’s also important to make sure you don’t give them too much money, particularly earlier on in life to ruin them. I mean, most of us make enough money that we can truly ruin our kids and so I think you have to be really careful how much and how you pass that money on to them. And hopefully, as they prove that they can use it responsibly you can give them a little bit more.

**Term Life Insurance Companies**

“You always speak of buying the cheapest term life insurance policy one can get at places like term4sale.com. But when I purchased my own policy I worried a lot about the financial health of the insurance company, especially when one buys a term of 20 plus years. Should a young doctor worry about getting a policy from financially sound companies only, even if they cost a bit more? After all, if something were to happen, you’d want them to actually pay out.”

How much does the strength of the insurance company matter
when it comes to term life insurance? And I think it matters. I don’t think it matters as much as a lot of insurance agents think it matters, but it’s worth looking at. At Term4Sale companies are rated A++, A+, A, A-, those are basically superiors, superior, excellent, excellent. The default on the site is that they only show you companies that are excellent and up.

I ran my numbers on the site recently and the cheapest company was still rated an A. I don’t think this is really a big issue in practicality as long as you’re not going to go to a D company or an F company or probably even a B company. But is it worth dropping down below A plus plus to save 100 bucks a year? I think it probably is. I’d be comfortable with anything that’s rated A or higher and wouldn’t think twice about it. But if you’re really worried about it, pay another hundred bucks a year and get one of the very top rated companies.

Financial Conflicts of Interest in Medicine

I received some feedback from Podcast 85 where I interviewed a young periodontist.

“I was surprised to hear you say that medicine is more insulated from financial conflicts of interest because of the opaqueness of insurance reimbursement. Personally, I feel like I am wrestling with a devil on my shoulder everyday with regards to conflicts of interest. I’m an academic vascular surgeon and I am on a contract that is heavily dependent on RVU generation, and this seems to be the norm in many academic/employed contracts. When I do a lower extremity angiogram, a diagnostic procedure reimburses 4.5 rvus, this increases by 100% if I do an angioplasty and 150% if I do an atherectomy. To make matters worse, there is little time difference in any of the above, and murky data to guide therapeutic modality choice. I’m constantly weighing evidence
based medicine and best practices against that little voice telling you to earn more. I can’t imagine I’m the only one else out there with this feeling, in fact I’ve heard docs joke “Dr. So and So doesn’t participate in non-RVU generating activities”. I would love to hear more discussion about this because I think these sorts of production contracts are becoming so ubiquitous.”

Certainly, there are ways in which you can have conflicts of interest in medicine without a doubt. I think this surgeon describes about as bad as they get. For example, if you are on a salary, just a flat salary, say you’re a military doc, there is basically no conflict of interest there whatsoever. In my group, it is not completely eat what you kill, but we are the business owners. At the end of the day, we split up what’s left and divide it by how many shifts you worked in that month.

That insulates you a little bit from the day to day decisions. Yes, you know that if you do things that bill more, you’re going to make more money. But since the group has 18 docs in it, every little decision you make, you’re really only getting 1/18th of the difference in that additional money that comes in from making a decision one way or another. I think the conflict of interest there is much, much smaller and much easier to resist, than if you are 100% based on RVU compensation. I think a minority of doctors are 100% RVU based. So compared to a lot of other professions, your conflicts of interest are much smaller. Are they invisible? Obviously not. And this doc has given a great example of when they are not.

**Single Stock Holders in Taxable Account**

Also, I received some feedback from Podcast 86, regarding legacy holdings in taxable accounts.
“There is another way to diversify a single stock holding without selling, donating, or gifting the shares. It involves using an exchange fund. It’s relatively unknown among most investors and typically requires a significant, single stock holding ($500,000+), but exchange funds allow you to contribute your single stock into a pool of other stocks formed by the exchange fund and then when you withdraw your capital, your single stock holding converts into a basket of diversified stocks (and often some real estate, by law) from the pool without triggering capital gains taxes. Obviously, there are fees paid to the exchange fund that make the magic happen.”

He says Eaton Vance provides one of these exchange funds. So this is another way to achieving diversification with the same amount of capital gains. So this is one other option if you’re trying to get rid of a very concentrated holding and diversify your portfolio a bit.

Ending

Thank you for the feedback. This is a great community to find answers to your financial questions. Ask in the WCI Forum or in the WCI Facebook group. Or if you want to have your questions answered on the podcast go record them here!

If you are interested in investing in the CityVest access fund you can get more information at CityVest.

Full Transcription

This is the White Coat Investor podcast where we help those who wear the white coat get a fair shake on Wall Street. We’ve been helping doctors and other high income professionals stop doing dumb things with their money since 2011. Here’s your host, Dr. Jim Dahle.
Welcome to White Coat Investor podcast number 93 Private Real Estate Funds. This episode is sponsored by Chad Chubb of WealthKeel based in Philadelphia. WealthKeel is a financial planning firm that works with physicians across the country. WealthKeel specializes in crafting straightforward, actionable financial plans for Generation X and Generation Y physicians.

They navigate through the increasingly complex decisions you have to make with your money, allowing you to free up time and energy to focus on your family, your work and what you love most. To learn more and to schedule your FREE icebreaker session, call 267-590-9533 or visit wealthkeel.com/wci or email Chad directly at Chadchubb@wealthkeel.com. Thank you for what you do. I know your daily work is not easy, that’s why you had to train for it for so long. I was called to the floor from the ER for a code the other day, it wasn’t actually a code, they just needed some assistance.

It turned out one of the patients had pulled out his dialysis catheter and bled all over the place. It was pretty impressive, the amount of blood that was underneath him once we rolled him up, which certainly explained why his blood pressure was 60 over 30. Luckily, the nurse had stopped the bleeding with some direct pressure and all the patient needed was some blood which we promptly gave him. And his blood pressure, as you might imagine, became much more normal. But even those little things you realize are life saving
interventions that we do all of the time. And it really does make a difference in people’s lives. So thank you for what you do if nobody else is thanking you. Hopefully, you’re at least getting it from me.

I know this is podcast number 93 and you might have been expecting podcast 92 this week. We will be getting the 92 here in the next week or two, it’s actually all recorded and ready to go. But it turned out our guest, who is a military physician actually had a requirement that the military had to sign off on the podcast transcript before it went live. So we’d give them another week or two to get that done in order to comply with their demands. We want to thank all of you in the military for your service and recognize that there are often a lot of additional red tape issues with doing that.

Thank you to those of you who are leaving us questions at speakpipe.com/whitecoatinvestor. We’re getting more and more of those, in fact, it’s not going to be very long before those are probably the only questions we’re going to do on the podcast. And you won’t be able to just email me or tweet me something and get it on the podcast. I think we’ve got 10 or 12 now in the queue, and since we only do a handful of them every episode, it probably at this rate are going to be most of the questions we do. Be sure also that you’ve checked out the White Coat Investor network blogs.

This includes Passive Income MD, the blog written by Peter Kim who lives in California in a relatively high cost of living area. And it really focuses on boosting the income of physicians and increasing their passive income. He talks about lots of things, big focus on real estate there, but other kind of side gigs as well as other ways to really boost your income, great blog. The other one is Physician on FIRE. This one is written by Leif Dahleen also an anesthesiologist like Peter, but one who is probably going to be retired here within a few months.
He’s based out of the great White North just about, he’s up in Minnesota suffering through a terribly cold winter it sounds like. But he writes his blog all about FIRE financial independence and retire early. And it is a great resource for those who are ready to become financially independent particularly if you’re interested in getting out of medicine altogether. Also, if you haven’t followed us on Instagram and Pinterest, that’s our new thing. We had actually a fantastic month last month. I think our number of Pinterest followers went up by like 50% in a single month. So there’s still time to get in on the ground floor there.

Katie and I had an interesting day, this last month of January. We went down to Vegas one morning, we booked flights and went down there. And they actually picked us up at the airport in a limo. And drove us around from casino to casino in a limo while we checked out the various conference space available in Vegas for our White Coat Investor Con 20. We’re looking forward to this, it’s going to be in March 2020 still trying to decide exactly which hotel we’re going to have it in as well as which week it’s going to be. The first week or the second week of that month, but really looking forward to that. It turns out if you tell them you’re bringing a 600 person party to Las Vegas for three or four days, they’ll pick you up in a limo and drive you around as well.

Our quote of the day today comes from Morgan Housel who said, “Enough people have been bamboozled by the finance industry that a sense of, ‘if it sounds too good to be true, it probably is’ has enveloped even rational promotions of optimism.”

Okay, before we get into today’s questions from readers, I want to talk for a few minutes about real estate in general and private real estate funds in particular. First though, a bit of a disclaimer, alternative investments including real estate, are 100% optional to your portfolio. You don’t have to invest in any of them in order to be financially successful.
Funded adequately, investing 20% of your gross income into a boring strategy, like a Vanguard Target Retirement Fund or a Life Strategy Fund will lead you to retire as a multimillionaire, on a typical physician income, especially when you’re maximizing the use of retirement accounts. So keep that in mind. Everything going forward from this point in the podcast is totally optional as an investor. Second, there’s a really easy way to invest in real estate called the Vanguard REIT or Real Estate Investment Trust Index Fund.

This fund buys up all of the publicly traded, real estate investment trusts in the United States, this buys them all. Basically follows and tracks the index of them. There’s a similar fund at Vanguard for international REITs as well. And like any Vanguard mutual fund, this fund offers a passive investing strategy, very low costs about 12 basis points a year, professional management and daily liquidity. And many investors have chosen to add that fund to their portfolio because its correlation with the overall market is only moderate. If you actually look at the correlation the day I recorded the podcast, it was .46.

So one is perfect correlation, zero is no correlation whatsoever, minus one is negative correlation. The correlation between the total stock market and the Vanguard REIT index fund is .46. It’s not uncorrelated completely but it’s significantly less than most stock investments. Obviously, it’s not as uncorrelated as stocks and bonds. The correlation between those two is like .01. I mean, they’re almost completely uncorrelated. But there’s definitely some diversification benefit there with the REIT index fund. In fact, a lot more than a lot of other stock asset classes that you might invest in.

For example, I checked today what the correlation is between the total stock market and the small value index fund. And it was point nine three so much, much higher than the .46, you get out of the REIT index fund. However, there is no doubt...
that publicly traded REITs are influenced by the whims of the overall marketplace. In December, for instance, the REIT index fund lost 6%. When the market goes down, those do go down even with no seeming change in the real estate market. And sometimes REITs get absolutely hammered, in 2008 that Vanguard REIT index fund and I know because I owned it, lost 78% of its value from the peak to the trough.

And that makes a lot of investors including real estate investors nervous. The truth is, real estate does fluctuate in value daily. But the volatility is somewhat hidden to the investors because the value of the asset isn’t to market daily, like a publicly traded stock or mutual fund. Also, one reason why people may opt to invest in something besides publicly traded REITs, is because they want to be paid for being illiquid. There is a premium for being willing to give up your liquidity and they want to make that with some of their portfolio, that would provide a little bit of extra return to the investment.

Also, because real estate is not nearly as efficient as the stock market, a lot of people hope to add some value, add some return to their investment through smart active management. My experience with alternative investing really began back in 2012, with peer to peer lending. These are loans that were made to people, they basically came in, they borrowed money from their peers, from these companies like Prosper and Lending Club and they could use it for whatever they wanted. A lot of times it was to pay off their credit card debt. They had credit card debt at 30%, they get alone of 15%. Well, it made a lot of sense to take it.

And the idea was that the investor would then make a very good return. So a lot of these notes that you could buy through Lending Club would have a yield of 20% or 22%. And you know some of them were going to default, but you expect that even with the defaults, you could still get pretty decent return. And for years I had a pretty good return it was about 12% a
year but that gradually came down. And part of that was, that a lot of institutional money came into that asset class and really was able to get the really sweet deals out of it, leaving the individual investor kind of pick it at what was left.

And so as my returns decreased to maybe 8% a year, I started looking around going, why would I loan money to people, that’s totally unsecured just to make 8%, when I can go make hard money loans, that’s backed by a real live piece of real estate and make eight, nine, 10, 12%? It just didn’t make much sense to be doing that. And so I basically exited from that asset class, those peer to peer loans. It actually took a while, in fact, technically I’m not even out yet it’s terribly illiquid some of them. There was a way to sell some notes at Lending Club but the demand for them wasn’t terribly high. And so I’ve still got a few of them maybe $1500 worth that I still haven’t exited. And then I’ll probably be holding on for another two or three years.

Plus, there were some shenanigans at Lending Club, their CEO was doing some things you shouldn’t have been doing and it just got to the point where I didn’t like the platform risk and decided if I’m going to be lending money, I might as well get it backed by an asset. I kind of looked at crowdfunded real estate. And both on the equity side and on the debt side and the benefit there, when you go to these companies like Realty Shares and Realty Mogul and Peer Street et cetera, is that you could get into these loans for a relatively small minimum. Maybe it was $2,000 maybe it was 10 or 20,000 maybe at the most, but it was rare I had to put up much more than that. And so on a typical physician income, you could actually do that and get some diversification. You weren’t putting everything into one little loan.

But it never felt very diversified and it never felt very passive. It certainly wasn’t as passive as I would like. I’m spending far too much time, seeing patients and running White
Coat Investor, I don’t have time to be spending hours combing through all these sites trying to decide which house flipper to lend money to and which one not to. And so I started looking a little bit more toward the real estate funds, that would take care of that issue for me. My portfolio as you may recall, is about 60% stocks, 20% bonds and 20% real estate. Of that real estate segment of 5% is in publicly traded REITs, 10% is an equity deals and 5% is in debt side deals. And so as I started looking toward those funds that would take care of this diversification for me and the hassle as well as provide a little bit of liquidity in many cases, I have just gradually moved in that direction.

And part of what facilitated that for me was I just had more money, a white coat investor become more successful in our income and gone up. And all of a sudden the minimums on these funds that might be 50 or 75 or 100,000 or even more just became something that I could actually handle. Whereas, before when I was most in a physician income, I couldn’t really handle that. It was too much for me to come up with, 50 or $100,000 at a time to get into these investments. In an effort to make my investing in these hard money loans, a little bit more diversified and more passive. I first tried a firm called Alpha Flow, and that’s technically a registered investment advisor, they charge 1% a year.

But I was willing to give up 1% in order to be invested in dozens of loans instead of a handful and do not have to pick them out myself and to provide some liquidity on these loans. The returns were about what I’d been getting minus the 1% fee. So this worked out to be something in the 7% range, I think. I had to be an accredited investor already to get into these investments. But once the minimums on those funds became less of an issue for me, I branched out a bit particularly with these hard money loans. I went to a fund called Broadmark. And Broadmark, they have a fund that their first one was up in the Seattle area. Their second one is actually in the Utah and the
Colorado area and that’s the one I ended up investing in. I think I got into it for 75,000. I think their minimum is usually 100,000 but the fact that I had a blog cut me a little bit of a break. But they basically give you a 6% return on those hard money loans and then after that, you split the profits with the fund at 80, 20. You get 80, they get 20. And so that’s been a great investment for me. Over time I have made about 10% or so a year on that and it’s been pretty steady month after month, so that’s been a good investment for me. I also reached out to another fund put on by Arixa Capital which is a firm that does hard money loans in California.

They charge 1.75% per year, which seems really high when you compare it to mutual funds. But you got to bear in mind that you’re not exactly comparing apples to apples there. But they lend primarily in California and it turns out that the California market is a quite a bit more competitive. And you really can’t get quite as high of a yield there as you could in Utah and Colorado, for instance. And so they have both unleveraged fund and leverage fund, I invested in the unleveraged one. And I think again, I ended up with returns in the 7% or so range from that. But I’m always looking for other funds not only to provide diversification, but just to see people who are doing this well.

I mean, hard money lending is not particularly complicated, right? It’s basically house flippers that need cash to fix up a house and then sell the house in six or 12 months. I mean, it’s the same thing that was being done through these crowdfunded sites online. It’s being done by these funds. The developer comes to them and says, “Hey, I need a loan for six months. The higher interest rate doesn’t bother me, that’s just a cost of doing business, but I need to close the loan quickly.” And so they would come to these hard money lenders basically who can close their loan in three days or a week as long as they meet their underwriting criteria. But they weren’t as strict as the bank. They didn’t make you
wait six weeks to get your money. And so that is the proposition here, is these home flippers are coming to these hard money lenders in order to get short term money. But the benefit for these funds is yes, each loan might be short term, but the fund isn’t short term. So over the long run, if you can charge these guys 10 or 12 or 14% interest on the loans, there’s a lot of money there to be made for the investors. The difficulty is, these funds tend to have relatively high minimums.

Even the two I mentioned, I think the minimums are in the 75 to $100,000 range. And a lot of these funds have minimums that might be $250,000 or a million dollars. And this was the dilemma that Alan Donenfeld with CityVest ran into. His brother is an anesthesiologist and Alan told them, “I think you probably have to been investing in real estate. I think it’s the best asset class, I think it has great returns et cetera.” And so his brother went and looked at these private real estate funds and then comes back to him and says, “I did pretty well in aesthesia, I got a multi million dollar portfolio but I can’t get into these funds with million dollar minimums and still be any sort of reasonably diversified.”

Alan looked into solving this problem that people who were accredited investors, meaning they had an income of $200,000 single, or $300,000 married, or investable assets of a million
or more qualified for these investments but couldn’t come up with the minimums. And so what CityVest does, is it forms access funds it basically puts itself as an intermediary between these big funds with a high minimums and the individual accredited investors. And by putting themselves in there and forming this access fund, they can lower the minimum investment for the investors. And sometimes negotiate a little bit better terms. Because they started going to the fund with 100,000 or 250,000 they’re bringing several million to the fund. And so they can often get a price break, better terms, et cetera, with the fund. But most importantly, then turn around to the investor and offer them a lower minimum. Because we’ve not a lot of docs, and come up with $100,000 at a time to invest in a fund like this. Certainly, in the first half of their career, a lot of docs can invest $25,000 at a time. And so that is kind of the CityVest proposition and I discussed on the blog a CityVest investment last December a bunch of people, a bunch of white coat investors ended up investing in it, I did not actually invest in that particular deal. But I think 120 people actually ended up talking to Alan about the investment and I think 44 of those hundred and twenty actually ended up investing, which is pretty good because the time limit was pretty sure is only over a couple of weeks and that was over Christmas. And so those guys got in on that fund.

But CityVest has another fund that they are forming right now and expect to close certainly by the end of March. This is another access fund and the fund that it will invest in is, a DLP lending fun. DLP is the name of the firm and basically this access fund is going to gather up money and form this fund of several million dollars, maybe three, four, seven, eight the goal is 10 million, but I don’t think they’re going to get there. I think they’re probably going to be closer to the six or seven or 8 million mark and then take that money and invest into the DLP fund.
It’s a good opportunity to get into this sort of asset class. DLP has an excellent track record it’s not that long, they only started in the last quarter of 2014 so it’s worked a little over four years now. But their records is very, very good, it’s up over 14% is what they have given to their investors so far, doing these hard money loans. Now, there’s lots of pressure in this space and so it wouldn’t surprise me if the returns were a little bit lower going forward from here. But this fund does well, it’s done well in the past, and every expectation is that it will continue to do well going forward.

Now, this particular fund, the DLP fund is basically an Evergreen fund, right? It’s not a fund with a stop date. But the access fund to be informed by CityVest is. The plan is for this fun to run three or maybe four years. It could possibly be extended another year if all the investors agreed to do it. But mostly this is going to be a three to four year investment. There’s not going to be any liquidity in those three to four years. You can’t get your money out if you need it. But over that time period, the expectation is that it will provide nice solid returns and exposure to this asset class of hard money lending.

So the proposition here if, you go to DLP directly, you’ve got to have a quarter million dollars. And that’s just kind of a big hurdle to get over for a doctor, especially if you want to have any sort of diversified portfolio, especially in my case. I mean, I only put 5% of my entire portfolio into hard money loans and so if I want to have three or four different funds out of that 5%, well, that takes a very large portfolio to put $250,000 in a single fund.

So DLP charges 1% a year basically is what they charge to the investors and everything else that comes in from the fees they charge to the home developers and the interest they charge the home developers gets passed on to the investors. There’s one other fee they charge when you exit the fund, DLP charges a 5%
fee. It’s kind of like a back load that way but I think the idea is to incentivize you to leave your money there long term rather than jumping in and out. So what CityVest did is, they went to DLP, and they said, “I can put together an access fund and the rules on that allow you to put up to 100 investors in the access fund. But we need you to lower the minimums for each of them, basically.” And so what CityVest is offering is a minimum of $50,000 instead of $250,000, you can invest only 50 and that is a nice benefit.

But they also negotiated more, that 5% fee to exit DLP won’t exist for those who come through this access fund and so that is a great benefit. Over five years, that 5% fee adds up to 1% a year so that’s not insignificant at all, it is a major, major benefit to go in through the CityVest fund. Of course, anytime you put somebody else in there, there’s going to be some additional fees, right? CityVest charges, three fees. The first one is a one time fee that is spread over all of the investors in the fund. This is a $50,000 basically set up the fund fee. And so depending on how much money is invested in the fund, it depends on how much of a fee that really is. If $5 million gets invested, that’s about 1%. If $10 million gets invested, that’s about .5%.

The second fee is charged each individual investor, it’s $500 a year. And that’s basically to cover the costs of running the fund here. And that works out to be about 2% a year, if you invest $25,000, or if you invest $50,000, that’s about 1% a year if you invest $100,000 it’s .5% a year. So it depends on how much you invest, it depends on how high that fee really is for you.

Then the last fee is .75% a year paid to CityVest. So in exchange for those fees, what they do is they give you a lower minimum and they manage to get that 5% exit fee waived for you. So that is basically the proposition CityVest is making. CityVest comes to me and says, “Hey, I need some more investors, you know a lot of doctors, if you refer me doctors,
we will also pay you, and out of what we earn off those fees from the doctors.” So I said, “Well, that’s great. But at each step, I want there to be value added for the investor.” And so the value I was able to negotiate with CityVest was to lower that minimum from $50,000 to $25,000 for you.

If you come through the links that we’ll put in the show notes, you can invest with only $25,000 into this fund. The other concession I was able to get from CityVest was a decrease in that 0.75% annual fee for the first year, that fee will be cut in half. And so that’s the incentive for you to come through my links rather than to go directly to CityVest and to invest in that fund. Even after those fees, if this fund makes the 14 and a half percent it’s been making, you’re still going to be making 10, 11, 12% in that range. It’s an excellent return for hard money lending fund. I mean, look at the Broadmark fund. I mean, I’m making 10 something percent on it. Look at the Arixa Fund, I’m making seven or 8% on that. Look at the Alpha Flow, I’m making seven or 8% on that. So yes, you’re paying some fees there but even after fees, your return should be good enough to be worthwhile invest in there.

So what’s the difference between this fund in some of those other funds? Well, instead of lending in California or Utah or Colorado, this DLP fund lends primarily in Pennsylvania, Florida with a little bit in New Jersey. And there’s some things about both the types of houses that they lend money to, they’re being developed. They’re a little bit C and B class houses rather than A class houses, cheaper houses basically that allows them to charge a little bit more. And frankly, there just aren’t as many people doing these loans out in those states as there are in California, as that allows them to have these high returns.

So I expect I’m going to invest in this deal as well. I haven’t decided how much I’m going to put in, obviously, the minimum will be 25,000, but I suspect I’m probably going to be closer to the 50 to $100,000 level just because I want to
minimize those fees that get minimized. That $500 per investor fee, is much lower as a percentage of the return if you invest 100,000 verses 25,000. Also, the incentive of course, is to get as many investors in the fund as possible. And I don’t think we’re going to have trouble getting the maximum 100 in there but to have each of those 100 invest as much as possible because the more it’s invested in the fund, the more that initial $50,000 fee is spread out over and lowers that fee relative to the entire investment.

If you would like to join me on this investment or learn more about it. There will be links in the show notes and you’ll be able to go to CityVest and talk to Alan Donenfeld and go over the paperwork and ask him any questions you want to about the deal and learn more about it. I’ll be talking about a little bit more on social media, maybe even on the blog a little bit in the coming weeks, but that’s basically the explanation of the deal. Okay, make sure if you want that special deal to be able to only invest 25,000 or to get that half of your first year’s fee waived that you let them know you came from White Coat Investor, otherwise you won’t get that.

Okay, let’s get into some of these SpeakPipe questions. Our first one comes anonymously and here it is. My question is about having a one time lump sum and how you treat it. There’s a ton of consolidation in healthcare today across multiple specialties. Along those lines, my rather large specialty practice is purchased by a private equity group to create a new practice management venture along with a few other founder practices. And my questions are both philosophical and practical. First, how would you count the proceeds from such a one time deal as it pertains to adjusted gross income for the given year? Let’s just say to use around numbers that the by out for physician was a million dollars plus another $500,000 in stock in this new venture, would you separate this one time payment out from your adjusted gross income or would you lump it all together?
So for instance, if you made $500,000 in 2018, would you say that you did make 1.5 million or would you count this as a separate bag unto itself? And then secondly, how would you approach a sudden windfall like this? We are planning to invest almost all of the actual proceeds those dollar figures which is made up, but we have been slowly doing it, paying taxes and whatnot, but I’m just curious how you would approach utilizing that money?

Basically the question here is, what do you do with a million dollars plus $500,000 in stock? How does that affect your adjusted gross income? Should you treat as a separate bag or just part of your income? Well, I’ll tell you this, the IRS is going to treat you as just part of your income, so you might as well do that. And when you’re using tax terms like adjusted gross income, that’s what we’re talking about. We’re talking about your adjusted gross income. And if you make the money in that year, you got to pay taxes on in that year.

But just philosophically, anytime you make money, it all really goes into the same pot, no matter where the money came from. Whether it came from your investments, whether it came from your spouse’s income, whether it came from your income, whether it came from inheritance, it’s all money, right? It’s all fungible and you ought to treat it all the same. That’s just a common behavioral mistake that people make to treat it as some separate amount, just because you had this windfall coming in, you got to do something different with it and that’s not necessarily the case.

So the second part of that question, however, was what do you do with a windfall? Hopefully, everybody listening to this podcast will get some sort of a windfall during the course of their life. You don’t know how much it’s going to be, you don’t know when it’s going to come but chances are, you’re going to receive something that maybe you weren’t expecting. And that’s really my definition of a windfall. But there’s really three categories of windfalls. The first one is the one
I call spare cash, right? This is money, maybe $10,000, maybe $200,000 that you weren’t expecting. And I would just take that money and kind of fold it into my existing financial plan.

Maybe you’re working on paying off student loans or paying down a mortgage, you’re trying to max out retirement accounts or putting money towards your kids’ college, you’re trying to save up for a new car, whatever. I just take that money and divide it among my goals in whatever manner I see fit, I’ll try to minimize interest and decrease taxes and maximize your returns. So early in your career, it’s probably going to go towards student loans, in your 50s maybe it all goes toward your mortgage, but most likely it’s going to be split among all the different financial goals you’re trying to accomplish, just like any other money you made, like your monthly paycheck.

The second category is what I consider enough money to make you financially independent. Maybe this is an inheritance of one or 2 million, it’s really enough to change your life in a significant way. And this is kind of the amount that this doc was talking about in the question. The best thing to do upon getting that level of money, is probably nothing. Do nothing for a few months, or maybe even a year, give it some time and really think about what you’re going to do with your life. If you’re ready to retire already, go ahead and do so. If you want to get out of medicine, write books, you can do that too. If you love what you’re doing, maybe you put a chunk toward retirement, give some away and you spend some, all right?

The third category is what I call ridiculous money. Okay, this is when you get a windfall like a lottery winnings, which if you invest it wisely there’s more money than you could ever spend given your current lifestyle. Okay, it might sound similar to category two, but is different in a few important ways. At this point, you’re going to need to engage in some pretty serious estate planning for instance. And you have a
real opportunity to make change in your community and in the world. So this is a responsibility that you can’t take lightly. You’re also going to have the hordes coming after you, both family members and just random people if they find out you received a windfall like this.

It makes me think about what Andrew Tobias recommended in the only investment guide you’ll ever need. Here’s what you said you should do if you win a million dollars. He said, “Go out for a very nice dinner, put about one year of normal living expenses someplace liquid like a bank or money market fund, and then put roughly equal sums into US Treasury securities, maturing to one, two, three and four years. Then put the bulk of the remaining money into stock index fund split between US and foreign investments. Buy a bigger house if you want one, but not so big that the cost of carrying it will strain you in any way. Maybe even consider buying a small rental property but don’t buy a boat is what he says. Make sure your will is in order and then relax and forget the whole thing. That’s Andrew Tobias’s advice and I think that’s pretty good especially the advice about not doing anything quickly. Now if you just inherited ridiculous money, try not to let anybody know about it, right? Because then you’re going to have the hordes knocking on your door. Another consideration, I think, is to actually consider annuitizing some of the money, right? You hear about all these lottery winners they go broke. Well, you can’t go broke if you ended up annuitizing it such that it’s going to pay you out a certain amount every month from now until the day you die.

It’s also a great time to get some solid unbiased advice. Talk to a CPA for some tax advice. Maybe an attorney from estate planning and asset protection advice. Pay him a fair hourly rate, rather than some percentage of your windfall, pay off your debts. I mean, if you’ve got some big inheritance, what’s the point of lugging around a bunch of little debts anymore? Get rid of them. And then put a big chunk of the money into
safe investments, CDs, bond funds, money market fund, et cetera. You have a much lower need to take investment risk than you did before the windfall. So take advantage of that by taking less risk.

Then I think it’s important to do a couple of other things. One is spend some of it. You just had a big windfall, this is like a diet, right? If you never break your diet, if you never loosen up just a little bit, you’re probably going to explode and the diets going to fail. So spend at least a little bit of money, right? Don’t go crazy, buying some massive yacht or something, but spend a little bit of the money. And then give some of it away, maybe some to your family but mostly to real charities they’re going to do some good in the world. I think that helps you keep money in the proper place in your life. And of course, remember that one of the benefits of having enough money is that you don’t have to maximize everything out.

You can use this to worry less about money because you have more now. I think that’s what you ought to do, if you get a big windfall, and whether that comes from selling your practice or whatever, it’s really all the same. Bear in mind one difference with selling your practice, particularly to some of these corporate management groups, is that it often comes with a lower future income. You’re trading a lump sum now for a lower income later. And so you got to keep that in mind, if you’re going to be making less money going forward, you’ve got to plan your lifestyle going forward on less money. And so in that sort of the case it’s important, but most of that windfall toward retirement. Okay, our next SpeakPipe question comes from Kelly.

Hi, my question is coming as the wife of a doctor who is just finishing his fellowship in pediatric anesthesia. He’s going into academic medicine, he just signed his contract to start at an institution this Fall. He will be going for student loan forgiveness and is on track right now to have the debt
forgiven in about five years after he starts the attending job. My question is, what are some of the things that we should be thinking about and considering to do the math, if you will, to see if we can afford for me to quit my job and become a stay at home mom?

We have two young kids, we currently have a full time nanny for them and I work. But I would love to have more time with them, especially for the next couple of years when they’re very young. But I want to know, what are not just kind of the short term things that we should consider in terms of the impact on our finances, but also what are the longer term things that we need to be thinking about in terms of how it could impact our retirement and what not, insurance needs and things like that? So without going into specifics here, we would just love some general guidance on how to think about it.

As you heard, Kelly’s husband is a pediatric anesthesiologist coming out of fellowship. He’s an academic, he’s going for public service loan forgiveness. And her question is really what do we need to do to decide if we can afford for me to quit my job? They’ve got a nanny, and she wants to quit but is a little bit worried about both the short term and the long term issues behind quitting. I think this is actually really common, particularly in the traditional scenario where the guy is the doc. He has been plugging through medical school and residency and fellowship and been supported by his wife, while they may or may not be having children as well.

And so this is probably a pretty common question and pretty common issue to deal with. But there’s a few things to consider. First of all, this doc is going from a fellow salary to an attending pediatric anesthesiologist salary, all right? There’s no doubt in my mind that if they keep their lifestyle under control, she can certainly quit, walk away and never work again. Let’s be practical about this. He’s going to have enough income to take care of business, to save up enough for
retirement, to pay off any debt, to pay for the house, to pay off the student loans. Although it sounds like he’s looking for forgiveness for most of them, but there’s going to be enough income there. I mean, that’s a huge boost in income.

I didn’t make anything near what pediatric anesthesiologist would make when I came out of residency and there was certainly plenty of money there as my wife did not have to work. If you don’t want to work, I don’t think that’s something that necessarily has to be done. But are there consequences? Sure, consequence number one is your income is not going to be as high as it would be if you continue to work. No doubt, right? And so that’s an obvious impact, it’s going to be a little bit slower to reach your financial goals. It’ll take a little longer to pay off student loans and save up a house down payment and buy that new fancy car you want or become financially independent, whatever your financial goals may be. But there are a few other issues as well, you might not have thought about.

First of all, the income drop might not be all that much. Kelly didn’t mention what she does for a living. She might be a physician making $400,000 for all I know. But one savings you will definitely have, if you’re coming home to take care of kids is you won’t have to pay the nanny anymore. And so there is some savings there and when you actually look at the taxes you pay being the smaller second income in a family, oftentimes it is really not worth continuing to work at all, when you calculate out your hourly rate. Once you include the cost of a nanny and you include the cost of the additional taxes and all those kinds of things, that can go away when you are working at home.

That’s an issue there but there are a few other issues. One, if you’re no longer working, you are going to probably want to have a little more life and disability insurance on the breadwinner. Now it’s not a bad idea to have some life and disability insurance or at least life insurance a little hard
to get Disability Insurance I suppose if you’re not making an income. But some life insurance on the person who is being a stay at home parent because what they’re doing has real value and you can calculate the economic value of it just look at what a nanny costs and a housekeeper costs and additional meals out costs and all those kinds of expenses that would have to be paid if there was not a stay at home parent.

But probably the most important long term issue here is the effect on her career, because when you take significant time out of the workplace, chances are your long term earnings are going to be lower and it will be harder to get back into the workplace. And you will probably not be as far along in your career as somebody who spent more time in that career rather than taking time off to raise a family and it might be impossible to get employed at all.

You get out of medicine for more than a few years and it’s almost impossible to go back in. Nobody’s going to want to license you, no one’s going to want to give you privileges et cetera. And so you have to be really careful I think probably the biggest thing to be careful about here is the impact on your career. If you’re sure you’ll never go back to it no big deal. If you think you might you may want to look into part time work, you may want to look into some way to keep your skills up. Okay, let’s take another SpeakPipe question this one from Michelle.

I’d love to hear you do a podcast on how you teach children ages three to 23 how to be financially literate, unspoiled and charitable.

That’s a tall order, it’s difficult. But I think there’s a lot of things you can do. I think the financially literate part is the easy part. It’s relatively easy to teach your kids about money once you understand it yourself. We start very young. Our three year old the other day was playing monopoly with our nine year old which was always interesting to see. And she said she wanted to buy a property and the nine year old...
explained to her, “Well, you’re going to have to go into debt to do that.” And so she did and then she started crying, “I don’t want to be in debt.” And so you can start pretty young teaching people about debt.

I make my kids listen to Dave Ramsey on the radio. Sometimes when we’re driving around in the evening to their activities. And they all scream and cry about it. “No, we want to listen to something else.” But you know what, in the end, some of those lessons are being absorbed, and they’re learning to pay attention to finances. They’re learning about the dangers of debt, they’re learning about retirement accounts, they’re learning about investments. They’re learning about these things that are important. But I talk to them about finances all the time, as you might imagine. I mean, you’ve seen some of Whitney’s writings on the blog and I think as the other kids get older, you’ll probably see some writings from them as well.

But the financially literate part I think is relatively easy. You just got to talk to your kids about money and teach them about stuff. And you’d be surprised this stuff is not that complicated. A lot of it can be learned at relatively young ages. You can even give them books, there some books that are written specifically for kids and you’d be surprised they find they’re interesting. All of my kids are gone had some sort of entrepreneurial pursuit, it might be a lemonade stand, they might be shoveling driveways for somebody else. You also have opportunities, I think, at times when they’re trying to raise money for something. You tell them, you’re going to have to earn a certain percentage of this yourself. For example, in June, Whitney and I are going to Honduras on a medical mission. And she wants to go along and I told her, she had to raise a certain amount of the money to be able to go along. And so she’s coming with up with all kinds of ways to raise money. And so I think it’s good to teach them a little bit about entrepreneurship that way as well.
The other two questions unspoiled and charitable, are a lot more difficult. Let’s take the charitable one first. One of the things we do is we give away a lot of money. As you know, if you paid attention to the blog the last couple of years, we’ve given away more money than we spent and we’re proud of that, but we want to pass that value on to our children. And so once a year at least we have a family meeting and decide what charities we’re going to support with our money that year.

And each person in the family gets an equal say, and we go around and we battle it out. And you have to argue for your favorite charity. I wasn’t able to talk anybody else in the family into donating to the access fund this year, which is a charity that basically helps keep climbing areas open. But we end up donating to other charities instead. And so I think I actually involving them in the family finances in a way that’s appropriate is also a great way to teach them to be charitable. Not only money though, also with time, and you can take them out and do service projects and those sorts of things with your children and teach them to be charitable.

It also helps I think, particularly when traveling to point out that not everyone has the advantages and opportunities that they have, which kind of segues us into the unspoiled section. And this is the big challenge I think when you start making decent money, particularly way money than either of you grew up with, is keeping your kids from running into being spoiled. And I don’t think I have all the answers on this one for sure. But I think some things that you can do are to maybe limit what they have. Just because you can afford to send them to school in a Range Rover doesn’t mean you should. Just as you can afford to buy them a $6,000 purse doesn’t mean you should, just because you can afford an iPhone, maybe they should have a flip phone until they reach a certain age. And so I think maybe artificially limiting how much money they see in their lifestyle is beneficial to them. It also helps to
talk to them about the times in your life when you really
didn’t have that much money. I’m constantly reminding my kids
that when they turn 18 and get their own car and their own
house and their own job that they can do whatever they want
and until then they have to follow my rules. And so that’s
kind of a constant reminder to them that at a certain point in
their life, they’re going to be responsible for themselves and
have to live on their own income.

I think it’s also important to make sure you don’t give them
too much money, particularly earlier on in life to ruin them.
I mean, most of us make enough money that we can truly ruin
our kids and so I think you have to be really careful how much
and how you pass that money on to them. And hopefully as they
prove that they can use it responsibly you can give them a
little bit more. Okay, our next question comes from an
anonymous asker let’s take a listen.

You always speak of buying the cheapest term life insurance
policy one can get at places like term4sale.com. But when I
purchased my own policy I worried a lot about the financial
health of the insurance company, especially when one buys a
term of 20 plus years. After some research on my own I found a
Comdex ratings and a solicited quotes directly from the top
four to five companies with ratings above 95. And ended up
buying a term policy from Northwestern Mutual. What role do
you think the Comdex ratings and all the ratings such as
customer service responsiveness should play in docs deciding
on which policy to buy? Should a young doctor worry about
getting a policy from financially sound companies only, even
if they cost a bit more? After all, if something were to
happen, you’d want them to actually pay out.

Basically, this questioner is asking how much does the
strength of the insurance company matter when it comes to term
life insurance? And I think it matters. I don’t think it
matters as much as a lot of insurance agents think it matters
but it’s worth looking at. So he mentions a site that’s
It’s a great place to get life insurance quotes without giving them any personal information and being able to compare them. But I think an interesting exercise can be done by going to that site and actually looking at the ratings for these companies. So these companies are rated from A++ plus which is superior to F, which is in liquidation and everything in between.

There’s A++, A+, A-, those are basically superiors, superior, excellent, excellent. And the default on the site is that they only show you companies that are excellent and up, so you’re either superior or an excellent. If you want, though, you can look at companies that are very good, which are the Bs or adequate, fair, which are the Cs very vulnerable, which are the Ds, right? So you can go as far down that list as you want to. But an interesting thing you’ll notice if you adjust that and look at the options that term for sale gives to you.

For example, if you ask for only the very top rated companies, the A+ pluses, the one it will come up with at the top of the list. And I will just put in, basically my birth date, a 30 year level term policy for a million bucks. It comes up with $1,000,532 a year. And it’s interesting if you just go with a default option the one that comes up at the top is Cincinnati Life Insurance Company, which is $1,415. It’s about $117 less you can save by going with a company that isn’t the very top rated company, so that’s pretty good. I went ahead and I put in basically, I let them go down as far as I think it was B- or so, which is still okay. But what turned out to be the best company? Well, it was Cincinnati still.

And it turns out that if you look at this list, the TIAA-CREF is the very top rated one that comes up here at $1,532. But in the very next category is Lincoln at $1,483 a year and in the third category is Cincinnati with $1,415 a year. And so even if you go way down the list, the cheapest company is still going to be Cincinnati which is A rated. I don’t think this is really a big issue in practicality, you’re not going to go to
a D company or an F company or probably even a B company. But is it worth dropping down below A plus plus to save 100 bucks a year? I think it probably is. I’d be comfortable with anything that’s rated A or higher on that and wouldn’t think twice about it. I think it’s fine to just use the default, the term for sale users for quality in the company. But if you’re really worried about it, pay another hundred bucks a year and get one of the very top rated companies.

Okay, I wanted to go over a little bit of feedback. We got the first one is from Podcast 85. Jim I want to say, Podcast 85 is fantastic. I love the format with regards to interviewing a doc and delving into the details their financial life. I was surprised to hear you say that medicine is more insulated from financial conflicts of interest because of the opaqueness of insurance reimbursement. Personally, I feel like I’m wrestling with the devil on my shoulder every day with the record to conflicts of interest.

I’m an academic vascular surgeon. I’m on a contract that is heavily dependent on RVU generation. This seems to be the norm in many academic and employed contracts. When I do a lower extremity angiogram, a diagnostic procedure reimburses, 4.5 RVUs this increases by 100% if I do an angioplasty and 150%, if I do an atherectomy. To make matters worse, there’s little time difference in any of the above and murky data to guide therapeutic modality choice. I’m constantly weighing evidence bases medicine and best practices against that little voice telling you to earn more. I can’t imagine I’m the only one out there with this feeling, in fact I’ve heard docs joke that Dr. So and so doesn’t participate in non RVU generating activities.

I’d love to hear more discussion about this because I think these sorts of production contracts are becoming so ubiquitous. Yeah, certainly, there are ways in which you can have conflicts of interest in medicine without a doubt. And I think this surgeon describes about as bad as they get. For
example, if you are on a salary, just a flat salary, say you’re a military doc, a VA doc, whatever, there’s basically no conflict of interest there whatsoever. In my group, it is not completely eat what you kill, but we are the business owners. At the end of the day we split up what’s left and divide it by how many shifts you worked in that month. And so that insulates you a little bit from the day to day decisions. Yes, you know that if you do things that bill more, you’re going to make more money. But since the group has 18 docs in it, every little decision you make, you’re really only getting 1/18th of the difference in that additional money that comes in from making a decision one way or another. And I think the conflict of interest there is much, much smaller and much easier to resist, than if you are 100% based on RVU compensation. I think that’s actually kind of a minority of doctors that are 100% RVU based. And so I think comparatively to a lot of other professions, your conflicts of interest are much smaller. Are they invisible? Obviously not. And this doc has given a great example of when they are not.

Also, I got some feedback from Podcast 86, regarding your podcast 86 on concentrated single stock holders in taxable accounts. There’s another way to diversify a single stockholder without selling donated and gifting the shares. It involves using an exchange fund and this here is right to point this out. This is true, this would have been a good thing for me to mention. He says, “It’s relatively unknown among most investors and typically requires a significant single stock holding like a half million or more, but exchange funds allow you to contribute your single stock into a pool of other stocks formed by the exchange fund, then when you withdraw your capital, your single stock holding converts into a basket of diversified stocks and often some real estate by law from the pool without triggering capital gains taxes.

Obviously, there’s fees pays to the exchange fund that makes the magic happen, he says Eaton Vance provides one of these
funds. So this is another way to basically flush capital gains out of your portfolio. Maybe that’s not the best way to put it. Rather than flush capital gains out what you’re doing is you’re achieving diversification with the same amount of capital gains. So that’s one other option to do if you’re trying to get rid of a very concentrated holding and diversify your portfolio a bit.

All right, this one’s gotten a little bit long so we probably ought to start wrapping up here. Our advertiser, our sponsor for this podcast is WealthKeel who utilizes a simple flat fee structure to offer both financial planning and investment management as well as project specific hourly advice. Chad, is a certified financial planner and fiduciary for physicians and their families. He’s been quoted by medical economics, the American Medical Association and CNBC for his work with physicians. Over the years countless WCI readers, both delegators and do it yourselfers have trusted Chad and his team at WealthKeel for ongoing financial planning and one time plans. To learn more and to schedule your free icebreaker call, visit wealthkeel.com/WCI or email Chad directly at ChadChubb@wealthkeel.com.

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8 Essential Traits of a Good Property Manager

[Editor’s Note: This WCI Network selection comes from Passive Income, MD and is all about how to find the best property manager. If you’re going to own real estate directly, finding a great manager is essential – You really don’t want to end up with a second job collecting rent and taking 3 am phone calls, do you?]

We want to invest in more “passive” income, where we can create wealth in our sleep—or at least while we’re enjoying time with our families and on our hobbies. Owning a rental property doesn’t sound so passive when the phone rings at three in the morning.

Instead, would-be real estate investors often find themselves opting for real estate funds, REITs, crowdfunding, or another (less hands-on) form of investing. I think all of these are great options, and I’ve found myself heavily invested in those as well.
However, I believe that **owning properties** is an amazing vehicle for developing long term wealth. I’ve seen it in the lives of some family members, friends, and a good number of financially-free physicians.

I’m sure you would agree that the idea of owning rental property is great—at least, in theory. But in reality, how are we supposed to own a rental property but still have the time to pursue our jobs, travel, spend time with our loved ones, and golf?

The key is simple: **Find good property management.** Sure, you could manage that property on your own, but is it worth it? In most, if not all, cases, I believe that you should leave the hands-on management up to someone else and free up your time. After all, your time is the most valuable resource.

Finding a good property manager is easier said than done, however. How can you find one of the good ones? What’s the evaluation process? Well, I’ve compiled a few essential things to look for when you select one for your property:

**How to Find the Best Property Manager**

**Experience**

This one is pretty obvious. You want someone who knows how to handle things properly, so they’re not calling you at the slightest issue. Find out how long they’ve been managing properties and the number of properties and/or units they have in their portfolio.

Ask them how they handle tenants who pay late, how they handle tenant complaints, and what they do with known troublesome tenants. They should also understand local laws when it comes to regulations, evictions, and standard operations of the
Extremely Detail-Oriented

I’ve dealt with a good number of property managers in my relatively short time as an investor. Finding someone who focuses on the details is crucial.

Running a business, which is what owning rental property is, requires every penny to be tracked and documented. After all, when it comes to tax time, the IRS wants that information. Will your property manager hand you poorly-written expense reports? Would they calculate the net operating income accurately?

Not only will this characteristic help both of you in the day-to-day tasks, it’ll be immensely beneficial through in the future, even if a different manager takes their place at some point.

Organized

Going hand in hand with the last point, finding a property manager with good organizational skills will save you some major headaches. If they have a clear process for even the little things (collecting rent, screening potential tenants, resolving maintenance issues, etc), you can be much more
confident in their ability to handle larger things when and if they arise.

Also, if you have a business-related question, especially around tax time, an organized manager will be able to answer it. This is your business, so finding someone with this trait will help ensure it runs smoothly.

**Fair Fees**

This is a big one. The whole idea of having a property manager is off-putting to a lot of potential investors, largely because it implies a sense of reduced profits. Having to pay a manager means you’re limiting your returns, after all.

Well, I just consider it a standard expense when I look for a rental property. I make my projections on returns based on an expected management fee and make sure I’m happy with that before purchasing the property.

What is the standard management fee? Well, it varies according to the type of property you have. I’ve found that if it’s a single family home, management fees tend to run 8-11% of the monthly rate. For multifamily, they seem to run from 5-8%, depending on the size of the building. Again, make sure you ask for a full fee sheet because typically, there are so many additional fees for example when there is tenant turnover or even when there’s rehab.
Good with People

I’ve found this to be extremely important. Not only is your property manager the manager of a building, they’re also an organizational leader. Trust me, if your tenants can’t stand your property manager and the way they talk to them, they will consider leaving. It’s happened to me.

Tenant turnover can be a killer on the bottom line - especially when you lose good, reliable tenants. Find someone who has a good demeanor. Fortunately, whether or not they have this characteristic should be pretty apparent after a few face-to-face meetings.

Communication Skills and Responsiveness

Have a property manager that’s hard to get on the phone? Right off the bat, that’s a major red flag. Communication is everything in this business, and the property manager is basically your eyes and ears when you can’t physically be at the property.

You’ll find a good property manager will communicate immediately (when appropriate). They may handle it themselves first, but they should make you aware.

Finding yourself leaving tons of messages and sending emails before getting a response is not what you want. It may be that they’re bad communicators or they just have too many properties to manage. Whatever the case, if you’re not getting the response you need, you’ll be in for a bad time.

Tech Savvy
There have been a good number of advances in technology that have made the lives of both tenants and managers way easier. Online rent payment options, portals for tenants and managers, and online maintenance requests have made communication simple.

As an owner, I now really appreciate having some sort of portal that I can log into to check my statements. Still, that last part isn’t a deal breaker for me, because having a manager who is good at reporting can make up for the lack of a portal.

However, it’s still nice to ask if they use a management system that allows you to do so (like Appfolio). Many tenants would even rather pay online than dropping checks in the mail. It’s a convenience thing, and the more convenient you make it for the tenant to pay their rent, the better.

Patience and Willingness to Teach

If you’re a novice property owner, having a manager with the willingness to explain things is an invaluable asset. Believe me, I’m still learning how to be the best owner and how to make effective decisions.

I’ve asked my property management a good deal of questions, trying to understand certain things, like why they patched something instead of replacing it, or why they set up their leases a certain way, or what their process for dealing with
trouble tenants is. The list goes on.

Bottom line: They should be patient with you and willing to teach you.

**Conclusion**

I’ve made mistakes in hiring a property manager and I’ve definitely seen how that can affect the way your business runs. A good manager has to wear many hats. They must be handy, they have to be knowledgeable, and be good with people (for better or worse). All of this comes from experience, yes, but it also takes the right kind of person.

I’ve rushed to find property management in the past, and I’ve paid for it with unhappy tenants, poor accounting, etc. It’s not fun. However, it took those situations for me to understand what makes a good property manager, and it made me realize that I shouldn’t compromise.

The tough part is discovering these traits before you hire them. Do this by asking for examples of accounting, what procedures and policies they have in place for other buildings, and paying attention to how they interact with you. In fact, don’t be shy. Tour another property that they own. Call those landlords and find out how happy they are with the management.

I believe this part is just as important as finding your
building. You need someone capable and competent to run not only the building but your business. They are your connection to the tenants and they need to handle that effectively.

Property management will free you up to what you wanted in the first place: enjoying time with your families and collecting that passive income.

Do you self-manage your properties or do you hire property management? Comment below!

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**Should You Invest in Real Estate Over a 401(k)?**

Q. Should I Skip Investing in a 401(k) in Favor of Real Estate?

I am a 4th-year medical student applying to residency and my initial plan is to do a Roth IRA and invest in real estate during my training (I have always had an interest in real estate and have been blessed enough to have successful mentors in that area). My goal is to build wealth, pay back student loans, and establish financial independence. However, I am not sure what to do about retirement accounts like a 401(k) when I finish residency and get my first “real” job. I have been reading lots of information on tax efficient ways to build wealth and, ironically enough, much of the information I have read think that investing in a 401(k) is a bad idea, especially when there is no match.
Tom Wheelwright (the tax advisor to Robert Kiyosaki who is the famous author of *Rich Dad, Poor Dad*) is vehemently opposed to a 401(k). In his book “*Tax-free Wealth*” he states that investing into a 401(k) is actually unwise for anyone seeking to build wealth for the following reasons:

**Investing in a 401(k) causes you to pay a higher tax rate on the profits from your investments.**

Outside of a 401(k), capital gains taxes from stocks are 15%, but if people retire rich, then their tax rate might actually be higher than 15% and their marginal rate might be over 20% as they withdraw money from the account. Since they deferred taxes by investing into a 401(k), once they withdraw money during retirement, they will not be able to pay the lower capital gains tax of 15% on their 401(k) profits. Instead, he/she will be forced to pay taxes on all the money they withdraw at the higher income tax rate.

**Investing in a 401(k) decreases your returns since you cannot invest using leverage.**

Unlike investing in real estate, where people can use leverage in the form of a mortgage to purchase more homes or investing in a business where people can use debt to purchase equipment or leverage their time by hiring employees, a 401(k) doesn’t offer that flexibility. He states that it’s much harder to invest using leverage inside of a retirement account and this
limits the types of investments one can make and thus lowers the returns they could have otherwise received. The example he uses is the limitation on what real estate deals one can purchase inside of an IRA vs outside of one.

**Investing in a 401(k) Decreases Control**

Investing in a 401(k) decreases the control you have on your investment since there are so many restrictions associated with them. The government has many rules on how much you can put in it, when you can take the money out, and what types of investments you can make inside of it.

To summarize, he recommends against putting money into a 401(k) since it only offers temporary tax savings and has many negative consequences such as the three listed above. He states that those who are seeking to build wealth and permanently lower their taxes should instead invest in things like businesses, real estate, commodities etc.

What are your thoughts? If you still advise that people invest in a 401(k) (even when there is no employer match), what is your reasoning? How do we combat the higher tax rate, the government restrictions, and the inability to use leverage to realize higher gains? I understand that this email is quite long, but I would love to hear your thoughts.
Let’s put a few arrows into the anti-401(k) balloon shall we Hermione?

A.

This reminds me of a post I did in 2017, titled In Defense of the 401(k), and in fact, the original name of this post was “In Defense of the 401(k) Part 2” until my editor pointed out that title had almost zero SEO value. Alas, the things we do in search of web traffic. So, I hope nobody thinks the title means I think real estate is a bad investment. I do not think that and have plenty of money invested in real estate myself. However, I also max out my 401(k)s.

It seems this tax-advantaged investing account is a frequent boogeyman for real estate investors. Like many of the arguments in this email, I think that’s a little silly. Like I did in part 1, I’m going to deconstruct the arguments, point out where they’re wrong, where they’re right, and where they’re simply a half-truth.
Kiyosaki Is No Real Estate Authority

First, let’s start with the obvious, at least obvious to those who have been in the personal finance sphere for a while. Robert Kiyosaki wrote a best-selling book(s), but it was based on a lie and has been heavily, accurately, and appropriately criticized. Every Kiyosaki fan should be aware of these criticisms, probably best expounded by John T. Reed. Needless to say, once you read that, you’ll be far more skeptical of anything and everything Kiyosaki says, much less his tax advisor. It’s not that there is nothing useful in his books, but don’t treat it like scripture.

Residents Make For Lousy Real Estate Investors

Second, let’s go ad hominem (just a little.) You’re a fourth-year medical student and sent me this letter in November. Now I’m all for learning some finance and investing in medical school, but my recollection of November of MS4 was that it was all about matching into a residency position. You’ve already invested 7+ years into becoming a doctor, and have at least 3+ ahead of you. A career in real estate is very much a viable path to wealth, but it doesn’t seem to be the path you are on. A typical resident has neither the time nor money to be a successful real estate investor and I worry that spending a lot of time on that goal would affect what I think ought to be your primary focus – becoming a good doctor. Tell you what, come back in a half decade or so after you have completed residency, paid off your student loans, and built up a little capital to invest and let’s talk.

Seriously though, all a doctor has to do to become wealthy is learn to practice good medicine, live like a resident for 2-5 years after residency, save 20% of gross for retirement the
rest of her career, and invest it in some reasonable mix of stocks, bonds, and real estate. That doc is highly likely to retire with the equivalent of a mid 7 figure portfolio today, which will provide a physician level of income throughout retirement. Anything above and beyond that is a bonus. Lots of docs have done just fine with real estate and I don’t want to discourage you (probably couldn’t even if I wanted to.) It’s great. But it’s not a reason to hate on 401(k)s. There are many roads to Dublin. If you prefer real estate to stocks and wish to make your portfolio 80% real estate (the opposite of my 20% position), I think that’s fine. If you want to buy one property a year after finishing residency, I think that’s fine. But I see little reason to take an extreme position in the stocks vs real estate debate.

Real Estate Investors Don’t Like 401(k)s

Third, if the authors of all the books you’re reading don’t like 401(k)s, maybe you’re not reading the right books, or at least not all the right books. If all the books you read say the same thing, you probably ought to broaden your perspective a bit. May I suggest a book or two from a Bogleheadish perspective? Maybe something that talks about the benefits of
The Tax Advantages of a 401(k)

Fourth, I’ve been surprised at the pathetic understanding of the tax code among many real estate investors. Somebody in some seminar or book somewhere told them that real estate is awesome for taxes and retirement accounts suck and they just believed it without actually learning how the tax code works. Let’s talk for just a minute about the tax benefits of a 401(k).

#1 Tax-Protected Growth

The investments in the 401(k) kick out income and you occasionally sell something with a gain and buy something else. You don’t pay taxes on any of that as it grows.

#2 A Big Tax Break

The second benefit is a big fat tax break the year you contribute to the account. In fact, this is the biggest tax break available to a doctor. My practice has offered a 401(k)/PSP ($56K in 2019) and a DB/CBP ($5-120K in 2019) allowing $61-176K to be protected from taxation. At my 42% marginal tax rate, that could knock as much as $73,920 off my tax bill once I am old enough for that $120K/year contribution. For each year I contribute. That’s hardly insignificant, but wasn’t even mentioned in your email and presumably in Mr. Wheelwright’s book.

#3 Withdrawing at a Lower Tax Bracket

The third benefit is the opportunity to do Roth conversions or withdraw money in your lower income years. The idea here is to defer taxes from high-income years to low-income years. For most docs that aren’t super savers, they’re going to be able to withdraw or convert money at a lower tax rate than their
rate at contribution at some future date. That might be as they phase out of their career. It might be in early retirement before they start taking Social Security or have to take RMDs. It might even be in later retirement. Most docs drop a couple of brackets or more when they retire, so even if the brackets inch up a bit, they still come out ahead. In addition, especially before taking Social Security or for someone without a pension or a bunch of rental income, they can use those tax-deferred withdrawals to fill the brackets. $24K standard deduction? That’s $24K that comes out tax-free. Contributing at 42% and withdrawing at 0% is a winning combination. The next $50K comes out at 12% and nearly $100K comes out at 22%. Win, win, win. This dramatically trumps the benefit of the lower capital gains rate (which isn’t always 15% by the way. For me in my state, it’s 28.8%. Lower than 42% yes, but not quite as awesome as it sounds, especially since it is also applied as the investment grows and not just at the end.)

Okay. Maybe you’re a super saver. You probably are given that you’re thinking about this stuff as an MS4. You could potentially be withdrawing at the same or higher rate in retirement, especially with a lot of rental income. So is the answer in that situation to avoid the retirement account? No way. The solution is to make Roth contributions and conversions at every opportunity. Or is there something I don’t know about investments never being taxed again that is bad? I can’t think of anything. I mean, if you like the lower long term capital gains rate, you’re really going to love 0%.

But wait, there’s more. In most states, retirement account money is also protected from your creditors. While you’ll likely never need that asset protection, it’s nice to have it. Investments in your taxable account do not have similar protection. Sure, you can put a real estate property into an LLC, but that’s not quite the same thing.
Okay, I think we’ve addressed your/Mr. Wheelright’s first point.

**What About Leverage?**

It is generally true that it is easier to use leverage outside of a retirement account than in one. Brokerage firms don’t allow margin to be used in a retirement account like you can use it in a taxable account. But there are plenty of situations where leverage can be used in a retirement account. You can buy a leveraged hard money loan fund with a self-directed IRA, for instance. You can even put equity investment property in a self-directed 401(k) and use leverage on it. Yes, Wheelright is correct that it’s a significant hassle. But it can be done.

Now, I don’t necessarily recommend you put investment property into a retirement account. But neither do I recommend you try to leverage up all of your investments. Leverage introduces additional risk, and it is a good general principle of investing that you avoid taking more risk than you need to take. Most doctors don’t need to take on much leverage risk in order to meet their reasonable investing goals.

I think we’ve now addressed your/Mr. Wheelright’s second point.

**Are 401(k)s Inflexible?**

There’s no doubt that 401(k)s are less flexible than investing in a non-qualified account. That much is true. There is a price to be paid for those awesome tax and asset protection benefits. However, they’re not nearly as inflexible as the typical real estate investor thinks. Consider all the possible exceptions to the 10% penalty for withdrawing money before age 59 1/2:
- Unreimbursed medical expenses > 7.5% of your adjusted gross income (which may not be that high if you’re retired)
- Pay for medical insurance
- Disability
- Inherited IRAs
- Qualified Higher Education Expenses – for you, your kids, or your grandkids
- A First Home for you, your child, or your grandchild.
- IRS Levy
- Reservist Distribution
- Early Retirement Via the SEPP rule

What exactly do you think you’ll need to tap your retirement money for that isn’t on this list? Besides, if you’re such a super saver that you’re worried you might pay more on withdrawal from a tax-deferred account than at contribution, you’re almost surely going to have investments that are outside retirement accounts anyway.

In addition, you can borrow up to 50% of a 401(k) or $50K, whichever is less.

I think we’ve now addressed your/Mr. Wheelright’s third point.
Bad 401(k)s

Another issue some worry about is lousy 401(k)s. Some 401(k)s have tons of fees and have lousy investments. Even in those cases, the 401(k) is probably still worth using. First, because you probably won’t be in it for long before your employer changes it (especially with all the lawsuits going on against employers for neglecting their fiduciary duty) or before you change employers. But second, the overall tax break is so large that it will overcome even moderately high fees over the long run.

A Reason To Avoid a 401(k)

Can I imagine a scenario where it might make sense to skip a 401(k) contribution in order to invest in something else? Sure. This would be a situation where I either had very limited investment dollars or exceptionally large retirement account availability AND a particularly attractive investment that could not be placed into the retirement account. I mean, if you can buy a surgical center likely to provide 30% returns going forward, then you can probably justify skipping the 401(k) that year if you absolutely have to. But I don’t think you should put all of your money into real estate, and if you’re going to invest in stocks and bonds (and even REITs), you might as well do it inside retirement accounts and enjoy the tax and asset protection benefits.
401(k) Vs Real Estate – I Invest in Both

As you can see, while there is some truth in what Mr. Wheelwright is saying, it can be very misleading. You owe it to yourself to understand how a 401(k) works and then make an informed decision about it. I suspect that, like me, you’ll choose to max out the 401(k) and then invest in real estate above and beyond the 401(k). You’ll notice I haven’t even talked about an employer match. I’ve never actually had one, but I’ve been maxing out a 401(k) (or two, or three) every year since I left residency. A match makes this all even better. A match is best thought of as part of your salary that you’re leaving on the table when you don’t contribute enough to the 401(k) to get it. That would be really stupid. I invest in real estate. I also have four 401(k)s. They don’t seem to be slowing down my wealth creation one bit.

What do you think? Would you skip a 401(k) in order to invest in real estate? Do you invest in both? Why or why not? Comment below!
Why Investing is Hard

Investing is hard. In fact, it is so hard that the combination of a decent income, financial literacy, and financial discipline is so rare that it effectively functions as a superpower. Today we’re going to talk about twelve reasons why investing is so difficult.

# 1 You Need to Have Something to Invest

Inexperienced investors focus on the investment, while those in the know focus on having something to invest. Having something to invest requires three things:

1. A reasonable income
2. The discipline to not spend your entire income
3. Avoiding loss of earnings/capital through divorce, death, disability, liability, and speculative investments

You’re going to need a fair amount of each of those things to be successful, although you can often make up for a low amount of one of them with an extreme amount of another.
# 2 Wall Street is Out To Get Us

By Wall Street, I refer to the financial services industry. This can include bankers, insurance agents, stock brokers, attorneys, accountants, investment managers, financial planners, and advisors of all types. At the end of the day, these professions exist to transfer money out of your investments and into their investments. That’s not to say there are never times when they add more value than they cost. But in investing, you get what you don’t pay for. The less you pay in fees, the more you have and can use to save, invest, and later spend. The successful investor is very fee-conscious. She knows what fees she is paying and evaluates them periodically against the value received. She understands the financial conflicts of interest of her advisors and weighs the advice with them in mind. She completely avoids the vast majority of financial services firms and professionals like Odysseus tied to the mast.

# 3 Investing Takes Too Long

Successful investing is all about the “get rich slow” plan. That would be fine if we weren’t both impatient and mortal. Most reasonable investing plans span decades. Juxtapose that with our attention span, that may be minutes at best, and you have a recipe for failure. Jack Bogle has repeatedly said that the three most important words in investing are “Stay the Course.” It actually doesn’t matter what your investing plan is, as long as it is something reasonable. What really matters is that you can stick with it in the long run. Better to be 60% stocks and stick with it than 80% stocks and bail out in a bear market.

# 4 We’re Competitive

I like competition. I thrive off of it. As a kid, a friend and
I would play trampoline basketball. The game would last hours because neither of us wanted it to end. We didn’t really care if we won or lost, but we wanted it to be close. “Win by two.” “If I make this shot, I’m back in.” “Make it, take it.” “Dunks are worth two.” Nobody ever asked, “Why’s James crying?” because James didn’t cry. It should be no surprise that despite relatively humble beginnings, one of us founded The White Coat Investor and the other one is a successful Chief Investment Officer of a private equity firm. Now, most people probably aren’t as competitive as we are, but most people ARE competitive, particularly those who earn enough to actually be successful investors. However, when it comes to actually winning at investing, competitiveness is bad because it leads to two problems:

1. Keeping up with the Joneses. If you try to keep up, you spend too much and have nothing to invest (see # 1 above).
2. We focus on beating the market or other investors rather than our own financial goals.

You see, investing is a single player game; it’s just you against your financial goals. You don’t have to beat the market. You don’t have to beat your neighbor. You don’t even have to beat your brother-in-law. The truth is we can ALL win. But if you don’t keep that in mind, you’ll end up succumbing
to FOMO - Fear Of Missing Out and end up buying high and selling low, a financial disaster.

# 5 It Requires Hobby-Level Dedication

Investing is a great hobby, perhaps the best-paying hobby there is given the cost of high-quality financial advice and management. But our financial world is so complex that if you don’t take up investing as at least a minor hobby, you probably won’t become good enough at it to be successful. That’s unfortunate since it is such an integral part of a successful life. Plus it’s boring for most of us. Here we are, with a second job as our own pension fund manager in our 401(k) world, and we know nothing about doing that job and have little interest in learning. What a tragedy.

On the other side of the problem are people who take it to the extreme. All of a sudden, all of our decisions are first weighed from a financial point of view, even when that is inappropriate. Perhaps we become miserly. Perhaps we become consumed by a quest for more, more, more. Perhaps we just can’t step back and end up living an unbalanced and unhappy (even if financially successful) life. Picture the 65-year-old retiree who spends 3 hours a day reading up on stocks. What a waste.

# 6 Wealth is What You Don’t See

This confuses all kinds of people. Lots of people think they want to be a millionaire, but what they really want is to spend a million dollars. Unfortunately, those two things are complete polar opposites. You literally become a millionaire by NOT spending the $1 million that you could have spent. This is surprisingly non-intuitive and I’m convinced not understanding it keeps many from being successful. So figure
out what you want – to have lots of money or to spend lots of money, and take the steps required to get there.

You literally become a millionaire by NOT spending the $1 million that you could have spent.

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# 7 The Frank-Starling Curve of Investing

The Frank-Starling Curve is well-known to physicians who care for congestive heart failure patients. The goal is to have the patient’s blood volume high enough to maximize the heart’s stroke volume but no higher. Too low, you give them fluids. Too high, you give them diuretics to take off fluid.

Investing is somewhat similar. Increasing the time and effort you put into it helps, but only up to a certain point. Beyond that point, you’re often hurting yourself. Someone who is invested in crummy mutual funds and never rebalances is on the left-hand side of the curve and would benefit from more effort. A day-trader is way off the right side of the curve. It isn’t intuitive, but at a certain point, more effort and time spent on the task is more likely to hurt than to help.
# 8 Debt Numbness

Spending borrowed money for educational expenses and basic necessities for four years in medical school (perhaps eight or more if the doc also borrowed for undergraduate) and then allowing that debt to become even larger due to deferment, forbearance, low Income Driven Repayment payments, or special resident refinancing programs for three to seven more years of training causes doctors to be numb to debt. Everybody they interact with owes hundreds of thousands in student loans. It feels normal. Due to the long period of indebtedness, this attitude toward debt extends to auto loans, credit cards, 0% down doctor mortgages, and even borrowing for the education of your own children! This debt anesthesia can severely retard your ability to build wealth. Instead of your income being used to live the good life and build wealth, it is used to service payments. You’ve become a fantastic investment for somebody else!

Investing is hard, but it’s no harder than finding passable highways in Baja California

A related problem is the concept of “good debt.” I read about
this all the time in blogs and books, although the definition varies. Mortgages get thrown into the “good debt” category because they may be tax-deductible and the underlying asset may appreciate. Student loans get thrown into that category because “they help you earn more.” Low interest rate debt gets thrown in there too, no matter what the original purpose of the debt was. There is no doubt that borrowing at 2% and earning at 8% is a winning formula. The problem is that the concept of “good debt” worsens debt anesthesia. You no longer feel like your debt is an emergency because it’s “good debt” so you justify not paying it off as quickly as you ought to.

In addition, borrowing at 2% and NOT investing at 8% IS NOT a winning formula, but that’s what most who justify their debt because of its low interest rate do. Any time you have debt and you’re spending money on anything non-essential, you’re essentially borrowing to fund that purchase. You wouldn’t borrow at 4% for a Hawaiian vacation? How is that different from going to Hawaii while you still have 4% student loans? And 8% student loans? Are you nuts?

It’s a simple fact – money that is going to pay the interest (and even the principal) on your past spending cannot be invested for your future spending.

This debt anesthesia can severely retard your ability to build wealth. Instead of your income being used to live the good life and build wealth, it is used to service payments. You’ve become a fantastic investment for somebody else!

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# 9 You Change

Another issue that makes investing difficult is that very little is static, especially in your life. Your spending, your consumptive desires, your health, the size of your family, your tolerance for risk, and your income all change over time.
How can you set a retirement goal if your spending keeps changing? How can you set a savings rate when your income keeps changing? How can you set an asset allocation when your risk tolerance keeps changing? This need to stay the course is constantly butting up against the fact that the course is constantly changing, and that makes financial planning and investing a tricky business of constant adjustments.

# 10 The Investor Matters More Than the Investment

Too many investors focus their efforts outward, constantly searching for the best investment. In reality, they should be focusing inward, making themselves the best investor possible. The truth is that your actual investments, your asset allocation, so long as it is reasonable, matters far less than whether or not you can stick with it through thick and thin.

Too many investors focus their efforts outward, constantly searching for the best investment. In reality, they should be focusing inward, making themselves the best investor possible.

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# 11 We Are Poor Judges of What Will Make Us Happy

“Mann Tracht, Un Gott Lacht” is Yiddish for “Man plans and God laughs.” It turns out we are incredibly poor judges of what will make us happy. We think buying things, or buying experiences, or traveling, or giving money away will make us happy, then are surprised when the happiness we were seeking turns out to not exist or to not last. The problem comes when we start making long-term financial plans and it turns out that isn’t what we want after all. At its extreme, this leads
to divorces and massive repeated home renovations, both of which can be devastating for wealth building. But even in its more minor forms, it can be costly.

# 12 We Don’t Do Boring Well

Good investing is boring investing, but looking for excitement with your investments is a good way to go broke. Our desire for novelty is a major impediment toward staying the course with a long-term sensible plan.

Those are the twelve reasons investing is hard. Conquer them and you will find a simple, but not easy, pathway to wealth.

What do you think? Is investing hard or easy? Why? Comment below!
Competent to DIY Your Investments

Q. What do you think are good ways to ensure someone is really ready to take on their personal finances for themselves? From reading posts on The White Coat Investor Facebook Group, many people seem very educated about finances and are asking good questions. However, I also find that some who comment seem more confident than anything else. Other than continuing to read and learn, I wonder if there is a certain point where a person should know that they are capable of doing things themselves rather than using the various types of assistance out there.

A. I thought this was a great question and spent a long time thinking about DIY investing before writing this post. Hopefully, I answered it well, but if I didn’t, I’m sure you’ll let me know in the comments section.

# 1 You Don’t Have To Be Fanatical

Thanks to the reach of this website and podcast, I’ve interacted with literally hundreds of thousands of high-income professionals over the years. Many of those have used the information I have presented to learn how to competently
manage their own finances. By doing so, each of them will save hundreds of thousands, perhaps millions of dollars in advisory fees over the course of their lifetime. However, this DIY financial planning and investment management thing is too often presented as a dichotomy—you either have a full-service advisor or you do it all yourself. In my experience, there are many, many people who have found a middle path. That path may involve using a good fee-only advisor to draw up an initial financial plan, answer some questions, and set up a portfolio for you. The path may involve using an advisor for a few years before taking over yourself. Sometimes the advisor manages one account while you manage another. Sometimes people just check in with an advisor periodically for a second opinion on what they’re doing. This is especially common as people approach retirement.

Of course, there are also people who don’t want to do it themselves at all. I met another one the other night, a residency-mate of mine. She has zero interest in finance. She will never read this blog post. Frankly, the best thing I can do for her is to make sure she’s getting good advice at a fair price. Yes, she’s going to end up paying a lot of money for this, but she will be far better off paying a fair fee than doing a poor job of planning and investing on her own.

So, the first thing you need to realize if you’re going to be a competent DIY investor is that you don’t have to DIY to be successful. You can work with a financial advisor and reach your goals.

# 2 You Find Investing Interesting

A major characteristic of DIY investors is that they find personal finance and investing interesting. Not necessarily thrilling, but there is a certain amount of a hobbyist mentality that seems to be required. If you have enough interest, you will develop the knowledge and discipline
required to be successful. But there’s very little that can be done if you can’t find even a modicum of interest in this stuff.

# 3 You Can Write Your Own Financial Plan

Producing a written financial plan isn’t that hard to do. Many DIY investors are perfectly capable of doing so after reading a few good books and blogs and perhaps participating on some good internet forums for a while. Others need a little more help. Katie and I feel having a written plan is extremely helpful in reaching your financial goals, so much so that we spent two months of our lives putting together an online course to help you to make one. Many who don’t yet feel competent making their own plan will feel so after taking that course. However, others will need even more help and should hire an advisor to help them draft a plan, even if they don’t plan to continue to use the advisor.

If writing a financial plan seems easy to you, you’re probably ready to do it on your own. If that task sounds impossible, you’re not ready.
Most DIY investors are really **bothered by paying advisory fees**. It’s not that these investors are cheap (although they often are), it’s that they simply don’t see value there equal to the price being paid. When you start looking at your advisory fees and they really start bothering you because you feel that any mistakes you might make are going to cost you less than you would be paying someone else to prevent them, you’re probably ready to do it on your own. I wish it were true that advisors never make mistakes either, but unfortunately, that’s far from the case, especially given the **minimal requirements to call yourself an advisor**.

I’m not talking about ridiculous fees here. **If you’re paying five figures** a year for financial services, you can almost surely get similar quality advice for less. But when an advisor offers to manage your portfolio for $2K a year (a VERY fair price) and you think “No way I’m paying that,” you’re probably ready.

DIY camping on a 2,000-mile road trip from SLC to Cabo San Lucas.
When You Start Poking Holes in the Advice

After a while, many DIYers realize that they know more than many advisors. They start poking holes in the arguments and recommendations of the advisor. They can actually take a position and argue it well in many of the common debates out there such as:

- The ideal asset allocation
- What factors a portfolio should be tilted to and how much
- What a safe withdrawal rate is
- Roth vs traditional IRAs and 401(k)s
- How to incorporate real estate into a portfolio
- How to prioritize debt pay off vs investing
- Passive vs Active Mutual Funds

Many of my readers have had this experience as they’ve tried to teach their advisors about the Backdoor Roth IRA or the Multiple 401(k) Rules. When they realize they’re paying to teach their advisor, they’re probably well on their way out the door, along with their assets.

Note that becoming furious at bad advice that you’ve been given is not enough to DIY. Just realizing you’ve been sold whole life insurance inappropriately and overcharged for advice isn’t enough, although that often provides the motivation to get to enough in more ways than one.

You Have Read Some Books

While it may be possible to become a competent DIY investor without ever reading a financial book, it seems unlikely to me. I’d put the bare minimum for my readers at four books – a book on personal finance, a book on investing, a book on
behavioral finance, and a physician-specific book. Here are some recommendations.

# 7 You Know How To Answer Your Own Questions

When you first get started, you don’t even know what questions to ask. Then after a while, you know the questions but need some guidance to find the answers. I get these questions all day by email, Facebook, Twitter, and even in person. The next step is knowing how to answer the questions yourself. That might just be knowing who to ask, but more likely it involves knowing the language of finance so you can Google appropriately. It also involves a baseline level of financial knowledge so you have a framework into which you can insert the new information. It’s probably going to involve knowing your way around the various IRS publications and form instructions. You’ll know how to use the Morningstar database and mutual fund provider websites to learn about funds. You’ll have found some reliable forums and blogs that you can trust. Maybe you’ll even have built a network of trusted advisors or friends you can go to. But however you find the answers, you’ll know you’re competent to DIY when not knowing the answer to a question no longer fills you with dread and a desire to run out and hire someone to just do all this “money stuff” for you.

# 8 You Find Yourself Teaching

Here’s another common experience among DIY investors. They find they are spending far more time teaching than learning, whether in person or online. Many of them start blogs, do podcasts, or become fixtures on internet forums. They are often the “go-to” financial person in their group or residency program. If you feel like you could give a lecture to other doctors on the basics of personal finance and investing, you
are probably ready to be a DIY investor.

# 9 Balance Confidence with Humility

The classic surgeon stereotype is that they are sometimes right and sometimes wrong but never in doubt. It takes a certain amount of confidence to take on a task like managing hundreds of thousands or even millions of dollars. If you don’t yet have that confidence, you may not yet be ready to be out on your own. Of course, you don’t want to be overconfident either. For example, if you think you have a working crystal ball that will show you future economic scenarios, interest rate changes, or market performance, you’re probably overconfident. A certain dose of humility about how much more there is to learn is helpful, but you don’t want to be so “humble” that you’re paralyzed from taking necessary steps. Many DIYers have commented to me that their confidence actually trailed their knowledge by about a year and that they should have fired their advisor about a year before they did.

# 10 You’ve Developed Discipline

While I believe that most people with sufficient interest will develop both the needed knowledge and discipline to be
successful, you don’t really know how disciplined of an investor you are until you’ve suffered through your first bear market or economic downturn. I’m always amazed and worried to see brand new investors extolling the virtues of 100% stock portfolios and heavy doses of leverage. I think you are better off erring on the conservative side of asset allocations and leverage until you know yourself a little better. Then if your behavior in your first bear market is good, you can ratchet up the risk a little bit. If you’re like most though, you’ll probably find your risk tolerance is a little lower than you thought.

Underestimating your risk tolerance is no tragedy. Your return matters far less than your savings rate early on anyway. But overestimating it can be a financial catastrophe, especially late in an investor’s career. Risk tolerance is a lot like The Price is Right—you want to get as close as you can to your risk tolerance without going over. That would be a lot easier if your risk tolerance were stable. Unfortunately, we all have higher risk tolerance when we’re making money than when we’re losing it. The risk tolerance you care about is your risk tolerance AFTER you’ve lost years worth of savings.

I hope these ten suggestions can help you determine whether you are now competent to be your own financial planner and investment manager. It’s certainly a lot easier if you start
earlier when the consequences are smaller. But it’s really the same game — later on, there are just more zeros at the end of the numbers. I’ve managed four, five, six, seven, and perhaps eventually an eight-figure portfolio. It really is the same thing. I used to get nervous to buy $1,000 worth of stock but now swing around six-figure amounts just to do some tax loss harvesting. With time, you become more and more competent. Well, at least until the last decade or two of life, but that’s a subject for another time.

What do you think? Are you a DIY investor? How did you know you were competent to do so? Were you overconfident at first, or underconfident? Comment below!

My Money Is Worth More Than Your Money

[Editor’s Note: This post is republished from WCI Network partner, Physician on FIRE.]

No, Loonie Doc, I’m not talking about your loonie Canadian dollar. Nor am I referring to the measly seventy cents or so that the New Zealand and Australian dollars are now worth (in 2018). This article has nothing to do with exchange rates. Although, friends, it is true that my money is worth more than yours.
Today’s post is focused on the value of the American dollar in various retirement accounts. While I have seen a few very detail-oriented people adjust their net worth based on where their money is held, most of us — myself included — just add up the value of all the accounts to arrive at the total. Is that the best approach?

When a Dollar is Not a Dollar

If you’ve been earning and investing for a while you most likely have money in a variety of account types. Some of those dollars are inherently worth more than others, depending on the current and future tax treatment. Let’s take a look at each of those dollars, from the most to least valuable.

Roth Dollars

Roth dollars are the most valuable dollars you can have. If they were a day of the week, they’d be Saturday. You’ve already paid tax on them, and they will continue to grow tax-free until you use them. These dollars have a value of $1.00. The Roth dollars also benefit from being sheltered from required minimum distributions (RMDs).

While it may not be ideal to make large Roth investments when
you are in a high-income tax bracket, particularly if you anticipate a lower tax bracket in retirement, Roth dollars are sure great to have. If nothing else, contribute to a backdoor Roth for yourself and your spouse, if you’ve got one.

I made one small Roth conversion as a resident, a Mega Roth conversion as an attending, and have made backdoor Roth contributions for several years.

30% of our dollars are Roth dollars.

HSA Dollars

Dollars in a Health Savings Account (HSA) are the next best thing. They’re like Sunday; it’s still the weekend, but not as enticing as Saturday. When used for healthcare costs, the dollars in an HSA act just like Roth dollars.

Even better, you received a tax deduction when you put those dollars in the account. In the year that you contribute, you could say these dollars are better than Roth dollars, but after you’ve received that deduction, the dollars remaining are at best equal to Roth, and at worst equal to tax-deferred dollars.

There a couple ways to use your HSA dollars to cover healthcare expenses. One tactic is to use the account to pay
for healthcare expenses when they are incurred. A second option is to save receipts, allow your HSA account to grow tax-free for years, then take a large reimbursement for the sum of the receipts after collecting them for years or decades.

The latter approach, saving receipts, has the potential to work out in your favor. You receive the benefit of tax-free growth of dollars that are not withdrawn when the bill arrives. I’ve begun to implement this strategy, and I’m not convinced the record keeping is worth the small benefit. I’ll probably continue to save receipts until we pack up for our next adventure, and then cash in.

[Post-publication edit: I’ve cashed in and now choose to pay as we go. It’s a tiny portion of my portfolio and saving and tracking receipts is something I found to be cumbersome, but I do understand the benefit of doing it the other way.

I don’t pay directly from our HSA, though. I first put our healthcare expenses on a rewards credit card and then reimburse myself from the HSA. I think getting free travel is a bigger benefit than avoiding a bit of tax drag on this small portion of my money.]

If you end up with more HSA dollars than you can use for healthcare (not bloody likely), you can use the account like a traditional IRA at age 65. The money can be withdrawn penalty-free for any reason, but you will pay income tax if it not used to pay for healthcare expenses. Note that HSA money cannot pay for health insurance premiums, but can cover out-of-pocket costs and a lot of other expenses, like orthodontics and eyeglasses.

Flex Savings Account (FSA) dollars can be viewed like short-term HSA dollars, but typically must be used up by the end of the calendar year.
1% of our dollars are HSA dollars.

0% of our dollars are in Swedish krona

**Taxable Dollars**

“Taxable” sounds bad and expensive, just as “spinal” anesthesia sounds barbaric and scary. The truth is far from the implication from the off-putting word in both cases. Dollars in a [taxable account](#) are great dollars to have, and a spinal anesthetic, given below the level of the spinal cord, is often the safest and least invasive anesthetic option.

Taxable dollars are like Friday – part weekday, part weekend. You’ve already paid taxes on these dollars once, and the worst you’ll do is pay some tax on the growth of these dollars. At best, “taxable” dollars can be treated the same as Roth dollars.

How are taxable dollars taxed? If they earn interest in a savings account, the interest is taxed as ordinary income. If you sell a stock or mutual fund that has grown in value, you may owe some taxes on the gains. The same is true for dividends. Gains on equities held at least a year are treated more favorably, as are qualified dividends (as opposed to ordinary, non-qualified dividends).

The more gains you have, the lower the potential value of your taxable dollars. An equity purchased for $100 and worth $100
is currently worth more to you than an equity purchased for $10 and now worth $100. There are methods to avoid taxes on those gains, but some are not pretty (death) and some could be eliminated with a change in the tax code.

How can taxable dollars be as good as Roth dollars? A few conditions have to be met, but it is possible.

First, you must have a taxable income that keeps you in the 0% long term capital gains / qualified dividend tax bracket, which is about $77,000 for a couple in 2018 — a feat easily achieved by an early retiree.

Second, the investment must not spin off ordinary dividends or short-term capital gains. Passive index funds are good choices to meet these criteria. Growth stocks tend to pay fewer dividends, and Berkshire Hathaway famously pays none. Finally, your state of residence must treat gains the same way the federal government does. Not all of them do.

52% of our dollars are taxable dollars.

Tax Deferred Dollars

The final category contains your least valuable dollars. Monday dollars. While you have every reason to put as much as you can into tax deferred accounts when you earn a physician’s salary, the dollars won’t be worth as much as those above when it comes to retirement.

These dollars have not yet been taxed, but when accessed in retirement, you can bet your bottom dollar that they will be. These dollars can be held in a variety of numbered and acronymed accounts, each of which behaves a bit differently, but they all have one thing in common: income tax will apply.*
Unfortunately, many retirees will have most or nearly all of their dollars in tax deferred accounts. This isn’t an inherently bad problem, particularly if the balances are sufficiently large, but if you’re relying solely on tax deferred dollars to fund your retirement, your dollars won’t go as far as any of the other dollars we’ve discussed. If your total tax in retirement is 15% to 25%, your tax deferred dollar is worth 75 to 85 cents.

17% of our dollars are tax-deferred dollars.

Other Dollars

I’ve ignored other dollars thus far because I’ve already accounted for 100% of our retirement dollars. Other dollars would include pensions, which is a complicated topic recently covered by the Financial Samurai.

He frequently discusses real estate, too; we do not own investment real estate, but there are ways to own real estate or real estate funds in all of the account types listed above. We currently have a handful of investments in crowdfunded real estate in our taxable account. You can also hold real estate investments in a self-directed IRA.

Annuities can also be held inside and outside of retirement accounts. Cash value life insurance is something I have stayed away from and probably doesn’t deserve my attention (or yours).

Social Security is a benefit we Americans who have worked our 40 quarters can expect to collect at some point. I’m nearly 30 years away from collecting if the rules remain constant over those three decades. I have no idea how to value this benefit with so much time remaining. I expect we will receive a benefit and will treat it like an added bonus when the day
finally comes.

**Are My Dollars Worth More Than Your Dollars?**

Probably. With more than 80% of my retirement dollars residing in post-tax accounts, I’m in pretty good shape. If the situation were inverted, and more than 80% of my retirement dollars were living in tax-deferred accounts, those dollars simply wouldn’t go as far in retirement. The latter is a common situation. Certainly, some of you will have an even higher percentage in Roth and taxable accounts. You win! Someone will always have a higher income, a nicer home, a more ideal asset location ration, or a better behaved dog. Actually, the vast majority of you probably have a better-behaved dog, if you have a dog.

**So what?**

I don’t think we need to go to any great length to devised a formula or conversion factor for the different types of dollars we have. There are just too many variables. Even if the tax laws stay forever unchanged – they won’t – our circumstances will change. I could pay between 0% and 40% on the dollars I withdraw from tax-deferred accounts depending on what happens in coming years. Income can change, deductions
will graduate and leave the nest, even **gasp** filing status can change.

I do think it’s worthwhile to consider where your money is, and understand the relative value of your different dollars. Sometimes, I think we should shoot for a specific dollar amount before making drastic changes in our work/life balance. When I stop and think about our 25x (or 36x = financial freedom), I realize that the absolute number isn’t all that important, anyway. So now we’re shooting for a specific date.

What are you aiming for? Do you discount tax-deferred or other dollars when calculating your retirement assets or net worth? I’d love to hear your thoughts.

*Strategies exist to make Roth conversions while avoiding federal income tax*. You must have low expenses and/or a substantial amount of other dollars to spend in order to employ this strategy, and will only be able to convert a relatively small amount annually, but it is possible.
The Taxpayer Relief Act of 1997 reestablished Individual Retirement Arrangements (IRAs) and created Roth IRAs for the first time. Due to Congressional rules, both traditional IRAs and Roth IRAs had income limits that prevented high-income professionals from deducting traditional IRA contributions, from contributing to Roth IRAs at all, and from converting traditional IRAs to Roth IRAs. The 2006 Tax Increase Prevention and Reconciliation Act included a change in just one of these rules, the prohibition on Roth IRA conversions. However, that change did not actually take effect until 2010. A few wise people quickly realized this would allow for an indirect process whereby a high-income professional could start contributing to Roth IRAs and some even began funding traditional IRAs for 2008 and 2009 in preparation of a 2010 conversion.

Personally, my income was low enough in 2008 and 2009 that I could still contribute directly to Roth IRAs for my spouse and myself, so my first “Backdoor Roth IRA” was in 2010. We have
done it every year since. In January 2019, we will fund a Roth IRA for the 10th time via that same indirect or backdoor process. In celebration, I thought it would be worth stepping back for a minute and considering what has been learned from this.

(Contribution limits are for 2019)
How A Backdoor Roth IRA Works

Some are still not familiar with the Backdoor Roth IRA despite it being widely used now for a decade. It is basically a four-step process.

Step one is to make a contribution to a traditional IRA. If you are under 50, you can contribute $5,500 per year ($6,000 in 2019). Those over 50 can contribute $6,500 ($7,000 in 2019.) You can also contribute to a separate IRA for a non-working spouse. A high-income professional with a retirement plan available at work is not allowed to deduct this contribution.

Step two is to do a Roth conversion of the traditional IRA you just established, basically moving the money from the traditional IRA to the Roth IRA. A Roth conversion is a taxable event, but in this case, the tax cost is $0 because the basis of the traditional IRA is equal to its value. Put more simply, you don’t have to pay to convert those dollars because they have already been taxed.

Step three is to ensure that you have no money in a traditional IRA, SEP-IRA, or SIMPLE IRA as of December 31st of the year you do the conversion. This is to prevent a “pro-rata” calculation that the IRS requires on Roth conversions. You can learn more about the calculation by looking at line 6 of IRS Form 8606. Existing tax-deferred IRAs must be either rolled into a 401(k) or also converted to a Roth IRA (which may add a significant tax bill for the year.)

Step four is to make sure the tax paperwork is filled out correctly. Both amateur and professional tax preparers frequently make errors on Form 8606 or fail to file it at all.

Tax Reduction Strategies Spread Slowly

One of the more interesting lessons we’ve learned from the
Backdoor Roth IRA is just how slowly tax strategies like this spread. Bloggers, online financial forums, financial advisors, accountants, and financial journalists have been writing about this strategy for over a decade now, yet many who should be funding Roth IRAs indirectly still don’t know about the strategy.

**Tax Diversification Is Useful**

Another important lesson here is that tax diversification is useful. If a retiree has money in tax-deferred accounts, tax-free accounts, and non-qualified (taxable) accounts, she has a great deal of control over her tax situation in retirement. Tax-free withdrawals from a Roth IRA are particularly useful, both for the retiree and her heirs, and perhaps the best way to ensure a sizable Roth IRA in retirement is to make regular Roth IRA contributions throughout her working career and invest them aggressively.

**Backdoor Roth IRAs Are A No Brainer**

There are other methods of building a Roth IRA for tax-free retirement withdrawals, including contributions to Roth 401(k)s and Roth conversions of previously untaxed dollars from 401(k)s, traditional IRAs, and similar tax-deferred retirement accounts. However, both of these methods require
the payment of taxes that otherwise would not be paid. Pre-paying these taxes may still be the right financial move, but in both cases, a careful calculation and evaluation of your situation should be made. In contrast, a Backdoor Roth IRA is essentially a no-brainer. Since a high earner cannot take a deduction for the traditional IRA contribution, and investing the money in a taxable account leaves the money exposed to creditors and taxes as it grows, there is no reason to avoid putting that money into a Roth IRA, via the backdoor.

No Waiting Period Required

A lot of people, including some financial professionals, were concerned for many years that the IRS might apply the “Step Doctrine” to this indirect Roth IRA contribution process. The Step Doctrine is a concept occasionally employed by the IRS that if the sum of a number of steps is illegal, the process is illegal even if each of the steps is legal. It’s easy to see why one might worry this could apply to the Backdoor Roth IRA process. Due to this fear, many advisors actually advocate waiting for some period of time (weeks, months, sometimes a year or more) between the contribution and conversion step, or worse, recommended against doing it at all. However, despite thousands of investors doing this every year (and reporting it to the IRS on Form 8606) the Step Doctrine was never applied. Finally, in 2018, the IRS issued clarification that no waiting period was required, essentially giving the Backdoor Roth IRA their blessing. Unfortunately for those who never funded their Roth IRAs or complicated their tax paperwork and ran up the tax bill on the Roth conversion step by leaving the money in the traditional IRA for lengthy periods of time, there was no going back.

[Update prior to republication: Note that since they converted their IRAs to brokerage accounts a couple of years ago, Vanguard seems to make people wait a couple of days for the contribution to “clear” before allowing the conversion.]
It is also clear that Congress should simply eliminate the Backdoor Roth IRA process completely by allowing high earners to contribute directly to a Roth IRA. Those who know about it are doing it anyway and it is bad public policy to allow significant tax breaks only to those who are very familiar with the tax code. This is costing taxpayers additional money paid to tax preparers and financial advisors. In addition, it causes taxpayers to make decisions they otherwise would not. Self-employed individuals who wish to use a SIMPLE or a SEP-IRA for the sake of simplicity are forced to either establish a 401(k) or miss out on Roth IRA contributions. Taxpayers with existing IRAs are forced to roll that money back into a 401(k) or miss out on continuing to fund Roth IRAs. Those without an available 401(k) may end up doing Roth conversions that would otherwise be inadvisable. Congress should stop wasting our time and money and allow direct Roth IRA contributions.

Click To Tweet
Funding a Roth IRA indirectly has helped high-income investors
meet their financial goals and achieve tax diversification now for a decade. It’s time for Congress to simplify the process.

What lessons have you learned from doing a Backdoor Roth IRA? Comment below!

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**From 28 Funds to 3: Simplifying to a Three Fund Portfolio**

[Editor’s Note: The following post originally appeared on WCI partner site, Physician on FIRE, and shows how simple and cost-effective do-it-yourself investing can be.]

In real life, I don’t talk about money with many people, but there is one retired couple that I discuss dollars with rather freely. In recent years, as I’ve broached the subject of early retirement, they’ve taken a little more interest in what I’m doing, and have taken a closer look at what they’ve been doing. As you might know, I am a Do-It-Yourself (DIY) investor. The man in the couple I’m talking about is a DIY master in many ways. He repairs things. He designs things. He builds things. Then he remodels them. He built a complete 24’ by 30’ workshop for the sole purpose of building more things. Above that workshop, he built an efficiency apartment,
complete with dormers, a kitchen, and bathroom. It’s quite a place. But he’s never been a DIY guy when it comes to money. He understands it well and taught me some valuable lessons over the years. He was a business owner and had to hire someone to manage his businesses’ retirement plan for him and his employees. After retiring, his retirement savings continued to be managed by the same financial advisor.

Which Advisor Would You Choose?

In the six or seven years since he retired, the company that managed his money was sold or merged with another company two times, but he kept the same advisor whom he had grown to trust. Rather abruptly this fall, his advisor resigned, and he was offered two new names from which to choose.

How do you choose an advisor? You can meet face-to-face with each and develop your own set of criteria. Do we share the same vision? Will he consider my input? Does he have enough gray hair? Do we share the same alma mater and root for the same teams?

Actually, a better place to start is by looking up the names on BrokerCheck by FINRA. That is what this particular gentleman did. Guess what? Neither of the two names had a clean record. One had been terminated for “VIOLATION OF A
PROVISION OF THE FIRM’S COMPLIANCE POLICIES AND PROCEDURES.” I didn’t use ALL CAPS for emphasis – that’s just how FINRA states it.

The other (I’ll spare you the lengthy ALL CAPS) listed the following allegation: “Customer complaint alleges unsuitable purchase and sale of annuities resulted in undisclosed surrender charges and unforeseen tax obligations resulting in damages of approximately $37,000.”

Which advisor would you choose?

A Look at the Retirees’ Portfolio

In the past, I had casually mentioned to the couple that it wouldn’t be too difficult for them to manage their own nest egg if they had any interest. It would also save them some money, of course. How much? Well, we didn’t really know until we took a closer look at his current investments and fee structure.

The portfolio under the microscope consists of two tax-deferred IRAs and a joint taxable account. Fees consisted of the expense ratios of the funds, and a management fee that was believed to be 0.5%, which is what it was when they signed on.

Browsing through the 3/4” thick packet from their most recent
biannual meeting, we could see that the management fee (which was 0.5% six years and two companies ago) was now 0.73%. Funny — there was no recollection of that fee increase ever being discussed.

This is what they had in each of the accounts:

- **IRA 1** had 3.5% of the assets and held **16 different funds**.
- **IRA 2** held 83.8% of assets in **22 funds**.
- The **taxable account** held 12.6% of the assets in **10 funds**.

Since there was some overlap, altogether they held **48 positions in 28 different funds**. Let’s take a look at the details.
I determined the overall allocation to be roughly 47% US stocks, 14% International stocks, and 39% bonds. I would consider that an appropriate asset allocation for a couple that would expect to live another 15 years based on actuarial tables, but possibly 20 to 30 years based on current health and family history.

I would also consider that to be a really complex and costly way to manage a 60 / 40 portfolio. I showed them my portfolio, and I shared with them these links on the three fund portfolio:

<table>
<thead>
<tr>
<th>Fund</th>
<th>IRA 1</th>
<th>Taxable</th>
<th>IRA 2</th>
<th>Total</th>
<th>E.R.</th>
<th>Type</th>
</tr>
</thead>
<tbody>
<tr>
<td>PASDX</td>
<td>0.41%</td>
<td>2.04%</td>
<td>10.07%</td>
<td>12.51%</td>
<td>0.45%</td>
<td>80% Bond 40% Stock - 20% cash</td>
</tr>
<tr>
<td>BAGSX</td>
<td>0.29%</td>
<td>1.41%</td>
<td>6.26%</td>
<td>7.96%</td>
<td>0.55%</td>
<td>Bond</td>
</tr>
<tr>
<td>MDDVX</td>
<td>0.37%</td>
<td>6.98%</td>
<td></td>
<td>7.35%</td>
<td>0.93%</td>
<td>US Stock</td>
</tr>
<tr>
<td>MPGFX</td>
<td></td>
<td>6.80%</td>
<td></td>
<td>6.80%</td>
<td>0.65%</td>
<td>US Stock</td>
</tr>
<tr>
<td>FINSX</td>
<td>1.57%</td>
<td>3.96%</td>
<td></td>
<td>5.53%</td>
<td>0.66%</td>
<td>US Stock</td>
</tr>
<tr>
<td>BSBSX</td>
<td>0.26%</td>
<td>0.92%</td>
<td>4.25%</td>
<td>5.43%</td>
<td>0.55%</td>
<td>Bond</td>
</tr>
<tr>
<td>CMIDX</td>
<td>0.16%</td>
<td>1.05%</td>
<td>4.14%</td>
<td>5.35%</td>
<td>1</td>
<td>US Stock</td>
</tr>
<tr>
<td>AEGFX</td>
<td>0.36%</td>
<td>4.83%</td>
<td></td>
<td>5.19%</td>
<td>0.86%</td>
<td>International</td>
</tr>
<tr>
<td>HCAIX</td>
<td>0.33%</td>
<td>4.04%</td>
<td></td>
<td>4.37%</td>
<td>1.01%</td>
<td>US Stock</td>
</tr>
<tr>
<td>FFRHX</td>
<td>0.07%</td>
<td>0.73%</td>
<td>3.07%</td>
<td>3.87%</td>
<td>0.7</td>
<td>Bond</td>
</tr>
<tr>
<td>OAKIX</td>
<td></td>
<td>3.66%</td>
<td></td>
<td>3.66%</td>
<td>1</td>
<td>International</td>
</tr>
<tr>
<td>EVBLX</td>
<td></td>
<td>3.60%</td>
<td></td>
<td>3.60%</td>
<td>1.03%</td>
<td>Bond</td>
</tr>
<tr>
<td>CVSTX</td>
<td>0.10%</td>
<td>0.44%</td>
<td>2.74%</td>
<td>3.28%</td>
<td>1.11%</td>
<td>40% US Stock, 10% Bond, 50% Alt</td>
</tr>
<tr>
<td>AFIFX</td>
<td>0.26%</td>
<td>2.93%</td>
<td></td>
<td>3.20%</td>
<td>0.67%</td>
<td>US Stock</td>
</tr>
<tr>
<td>FDRXX</td>
<td>0.16%</td>
<td>2.97%</td>
<td></td>
<td>3.13%</td>
<td>0.26%</td>
<td>Bond (Cash Reserve)</td>
</tr>
<tr>
<td>PSAX</td>
<td>2.86%</td>
<td>2.86%</td>
<td></td>
<td>1.04%</td>
<td></td>
<td>Bond</td>
</tr>
<tr>
<td>TWEIX</td>
<td>2.58%</td>
<td>2.58%</td>
<td></td>
<td>0.94%</td>
<td></td>
<td>US Stock</td>
</tr>
<tr>
<td>VASVX</td>
<td>2.41%</td>
<td>2.41%</td>
<td></td>
<td>0.39%</td>
<td></td>
<td>US Stock</td>
</tr>
<tr>
<td>VBR</td>
<td>2.29%</td>
<td>2.29%</td>
<td></td>
<td>0.08%</td>
<td></td>
<td>US Stock</td>
</tr>
<tr>
<td>WIAEX</td>
<td>2.02%</td>
<td>2.02%</td>
<td></td>
<td>1</td>
<td></td>
<td>80% US Stock, 20% International</td>
</tr>
<tr>
<td>APIXX</td>
<td>1.56%</td>
<td>1.56%</td>
<td></td>
<td>0.37%</td>
<td></td>
<td>Bond</td>
</tr>
<tr>
<td>MIDAX</td>
<td>1.45%</td>
<td>1.45%</td>
<td></td>
<td>1.33%</td>
<td></td>
<td>International</td>
</tr>
<tr>
<td>ODMAX</td>
<td>0.05%</td>
<td>1.30%</td>
<td></td>
<td>1.35%</td>
<td>1.32%</td>
<td>International</td>
</tr>
<tr>
<td>JSOSX</td>
<td>0.27%</td>
<td>1.00%</td>
<td></td>
<td>1.27%</td>
<td>0.68%</td>
<td>Bond</td>
</tr>
<tr>
<td>WAAEX</td>
<td>0.17%</td>
<td>0.53%</td>
<td></td>
<td>0.70%</td>
<td>1.22%</td>
<td>US Stock</td>
</tr>
<tr>
<td>ACITX</td>
<td>0.14%</td>
<td>0.14%</td>
<td></td>
<td>0.47%</td>
<td></td>
<td>Bond</td>
</tr>
<tr>
<td>VOF</td>
<td>0.12%</td>
<td>0.12%</td>
<td></td>
<td>0.08%</td>
<td></td>
<td>US Stock</td>
</tr>
<tr>
<td>FCASH</td>
<td>0.01%</td>
<td>0.01%</td>
<td></td>
<td>0</td>
<td></td>
<td>Cash</td>
</tr>
</tbody>
</table>

Totals: 3.53% 12.63% 83.84% 100.00% 0.64
I offered my assistance in making a transition if they were interested, and gave them some time to mull it over.

They didn’t need much time.

When they came back to get the ball rolling, I showed them one more link and told them what I’d been up to in my spare time over the last year. That was a fun “reveal”.

The Proposed Fidelity Three Fund Portfolio

All three existing accounts (two IRAs and a taxable account) were with Fidelity. While I have mine with Vanguard, I had read about the recent lowering of fees in Fidelity’s index funds. Indeed, when I did my own discount double-check, the fees were a hair lower at Fidelity. I also realized the
transition would be a bit quicker and uncomplicated by sticking with Fidelity. Furthermore, Fidelity has branches you can walk into, staffed by humans at desks, and you can sit across from them.

We decided to remain with Fidelity.

Our goals were to keep a similar asset allocation, rebalancing to 45% US stocks / 15% International stocks / 40% bonds using these three funds:

- FSTVX — Total [US] Market Index Fund
- FTIPX — Total International Index Fund
- FSITX — US Bond Index Fund

Another primary objective was to reduce fees. Based on the existing average expense ratio of 0.64 and a management fee of 0.73%, their current fees were nearly $22,000 per year.

Switching to a three-fund portfolio using passive index funds to arrive at our desired allocation would bring the total annual fees under $1,000 per year, a savings of $21,000 per year. Of course, that $21,000 would be well spent if returns outpaced the indexes by at least 1.5% a year. The odds of that happening, and happening repeatedly, are exceedingly small.

Glancing through the investment performance packet, their portfolio had returned 2.2% over a trailing three year period net of fees. The same paperwork showed the S&P 500 returning 8% over that time frame (although it was actually 8.7% with dividends reinvested). International funds and bonds were relatively flat, but a 45 / 15 /40 mix would have returned between 4% and 5%, which looks pretty good compared to 2.2% (or 3.6% before fees).

This is what the proposed portfolio looked like.
We started with a call to Fidelity. The representatives were quite helpful, guiding us through the process of opening new accounts and transferring the money from the managed accounts to the newly created accounts. All of the mutual funds remained the same during the transfer.

Once the funds were in the new accounts, the fun began. I was the token oblivious loud guy on his cell phone you see on television. BUY! SELL. SELL! BUY! YES! MORE FSTVX! I was doing it with a mouse and computer, and no one was listening, but I barked out the orders just the same.

Some funds could be exchanged for new Fidelity funds. Others had to be liquidated to cash in the account followed by purchases of the new Fidelity funds. Some settled more quickly than others. I logged in daily for about a week to mop it all up.

<table>
<thead>
<tr>
<th>Fund</th>
<th>IRA 1</th>
<th>IRA 2</th>
<th>Total</th>
<th>E.R.</th>
</tr>
</thead>
<tbody>
<tr>
<td>FSTVX</td>
<td>3.5%</td>
<td>41.5%</td>
<td>45.0%</td>
<td>0.045</td>
</tr>
<tr>
<td>FTIPX</td>
<td>12.6%</td>
<td>2.4%</td>
<td>15.0%</td>
<td>0.11</td>
</tr>
<tr>
<td>FSITX</td>
<td>40.0%</td>
<td>40.0%</td>
<td>80.0%</td>
<td>0.05</td>
</tr>
<tr>
<td>Totals</td>
<td>3.5%</td>
<td>12.6%</td>
<td>83.9%</td>
<td>0.058</td>
</tr>
</tbody>
</table>

In the IRAs, we did not have to consider tax consequences. The taxable account was less straightforward. For better or worse,
there were actually a number of funds with capital losses.

It’s *worse* because we did this with the market at record highs, and most of these funds had been held for some time. I was not expecting to see losers. It’s *better* because we were able to take some losses to offset the gains, exiting most of the mutual funds with minimal tax consequence.

In the end, we were left with two mutual funds with mostly long-term gains of about $15,000 between the two. To sell would trigger a taxable event to the tune of at least $3,000 due to capital gains and state income tax. They’re not particularly bad funds, and there may be an opportunity to unload them *tax-free* in the future, so we decided to leave them alone.

**The Actual Portfolio Today**

This is what the portfolio looks like now.

<table>
<thead>
<tr>
<th>Fund</th>
<th>IRA 1</th>
<th>Taxable IRA 2</th>
<th>Total</th>
<th>E.R.</th>
</tr>
</thead>
<tbody>
<tr>
<td>FSTVX</td>
<td>3.5%</td>
<td>37.4%</td>
<td>40.9%</td>
<td>0.045</td>
</tr>
<tr>
<td>FTIPX</td>
<td>9.2%</td>
<td>5.8%</td>
<td>15.0%</td>
<td>0.11</td>
</tr>
<tr>
<td>FSITX</td>
<td>40.2%</td>
<td>40.2%</td>
<td></td>
<td>0.05</td>
</tr>
<tr>
<td>AIFIX</td>
<td>2.3%</td>
<td>2.8%</td>
<td>0.67</td>
<td></td>
</tr>
<tr>
<td>FNSX</td>
<td>1.1%</td>
<td>1.1%</td>
<td>0.66</td>
<td></td>
</tr>
<tr>
<td>Totals</td>
<td>3.5%</td>
<td>12.7%</td>
<td>100.0%</td>
<td>0.081</td>
</tr>
</tbody>
</table>

**Not bad, eh?**

That looks like a portfolio that can be managed by a *Do-It-Yourselfer*. The original portfolio before we tore it apart? That looks like something only a professional should mess with. I think that’s the point. It looks extraordinarily complicated, and it is, but it needn’t be. If it looked a whole lot easier, the professional wouldn’t be necessary.
Armed with a little knowledge and a willingness to stay the course through good times and bad, the individual can do this on his or her own. Of course, the typical investor can underperform the market due to behavioral factors (buying high, bailing low), so there is a role for recommended professionals for those investors who don’t have the knowledge or the fortitude.

The $22,000 in fees previously lost to the advisor and the fund companies represent at least a quarter of this retired couple’s annual spending. For every three or four dollars they spent as retirees, one dollar went to their advisor. And that’s considered normal and acceptable. I don’t like it.

Frankly, I’d be willing to bet the portfolio’s balances could be substantially larger if they hadn’t been nibbled at a little every year while they were growing. Remember, investment fees will cost you millions.

How can 1.4% in fees be so costly? Think of it this way. If you’re planning on the portfolio returning 3% to 5% with a conservative allocation to preserve capital, once you subtract the fees, you’re left with 1.6% to 3.6%. A sustainable withdrawal rate of 4% doesn’t look so safe after awhile.

With the new allocation, we didn’t quite get down to a three-fund portfolio, but nearly 97% of the portfolio is in one. We also weren’t able to get the expenses down to 0.058% or under $1,000, but we’re not that far off with a weighted ER of 0.081 and annual expenses of about $1,300.

I’d say we did pretty well.

For further reading on the three fund portfolio, check these out:

- He Has Read Over 250 Investing Books. He Recommends These Three Funds.
What do you think? Do you like the three fund portfolio? What did you think of the 48 fund portfolio? Why do advisors try to make things so complex? Comment below!

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**What is the Best Month to Buy a House?**

(Editor’s Note: The following was submitted by author, podcaster, mortgage lender, and long-time WCI advertiser, Josh Mettle. Josh specializes in financing physicians, dentists, CRNAs, and other professionals with highly specialized professional loan programs. Josh is also a fourth generation real estate investor and owns a number of rental homes, apartment units, and mortgages. This would have been a great post to run a couple of months ago, but better late than never. We bought our current home in October of 2010, and I was amazed at how much less competition there was compared to Summer 2006 when we bought our previous one. While there may be fewer homes on the market in the Winter, there are dramatically fewer buyers, so you will typically get more attention from your realtor, more time to make your decisions, less competition and probably a better price. In this piece, Josh gives you some tips on taking advantage of the fact that you’re buying in the Winter.)
The holidays are upon us, and more often than naught, prospective home buyers are putting their decision to purchase a new home on pause until Spring.

Who can deal with all that stress during the holidays? I get it, buying a home during the winter can be a little more challenging, even uncomfortable to pack up and move during the holidays when our tendency is to slow down the pace and relax a little.

If that resonates with you, then you can see why December and January are the absolute best months of the year to negotiate and purchase a home. The competition is enjoying the holidays and not out hitting the streets house hunting. The lack of buyers leads to longer listing times for sellers and more listings expiring without being sold.

The lack of holiday showings and offers make sellers more willing to negotiate the sales price of the home and/or give a concession towards your closing costs (which you can use permanently buy-down your interest rate).

For most of the country, we are still seeing solid real estate appreciation, but the winter months in many markets are the exception. I’ve copied the FHFA Home Price Index through September 2018 below, you can see most of the country (especially the Mountain region) is still in an uptrend of
housing prices. Meaning that in most situations the seller is in control because there are still plenty of willing buyers.

However, in most states, buyer activity slows in the winter and sellers no longer have the advantage. In Utah for example, we have a pretty predictable season of appreciation from March through September, followed by flat or even negative appreciation throughout the winter months.
The soft winter season is precisely when you can get the best price and lowest overall cost for your home and mortgage. Let me show you how!

**Three Ways You Can Save Money as a Winter Home Buyer**

1) **Offer Below The Asking Price**

Yes, this is elementary, but take a moment to think about the seller’s psychology at this point. They likely don’t want to sell in the winter, something urgent is likely driving the sale. Who knows what that could be, a divorce, job relocation, children not doing well at school, etc. Whatever the situation, know that no seller wants to have their home listed for sale over the holidays, so something is driving them to need to sell before spring.

Now to further add to the anxiety of the seller, keep in mind that home listing times can double or even triple in the winter. So that seller likely has an urgent reason to sell and is seeing low activity and very little happening, further adding to their motivation to be flexible to you the holiday buyer.

When your low offer comes in, most selling agents are going to
advise their sellers to consider the low offer because it might cost them less than continuing to hold the property until the summer buying season heats up. Needless to say, sellers are going to be much more likely to consider a below listing price offer in winter.

2) Ask The Seller To Cover Your Closing Costs

As interest rates have continued their ascent throughout 2018, mortgage rate increases are adding more to the total cost of homeownership than the home price increases most of the country has seen through the year. Most buyers don’t understand they can reverse the higher interest rate effect by employing a seller paid permanent interest rate buy-down strategy.

Let me show you an example, this is a Total Cost Analysis I created for a client who was considering making a low offer on a home. The client’s ultimate goal was to have the lowest overall payment and the Total Cost Analysis illustrated that using the seller’s funds to permanently buy-down the interest rate on the loan was three hundred percent more effective at reducing the payment than was a price reduction.

The first column below shows the market rate (based on their credit profile) and the full asking price of the home, which was four hundred thousand. This scenario resulted in a payment of $1,939.94 per month, which was above this client’s top qualifying amount.

The second column shows the same sales price with the seller paying nine thousand towards the buyer’s closing costs, which we used to buy-down the interest rate and decrease the payment to $1,801.60.

The third column shows a price reduction of thirty thousand dollars, which at the market rate (based on their credit profile), equated to the same payment as the nine thousand
dollar interest rate buy-down.

In this scenario, the client needed a payment closer to $1,800 a month to qualify and the seller was flexible but not thirty thousand dollars flexible.

Using the seller paid buy-down strategy, not only made the transaction work for the client and seller, but it also ended up saving the buyer $27,568 in interest over the life of the loan (below). It ended up saving both the buyer and the seller a substantial amount of money. The seller paid buy-down strategy is a true win-win that few understand and even fewer are utilizing to its potential.
3) Negotiate Repairs To The Property Or An Escrow Holdback

Keep in mind the psychology of the seller this winter, there is a little desperation in many markets. They need to sell or they would not be listing over the winter, they are seeing fewer buyers and even fewer offers. They are feeling a little like the guy on the dating app who keeps getting swiped left (what’s wrong with me and my house?).

This is an opportunity to be bold and to ask for as much as your local market will bear.

The last strategy is to ask the seller to address any and all repair items that your home inspector finds. Ask your home inspector to be aggressive and to find everything down to the caulk around the windows and bath that needs to be repaired. Then negotiate with the seller to fix these items found on the inspection report.
Most lending institutions will require the seller to complete these items prior to close but there are several whom will allow an escrow hold back, where the seller contributes money from the sales price into an escrow account and the work can be completed post close of escrow. If your lender does not offer this, look around, they are out there.

House hunting in the snow and during the holiday rush might not be as fun as house hunting in May with the spring sun on your face, but that’s exactly why you should be doing it. Running against the herd is never easy, but that is exactly why you should be considering house hunting and making offers in December and January, which are hands down the two best months to negotiate and receive the best terms from the seller.

When do you think is the best time to buy or sell a house? Comment below!

Legal disclosures: Fairway Independent Mortgage Corporation. NMLS#2289. 4801 S. Biltmore Lane, Madison, WI 53718, 1-877-699-0353. Other restrictions and limitations may apply. Equal Housing Lender. Disclosures Josh Mettle’s NMLS # 219996
Real Estate Investing Without the Hassle

[Editor’s Note: This post was originally published on WCI Network partner, Passive Income, MD. Like many of you, I love real estate as an asset class for its high returns and low correlation with stocks and bonds. And I hate the real estate market due to its inefficiency and characteristics as a second job. So anytime I can maximize the upsides and minimize the downsides, I become very interested. NNN leases are a way to decrease the hassle of owning an individual property because the tenant becomes responsible for most of the hassle and cost of maintaining the property.]

You don’t know how many times I’ve heard something along these lines from fellow physicians, “I’d love to own a real estate investment property but I don’t want to be called in the middle of the night for plumbing issues. It’s too much of a hassle.”

If this resonates with you, then a great solution for you might be investing in something called a Triple Net Lease (NNN) property. To help me explain what that is, I’ve decided to write this post in more of a question-answer type format.

What is a Triple Net Lease (NNN)?
A triple net lease is a commercial property in which there is most commonly a single tenant and that tenant is responsible for taking care of any and all issues.

So they take care of “the three nets”:

Net #1 – Property Taxes
Net #2 – Insurance
Net #3 – Maintenance

That means that you as the owner will not get called to unclog a toilet in the middle of the night or deal with monthly utility bills. The tenant is responsible for all of that. Typically there isn’t rapid turnover, so you don’t have to worry about re-renting often and you won’t get called about tenant battles like one tenant playing his music too loud late at night.

Hopefully, you’re seeing that it requires very little management. Essentially all you have to do is basic bookkeeping, file tax returns every year, and make the big decisions like when you want to refinance, sell or exchange the property. This makes it very attractive for owners, particularly those that aren’t in the same location or state.
What Are the Typical Returns and Are There Any Risks?

Because these are considered steady, safer-type investments, returns typically are expected to run in the 5-9% annual return range.

Sounds amazing, right? However, just like in any investment there are risks. The main risk is that the single tenant vacates before the term is up or goes out of business. A good number of these leases are written for 20+ years with slight escalations in line with inflation. So you want to make sure you choose reputable companies in good locations that will be around a while.

What Are Some Examples of Triple Net Tenants?

Common triple net lease property examples are pharmacies (Walgreen’s, CVS), the Dollar Store, Gas Stations, Banks, etc.
How Much Capital Do I Need To Invest in a Triple Net Lease Property?

The difficulty with purchasing reputable triple net leases is that they can be relatively capital intensive, ie. expensive. There are smaller triple net leases that are very reasonable however it’s not uncommon to see the property a Walgreen’s sits on in a good location go for 4-5 million dollars plus.

How Do I Invest In Triple Net Properties?

Do It Yourself

You can absolutely purchase these properties on your own. Leases will typically be in place but you can always hire someone to help handle the lease situation.

Where can you find some of these properties? Ask around and look for agents who specialize in these types of properties. Call any commercial brokerage and they can direct you to someone. You can also look on Loopnet for properties and to get an idea of what the current market looks like.

Invest through Funds and Crowdfunding

There are specialized funds that focus on NNN leases and diversify your risk by creating a portfolio of NNN leases. I like to think of it as a mutual fund that focuses on purchasing stock in NNN leases.

You can find these funds on your own or you can utilize real estate crowdfunding platforms to find them on occasion.

I know of one crowdfunding company in particular that
specializes in NNN leases. It’s interestingly named, Rich Uncles. It’s founded by the chairman of the largest commercial real estate company in the country, CBRE. Apparently, he’s the “Rich Uncle” we all wish we had.

They have a fund or REIT that basically only invests in NNN leases. You don’t need to be an accredited investor, minimums are $500, and after a year, the investment can be liquid. Historically they’ve returned monthly dividend payouts around 7% with an expected annual return of 12% over 5 years. Again, though, returns aren’t guaranteed but they seem to choose very conservatively and don’t take on a huge amount of leverage. You can check them out here.

**Summary**

Overall, Triple Net Lease properties may be a very good option for physicians or anyone who wants to invest in real estate, but would rather not deal with the headaches of active management. Sounds pretty passive to me.

*Does this sound appealing to anyone? Does anyone have experience with triple net leases? Would love to hear about it.*
Why Aren’t You Doing What You Recommend?

[Editor’s Note: Just a reminder that the CityVest deal discussed on the blog last Friday only lasts through the end of the year. If you missed that post, this is basically a chance to get into a private multi-family real estate fund with only a $25K minimum. More details at the blog post link above or this affiliate link. Remember how affiliate links work- if you invest after going through my link I get paid, although it doesn’t cost you any more to go through that link.]

A few months ago Jonathan Clements asked this question on Twitter:

If you were advising your neighbors, what portfolio would you recommend they buy? So why don’t you own that portfolio yourself?

6:17 AM - 19 Jun 2018

3 Retweets 14 Likes
It’s a good question, and one I had previously spent a lot of time thinking about, particularly once a year when I rebalance my parents’ portfolio, which is markedly simpler than my own, especially prior to the simplifications we made in our portfolio a year or two ago. To give you an idea what I’m talking about, here’s what my parents’ portfolio looks like:

- Total Stock Market 30%
- Total International Stock Market 10%
- Small Value 5%
- REIT Index 5%
- TIPS 20%
- Intermediate Bond Index 20%
- Corporate Short Term Bond Index 5%
- Prime MMF 5%

Eight asset classes, four equity, and four fixed income. It used to be seven until Prime MMF went to a yield of basically 0% for years and we split a 10% allocation to it and put some of it into short-term bonds to chase yield a little.

Meanwhile, ours looks like this:

- US Stocks 40%
- International Stocks 20%
- Real Estate 20%
- Bonds 20%
Just kidding. Kind of. I mean, those are the major divisions in our portfolio, but I’ve totally ignored the minor ones. You see, my parents own eight asset classes and only eight mutual funds. Katie and I have far more investments than them, and I often wonder if I should just be doing with our money what I do with theirs. That was part of the impetus for our portfolio simplification a couple of years ago. At any rate, even after the simplification (where we dropped P2P Loans, Large Value, Emerging Markets, Mid-caps, and microcaps), ours looks like this:

- Total Stock Market 25%
- Small Value 15%
- Total International 15%
- International Small 5%

Syndicated Real Estate Equity Deals, Funds, and Websites 10% (8 holdings as I write this)
- Syndicated Real Estate Debt Deals and Funds 5% (8 holdings as I write this)
- REIT Index 5%
- TIPS 10%
- G Fund 8%
- Intermediate Muni Fund 2%

So, in answer to Clement’s question, how can I justify investing differently than I recommend? I can think of four different reasons:
# 1 I Don’t Have a Single Recommendation

First of all, I refute the premise in Mr. Clement’s tweet. To be fair, he started his statement with “If” and it’s just a tweet, so nobody should take it too seriously, but my recommendation is for people to pick a reasonable portfolio that they can stick with through thick and thin. So I guess he isn’t even talking to me in the first place. When people ask me for a portfolio recommendation (and they do a lot) I tell them they need a written plan to follow and provide resources to help them develop one, from free blog posts, to an inexpensive online course, to a recommendation for a financial planner. If they just ask what I think of their portfolio, I label it either “reasonable” or “not reasonable.” I certainly follow my own recommendation to have a reasonable portfolio.

# 2 Multiple Investing Accounts

I have another problem that keeps me from having the same portfolio I might recommend to a neighbor. I have a different set of investment accounts than they do. For example, someone investing mostly in taxable is likely to have a very different set of investments from someone whose entire portfolio is in one employer’s 401(k). You have to adjust for that.

# 3 Access to Investments

Do as I say, not as I
On a related note, I have access to investments that others may not have. For example, through my old TSP from my military days, I have access to mutual funds with sub 0.03% ERs and the “free lunch” G Fund, basically a money market fund paying 3.00% (at time of writing, Vanguard Prime MMF is paying 2.35% and was paying much less just a few months ago). Also, as an accredited investor, I have access to investments that others do not have access to. That doesn’t mean those investments are always better than those available to everyone, but at least I have the chance to consider them. In addition, thanks to my level of wealth, I am able to get cheaper expense ratios on mutual funds and the minimums on accredited investments allow me to invest in them without significantly impacting the diversification of my portfolio. Like a realtor or real estate attorney might have access to some really great properties, I have access to some really great websites that are only available to me as an investment due to my inside knowledge of the industry.

# 4 I’m an Asset Class Junkie

I think the first person that I heard describe himself as an asset class junkie was Bill Bernstein. I fall into the same camp. If I think I’ll get even a little bit of benefit out of moving from seven asset classes to ten, I’ll do it. That said, I personally think three asset classes should be your minimum and I see a real benefit in moving from three to seven with limited benefit in moving to ten. Beyond ten, the additional complexity likely costs more than it is worth. I don’t know that I need more complexity in order to stay the course and avoid my urge to tinker, but my willingness to tolerate significant complexity certainly differs from that of my neighbors.

I personally think three asset classes should be your minimum
and see a real benefit in moving from three to seven with limited benefit in moving to ten.

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# 5 I’m Willing to Gamble on Non-Conventional Asset Classes

Some asset classes have been around for decades or even centuries, while others may be relatively brand new. I’m willing to take a chance on an unproven asset class with a small percentage of my portfolio. Is there an element of gambling there? Probably. But it’s a gamble I can afford and that I can tolerate if it doesn’t work out. I think financial advisors and knowledgeable DIY investors are often hesitant to recommend these sorts of investments to others because of their new and unproven results, even if a careful analysis indicates likelihood of significant profit. I’m just not going to recommend that my neighbors try to invest in physician financial websites, but they’re my best investments.

# 6 I Can Stay the Course Better Than My Neighbors

Having invested through a couple of bear markets, including one rather large one, I’m pretty familiar with my own risk tolerance. My neighbors may not even know what risk tolerance is, much less be able to determine their own. I know how I feel about tracking error; they likely do not, and even if they do, it may be different than mine. For example, my parents really didn’t want more than 10% of their portfolio (20% of equity) overseas, whereas I am very comfortable with 20% (33% of equity). The bottom line is my ability to take risk is likely significantly higher than theirs, which allows me to invest differently than they do.
# 7 Invest in What You Understand

On a related note, one of the primary tenets of investing is to only invest in what you understand. The more investments you understand, the more investments are available for you to select from in building your portfolio. You certainly don’t need to invest in everything to be successful; there are no called strikes in investing. But this is another good reason why I might invest differently from what I would recommend for someone else.

Despite these objections and justifications, I think Mr. Clement’s point is very clear and should be carefully considered by all investors. What’s good for the goose should be good for the gander. Just like you should have a very good reason to invest in anything besides an index fund you’d better have a very good reason to invest differently from what you might recommend to someone else. There’s a reason investors like to see their advisors and money managers “eating their own cooking.”

What do you think? Is it acceptable to invest differently from what you might recommend for someone else? Why or why not? Comment below!
In this episode I speak with a young periodontist.
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NML
Quote of the Day

Our quote of the day
day to day comes from Morgan Housel, who said,

"A hard reality is that what of the
n matters most in finance will never win a Nobel Prize: humility and room for error
Periodontics

We talk a lot about periodontics at the beginning of this episode. The training path is four years of college, four years of dental school, one year of general residency, and three years of a periodontist residency. When I asked him if this residency was one which paid you or one which you paid tuition for? He said it was a little bit of both. On the general practice residency, you get a little bit of a stipend, so you end up with a net positive but not by much. Certainly within the specialty programs on the dental side, a big part of what makes some programs more competitive versus others is what that ratio is. In his case, he had tuition but also had a stipend, so it was essentially a wash. It didn’t quite cover all the living expenses, but you weren’t in the hole a huge amount every year. Dramatically different from being a medical resident, where you’re getting paid $50-60,000 a year. He was fortunate because some postgraduate residencies you are paying $70-80,000 a year in tuition.

I asked what the range of incomes a periodontist can expect coming out of training is and he thought $180-$200,000 range is about a reasonable starting salary but within the first couple years you’re expecting it to increase as you have a larger active patient base and you’re quicker and have more experience talking to patients. Average income reported by the ADA is somewhere in the $250,000 range or a little bit higher.

So what does a periodontist do?

Everything essentially around the teeth. A lot of gum grafting around natural teeth or people who have active periodontal disease, taking care of that. A lot of times when patients are
getting more complex rehabilitations done on the prosthetics side, there is adjoining periodontal work as well, incorporates dental implants and associated procedures like bone grafts and things along those lines as well.

His wife is a prosthodontist. A specialty that basically covers restorative aspects of dentistry. She has more specific training in more complex rehabilitation work.

I asked if these are like some of the other residencies, like orthodontics, where it’s the top 10% of the class are the only people that can get into them, or are they less competitive than that. He thought all the specialties tend to skew towards the top of the class but probably the most competitive specialties to get into would be oral maxillofacial surgery and orthodontics.

**Debt Free**

Now on to his finances! This periodontist has been out of training for just a couple of years. He had about $150,000 in debt because he had some family help to get through school and training and his wife has a scholarship to pay for part of her schooling. But they purchased a condo in the city where he did his residency and that debt pay off amount included that mortgage. Pretty impressive!

He did something very unusual for doctors. He put everything toward the debt as he came out of training. Most people have had this deferred gratification for years and years, in his case, 12 years since he started college, and feel like maybe the world owes them something. You’re a doctor and now you want to spend something. But he didn’t do that. Why?

“Honestly, I think that is one of the most powerful messages you get from a group like the White Coat Investor. Not only the podcast, hearing it from the book, but just having a community of people around you. I think for me, a couple of
my close friends have done a pretty good job on the financial side as well, one of whom is a dentist in the local area that originally got me onto your information. I think just hearing that and knowing that other people are doing that, you see the reason as to why you would want to get some of the debt paid off versus jumping into some of the stereotypical things. I think the ones that I tried to avoid as best as possible was purchasing a home, so holding off on that for a little while, and the cars. I figured if I could do those things, I could give up on some of the smaller things at different times and still be okay.”

I think that’s exactly right. You just have to remember the big rocks is where you make the big difference.

Variable Universal Life Policy

He hired a financial advisor who was the daughter of one of his patients. She immediately tried to sell him a variable universal life policy, saying,”term insurance is actually the more expensive way to go because you’re just paying for the insurance and then the insurance goes away, where with this policy, there’s a cost of the insurance, but if you override it by a significant amount you’re going to have significant tax benefits within the policy. So it’s better for you to put all of that money in the policy versus just getting term insurance and then putting the money into the taxable account.”

Sounds like the classic sales lines that she gave him. I think part of it is most of the people selling it really do believe what they’re telling you. The problem is they just don’t have the financial background to really compare it to your alternatives. And the actual situations where it makes sense to use a variable universal life policy as another retirement account are pretty limited.
Even at physician and dentist incomes, certainly anywhere near the averages, it’s very hard to make a case for this sort of a policy. For the most part, these are getting sold to people that still have student loans, that aren’t maxing out their retirement accounts, and to make matters worse, the policies often aren’t even a good policy.

A variable universal life policy is not quite the same as a whole life insurance policy. There is lots of guarantees in whole life. Now, the returns are really pretty low. Even if you hold onto it for 50 years, it’s probably projected to have a return of around 5% a year, with a guaranteed return around 2% a year. But there’s a certain number of guarantees in there that they provide.

With a universal life policy, there’s a lot fewer guarantees, and with a variable universal life policy, instead of this money being invested by the insurance company and then they basically decide what they’re going to pay out as a dividend each year, you actually get to pick the investments from what’s available within the policy. So there are lots of available investments, and they’re basically mutual fund-like, is probably the best way to think about the sub-accounts in a variable universal life policy. The problem is they’re often lousy mutual funds inside these policies. It’s not unusual to have an expense ratio that’s basically 2%, which would be a terrible, terrible mutual fund. I see a lot of people that are kind of like this doctor and run into what sounds like a not very experienced advisor who’s recommending one of these, and the one they’re recommending is just the one the company they’re associated with has, or that pays the greatest commission, and isn’t even a good VUL policy.

I think if you’re one of those rare people for which this sort of thing makes sense, you have to have a really good policy. It definitely doesn’t make sense at any time if it’s a lousy policy, and so if the funds that are in it aren’t Vanguard index funds and DFA kind of funds, if you’re stuck with lousy
mutual funds, basically, inside it, it’s never going to work out well.

I hate seeing this sort of thing get pushed to somebody, especially at the beginning of their career when they have so many other competing needs for their limited cash. It might be a home down payment, buy a practice, pay off student loans, start maxing out retirement accounts. Most of us come out of training with a beater, and honestly, it’s okay to upgrade a car at some point in those first few years, and we just have all these needs for cash, and all of a sudden now we’re tying it up in some big fat permanent life insurance policy premiums. That’s the problem.

Firing Your Financial Advisor

This advisor’s name is Lauren, and she said to him, making a joke, “No load, no Lauren.” Thankfully he was like, “Okay, I don’t think that this is the fit. You know, I think we have a slightly different view.”

What she’s saying is, “I am a commissioned salesman. I make money when you buy things. If you buy annuities, if you buy a variable universal life policy, if you buy loaded mutual funds, that’s how I get paid for my advice.”

The problem with that is that Lauren faces, every day of her career, this terrible conflict of interest where she has to look at something and say, “Do I do what’s right for this person’s finances or do I do what pays me the most?” I think even good people can’t resist that for decades on end. It’s just asking too much, even of very good people.

The other problem is, I think the advisors that aren’t as educated about it, less likely to have relevant certifications, less experienced, the ones who have had most of their training in sales rather than any sort of financial planning or investment management, are the ones who are more likely to be in that model, so I think not only do you end up
paying for this terrible conflict of interest, and sometimes paying a lot for it, especially if you buy some huge VUL policy, but you end up with worse quality advice, so it’s just a bad thing all around. Your are a lot better off going to a fee-only advisor than really dealing with a commissioned agent.

There are times when we have to buy stuff for which people are paid on commission, and that is okay. You go buy a car at the dealership, that guy gets a commission, but when you walk in the door, you know the guy is trying to sell you every upgrade on there, he’s trying to sell you the most expensive car on the lot. He’s not pretending that he’s giving you unbiased investing advice, unbiased car-buying advice, and so you know what he is when you walk in there.

I think it’s the same way if you need to buy some term life insurance, you know that agent’s going to get a commission. If you need disability insurance, you know the agent’s going to get a commission. It’s the same with a lot of things that you buy, a lot of financial products, but I think it’s important to realize the difference between a salesman telling you about their product and unbiased financial advice.

When people need advice, my mantra is, “Good advice at a fair price,” and the fair price is more than a lot of people think at first. It’s going to be a four-figure amount, for unbiased advice. There is no price too low for bad advice, so the most important thing is to get good advice and then work on getting it at a fair price.

When people need advice, my mantra is, “Good advice at a fair price,” and the fair price is more than a lot of people think at first. It’s going to be a four-figure amount, for unbiased advice. There is no price too low for bad advice!

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Umbrella Policy

We discussed several of the insurance policies this periodontist has in place. For the life insurance, he basically has three policies. One at 20 years, one at 15 years, one at 10 years. The idea is that as he get further along a financial path, that he will need less and less term insurance. I think this is a good way to handle it. For most docs is a seven-figure amount they will want for term life insurance. One to five million, somewhere in there.

For his umbrella policy he has 1 million. Mine is 2 million. I may up it a little bit, but the key to an umbrella policy is to have a seven-figure amount. These things aren’t that expensive. They’re $200-500 a year, and you want to have a seven-figure amount, because you want, if something bad happens, you want the insurance company on the hook for enough money that they’re going to send you very good representation. You want to get their best attorney defending you from whatever it is you’re being accused of.

I don’t know that you can get that for the $50,000 that a lot of people are carrying around on their auto insurance policies. That might be the minimum in your state. About 80% of the umbrella policy claims are auto-related. Most of these, it’s like extra auto insurance for your liability when you run into somebody that’s worth a lot.

I keep seeing people trying to relate the amount of umbrella insurance to their net worth. Like if you’re a net worth of a million, you need a million in umbrella insurance. If you’re a net worth five million, you need five million in umbrella insurance. But there is no reason I can think of to put those two numbers together. There’s no relationship there. The only relationship you have is between the liability and the amount of insurance you have.

Having more doesn’t necessarily give you additional liability.
I suppose it makes it a little more easy to afford a more expensive policy, but the truth is is you need enough for whatever the claim’s going to be, so if you get a $2 million claim, you need $2 million. If you get a $20 million claim, you need 20 million. It doesn’t do a whole lot of good if you have $2 million in net worth and $2 million in liability coverage if you get a 20 million claim against you. You’re just as bankrupt as if you didn’t have the policy in the first place. So I think the key is a reasonable amount, and I’ve defined that as one to five million.

**Disability Insurance**

Here is the take away from our discussion on his disability insurance policy. Get rid of it once you don’t need it anymore. I see little reason to carry this thing to the grave for a couple of reasons.

1. It is expensive. Most of us are spending thousands a year on disability insurance, and that money can be used for other stuff. That’s the number-one reason why you want to get rid of it.

2. If you’re financially independent, if you have enough money to live the rest of your life, you don’t need to insure your income anymore. It just doesn’t make sense to keep the policy. Insurance is not a profit-making enterprise for you. The only person making profit off the insurance is the insurance company, and that’s because they can charge you enough that they can cover all their expenses, make all the payouts they need to, and still have a little bit left over for profit. Any time you don’t need insurance, you probably shouldn’t be carrying it.

3. The last reason is because these policies only pay until you’re 65 or maybe 67, and so if you’re 61, you’re still paying the same amount in insurance that you were paying at 35 for 30 years of coverage for only four years of
coverage. It’s only going to pay for four years, so the closer you get to retirement, yes, the more likely you are to be disabled, but also, the less you’re going to get paid out from it. At a certain point, you got to go, “This just isn’t worth it anymore.” I think for a lot of people, that happens in the late 50s and 60s.

Buying the House vs the Practice

This periodontist wanted to talk a little bit about some considerations when purchasing your doctor home and a practice.

He has a high savings rate currently in anticipation of these two purchases. For dentists getting into practice ownership in most scenarios, not always, but in a lot of scenarios, improves your ability to earn money. You want to get to the point where you can take out a loan so you can go and purchase a practice, because that may increase your income by 30%. Most banks want to see somewhere in the range of 5 to 10% of the purchase price of a practice in some form of a liquid account, if at all possible, so they’re hoping to see it outside of your 401(k) and that sort of thing.

The biggest consideration on his mind is that for most dental people, although they want to get the home first, they should actually get the practice first. Typically when a dentist or
dental specialist purchases a practice, it is a decision to anchor down in that area, more so than a home would be. When you’ve bought that practice, the likelihood that you’re going to move, unless something major happens, is pretty unlikely. The purchase of a practice is probably going to cost more than the house. He points out,

“I think the big consideration there for young doctors is making sure that we have the ability to certainly get enough leadership and management training so that we can take on a practice like that, but the big thing is making sure that we can get the loan, because there’s a lot of, I think, young dentists who want to purchase a practice that aren’t going to necessarily be given a loan for it. Some of these practices go for 1.5, $2 million. It’s not uncommon to have a large practice selling for that amount, and so getting ourselves in a financial situation where a bank would be willing to lend you that money is the biggest consideration there.”

I think what happens is people come out of school with half a million dollars in student loans, and then they get a half million-dollar mortgage, and then they try to get a half million-dollar loan for the practice, and then just, at a certain point, they go, “You want all this on an income of 150,000?” It’s just not going to happen.

Remember a house is mostly a consumption item. Yes, there’s some investment aspects. You get the saved rent is a dividend, and maybe the house will appreciate, so in some ways it has some investment aspects, but for the most part a big fat doctor home is a consumption item, and the practice is actually increasing your income, so it’s an investment more so than a consumption item. I think it’s important to buy the investments before you buy the consumption items.
Biases in Recommending Courses of Treatment for Patients

He wanted to discuss biases that sometimes lead us to recommend courses of treatment for a particular patient, saying,

“You’re very retrospective in thinking about the biases that other professionals have. I felt like if we’re going to do that for a financial advisor, I think we should put the microscope on ourselves in the same way.”

He points out most dental professionals are paid a percentage on what the practice collects. A number of things will vary on that. What procedures are done, how often they’re done, what the practice has the ability to bill for, whether in the fee-for-service model or some type of an insurance plan, all in some way, shape, or form affect the dentist income.

“As a young doctor, I feel there is definitely a temptation to do additional types of treatment for financial gain. Again, everybody has their own biases, but I do think that that’s one of those things that comes up, I think, more often, I don’t think that patients or other health care providers are necessarily aware of.”

I think for sure the medical side is more insulated from this because of the role of health insurance. It’s all so opaque. We don’t even know the prices of half the stuff we’re prescribing or tests we’re ordering.

I think dentist do face that conflict of interest much more readily than a physician does. It’s staring them in the face every day, and just like for a commissioned salesman that we were talking about earlier, you’ve got that temptation all day long that you have to resist to do the right thing for the patient, and only the right thing.
We have to realize that we have a duty to the patient that we’ve sworn, and it’s a duty not just to their health but also to their pocketbook, is quite frankly the way I look at it. It’s very difficult in medicine, though, because you literally cannot find out the price for a particular treatment for a particular patient in their insurance plan. Insurance really mucks it up quite a bit.

In dentistry he feels it is not necessarily that treatment gets truly over-treatment planned, it’s more that each specialty just have their slant towards what their background and their training is. That is maybe the most common bias that tends to come out. Not necessarily something bad for patients per se, but just that if you were a general practitioner versus being a periodontist versus being an oral surgeon, you would probably prioritize some treatment slightly differently in some scenarios.

I asked him what he personally does, knowing that he is only a couple years out of residency and nowhere near financial independence, still with lots of cash flow needs? What does he do personally to keep from over-prescribing or over-treating?

Separating the day that they do the examination from the time that they actually make treatment recommendations helps, so you can really go back and think about when and why you’re going to recommend treatment. Really going back and reviewing the evidence, saying, “Which treatments are truly needed?” and having criteria set for different classifications of things really goes a long way to eliminate some of that bias.

But he feels,

“a lot of it is just having conversations with the practitioners that we’re working with on the case to see if there are other needs that are out of our purview, what are they and how urgent are they and how do we make sure that other work gets done as well? Even if it’s not necessarily
something that we’re going to do, we just want to make sure that it makes the most sense for the patient. So I think the split time between the initial exam and the recommending of treatment for most patients is actually the most helpful thing.”

We have to realize that we have a duty to the patient that we’ve sworn, and it’s a duty not just to their health but also to their pocketbook.

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Needs vs Wants in Your Dream Home

“I think you’ve hinted on some podcasts before about minimalism and decluttering and really prioritizing just the things that you need versus the things that society says you want. You’ve owned a couple of homes. We’re going to be purchasing a home and, at some point, having kids. What would your recommendations be on how to prioritize the things that you truly need in a home that you’re going to make a lot of use out of versus the things that look really nice when you’re buying the fancy doctor home that you won’t necessarily use a lot of?”

Good question. I think it’s important to realize that upfront, that almost everything you’re talking about is a want and it’s just what you want the most. But I’ll tell you what, I’ve got a lot of space in my basement. This place is 4,400 square feet on three floors, and the only thing I ever come down to this basement for is to record podcasts. I don’t need 1,500 square feet to record a podcast. I think being careful how much you really want and need down the road is probably my best advice, just because every square foot you buy has to be furnished and carpeted and painted and insured and heated and cooled and landscaped and so on and so forth. So sometimes I think we get
these big eyes at what we really think we want, and two or three years from now we’ll feel a little bit differently about.

Debt vs Investing in Your Business

Our guest asked a good question for a friend. The friend has everything paid off except for the debt on his practice and primary residence. He is maxing out all his available tax-deferred things. He wanted to know if he’s got additional money, where do I recommend it go? Do you just blast money into the taxable account? Do you do equipment upgrades or do you do debt pay down?

I think in this sort of a situation, it’s not clear. When you’ve got 30% credit cards, there’s an obvious answer to the debt versus invest question. When you aren’t even putting enough money into your 401(k) to get the match, you’ve also got a definite answer to this question. The rest of the time you’re in some sort of a gray zone.

Some things to consider, like the interest rate and whether you’ve got other tax-advantaged accounts available to you, but assuming you don’t, and your question is really, “Do I take a guaranteed 4% paying down on my mortgage or my practice loan, or do I invest in taxable and hope to do better than that?” There’s no right answer there, and sometimes the right thing to do when you’re not sure what to do is just split the difference, which is perfectly reasonable as well. It does take away the power of focus a little bit. If you were focused completely on the debt, you’d probably pay it off a lot faster, but it’s a reasonable thing to do either way, to pay on the debt, to invest, or to do both at once. So no totally right answer there.

He mentioned equipment upgrades, though. If there are equipment upgrades you can do that will boost your income, I view that as a pretty good investment. Investing in yourself
and your practice is oftentimes the best thing that you can do with a dollar if it’s something that’s actually going to earn you more money. I would definitely look into that first before investing in a taxable account or paying down 4% debt.

**Budgeting**

I asked him what advice he has for the WCI community, what has he learned that he wants to pass on? His answer:

“\textit{I think the biggest, the most helpful thing, the most important thing you could do would be to track your spending. Get on Mint or something along those lines and be very intentional about what your spending is and don’t relate that to the level of income. I think of any tool or anything along those lines, that probably made a bigger impact than anything.}”

Good advice.

**Ending**

I hope you enjoyed this look into
so
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finances
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found
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to
apply
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your
life
Would you have answered differently? If you have questions you want answered on
Intro: This is the White Coat Investor Podcast, where we help those who wear the white coat get a fair shake on Wall Street. We’ve been helping doctors and other high-income professionals stop doing dumb things with their money since 2011. Here’s your host, Dr. Jim Dahle.

WCI: Welcome to White Coat Investor Podcast #85, The Real-Life Financial Experience of a Young Periodontist. If you’re like many of your peers, your heart probably drops each time you see how much you owe on medical school loans. But it doesn’t have to be this way. You don’t have to live life with high payments or high interest. CommonBond lets doctors take their old, expensive medical school loans and trade them in for one at a lower interest rate, which can save you thousands over the life of your loan.

WCI: You’re also protected by an industry leader in borrower protections, because life is unpredictable. You’ll have an award-winning service team helping you every step of the way, and the commitment-free application will show you your savings
in two minutes. As a member of the WCI community, you’ll get a $500 bonus when you refinance with CommonBond. Apply today at www.whitecoatinvestor.com/commonbond to lock in your savings before interest rates go up. CommonBond is a licensed lender, NMLS #1175900.

WCI: Thanks so much for what you do. Your work is important. I know it’s not always appreciated and it’s not always easy and you train for a long time to do it, and sometimes it feels like you’re not making any progress against your student loans or against becoming financially independent. But keep fighting the good fight. You can do it, and there’s a lot of people out there to support you here in the White Coat Investor community.

WCI: So don’t be afraid to reach out if you’re struggling and if you’ve been having a hard time of it lately. There are people in your situation. I know sometimes it seems like everybody’s got all their financial ducks in a row. I assure you, they do not. I wish I could give each of you a quick peek into my email box just so you would know you’re not alone in what you’re struggling with.

WCI: Make sure you sign up for the newsletter if you haven’t. You can do this by going to whitecoatinvestor.com/free-monthly-newsletter/. It’s totally free to you. You get the 12 Financial Boot Camp emails for free that come with it, and you can get updates on the blog and on the podcast and the free monthly newsletter that I send out that includes all kinds of good information like a market report and an update on what’s going on around here at the White Coat Investor, as well as two special things, one of which is a list of the best stuff on the web for high-income professionals that’s been published in the previous month, and the second thing is a blog post that isn’t published anywhere else. It’s basically, I call it the Monthly Tip, but the only way to get it is to sign up for the newsletter, so make sure you do that if you haven’t yet.
WCI: Our quote of the day today comes from Morgan Housel, who said, “A hard reality is that what often matters most in finance will never win a Nobel Prize: Humility and room for error.” Today we’re going to be doing something a little bit unique on the podcast. We’ve done something similar before, but it’s always fun to get a regular reader on here, even if they want to remain anonymous, and learn a little bit about their life and get a glimpse behind the scenes, so that’s what we’re going to do today.

WCI: All right, we have a special guest today on the White Coast Investor Podcast. I’m not actually going to tell you his name, though. This is a regular listener we’ve brought on. We’re going to talk about some of his successes and some of his struggles now, given where he’s at in his career, and maybe not put out too much identifying information for him, but enough that you can identify with him and maybe find some help with some of the things you’re struggling with and find the inspiration that will help you to reach your financial goals. So, welcome to the podcast.

Periodontist: Thanks so much for having me, Jim. I really appreciate it.

WCI: Tell me a little bit about your schooling and career, just so people know where you’re at.

Periodontist: Sure, yeah. Grew up, went to undergrad, and then as far as my dental training, I did both dentistry and my specialty is periodontics, so I had four years of additional training, did a general practice residency for one year, and the specialty is an additional three years, and that’s where I met my wife as well. She was doing a sister program in prosthodontics, and so we’re both within our selected specialties. So I’ve been practicing back where I’m from now for about two years.

WCI: So you’re training path is four years of college, four
years of dental school, one year of general residency, and three years of a periodontist residency. Is that correct?

Periodontist: That’s right.

WCI: Was this residency one which paid you or one which you paid tuition for?

Periodontist: You get a bit of both. On the general practice residency, it ends up being a little bit of a stipend, so you end up with a net positive but not by much. Certainly within the specialty programs on the dental side, a big part of what makes some programs more competitive versus others is what that ratio is. In our case, we had tuition but we also had a stipend, so it was essentially a wash. It didn’t quite cover all the living expenses, but you weren’t in the hole a huge amount every year.

WCI: But dramatically different from being a medical resident, where you’re getting paid 50 or $60,000 a year.

Periodontist: Oh, for sure. Yeah. Like I said, the salary’s somewhere in the … If I had to go back, maybe 40,000 for the year, but you have tuition as well. Yeah, I know a lot of people on the medical side are shocked by that, but there are some postgraduate residencies where you’re paying 70, $80,000 a year in tuition.

WCI: What’s the range of incomes a periodontist can expect coming out of training?

Periodontist: Yeah, I think for a periodontist starting out, from what I’ve heard, it seems like the 180 to $200,000 range is about a reasonable starting salary, but like a lot of things, I think, in dentistry or medicine, within the first couple years you’re expecting it to increase as you have a larger active patient base and you’re quicker and you have more experience talking to patients.
Periodontist: Average income, I think, reported by the ADA is somewhere in the $250,000 range or a little bit higher. I know a lot of those statistics are skewed down because a lot of them are practice owners, so that’s reportable income. I would think that average income would probably be somewhere around $300,000 range, but again, there’s a pretty wide variation.

WCI: What do you do every day? What does a periodontist do?

Periodontist: I guess what I tell patients is that if you’re thinking about work in the mouth, we’re almost like a subcontractor, in a way. We’re doing everything essentially around teeth. If there’s something that you’re not going to see, typically we’re doing it. A lot of it is gum grafting around natural teeth or people who have active periodontal disease, taking care of that in terms of pocket reduction in a couple of different ways.

Periodontist: A lot of times when patients are getting more complex rehabilitations done on the prosthetics side, there’s adjoining periodontal work as well. Then we certainly incorporate dental implants and associated procedures like bone grafts and things along those lines into the practice as well.

WCI: Now, your wife’s a prosthodontist. Tell us, what does a prosthodontist do?

Periodontist: Prosthodontics is a specialty that basically covers restorative aspects of dentistry, but you just have more specific training in that area. There’s definitely a lot of gray area on the restorative side between what a general dentist can do, really, and what any of the specialties can do. But prosthodontics is probably the most closely aligned on a day-to-day basis. It’s just that you have specific training in more complex rehabilitations work.

Periodontist: For most people, if you just came out of dental school and started practice, you’ve never really done a full
mouth rehabilitation or done anything super complex. You’re either learning, if you’re continuing education courses or continuums, or you’re learning on the fly a little bit. Prosthodontics residency’s just more of a, I guess, regimented way to get some of that training.

WCI: Are these like some of the other residencies, like orthodontics, where it’s the top 10% of the class are the only people that can get into them, or are they less competitive than that?

Periodontist: No, I would say probably the most competitive of them is probably ortho. I think that to be into an ortho program you have to be at the top of your class. I think that all the specialties tend to skew towards the top of the class, but I would think probably the most competitive specialties to get into would be oral maxillofacial surgery and ortho. But again, all of them, I think, skew relatively high on the class rank.

WCI: Now, in medical specialties, there’s a stereotype for each specialty. The orthopedists are the jocks from college, and the emergency medicine people are the adrenaline junkies, and the radiologists and the pathologists are the antisocial, hide out in the dark kind of folks. Are there these stereotypes for the dental subspecialties?

Periodontist: No. No, I wouldn’t say so. I think the one ... If I had to rag on one of the specialties, I think it would probably be oral surgery, because I think those people tend to have, I would say, of the specialties, probably the biggest egos among them. Ironically, every person that was in my dental school class that went to oral surgery is actually both a really nice person and a really smart person as well, but if there’s anybody that’s got a bit of a god complex, I think it tends to skew towards that one.

WCI: Interesting.
Periodontist: But I wouldn’t say that every single specialty has those kind of things going with them.

WCI: So you are a couple of years out of your training, and you’ve already paid off $100,000 in student loans. Tell me a little bit, a couple of things, really. Let’s talk about how you got out of dental school, including a four-year residency afterward, with only $100,000, number one, and number two, how you paid it off so fast.

Periodontist: Really, the debt was a combined debt, so I’ve joined a family practice. Parents are in the dental field as well, so a big part of it was honestly family help. The only debt that I actually had coming out of dental school and residency was basically subsidized loans, and I think the total was about 34,000.

Periodontist: In my wife’s situation, dental school we’ll get to in a bit, and Mexico’s a little bit less expensive, but she had part of her specialty training paid for based off a scholarship from her hometown dental school, so about 50,000 of that was basically her training as well. So that was the dental school debt, and then one other aspect of debt that we paid off which we can get into as well is I was in a condo that I still own in the city where I did my residency and we actually paid that off, which had about 50,000 remaining as well. So the total debt paydown ended up being somewhere in the range of between 130 and 150,000.

WCI: So you paid that off while she was still in residency, because she just came out this year, correct?

Periodontist: Right, so those things were incremental. In my case, I knew that I had six months of a grace period to pay off the 34,000, and I was also making the least amount at that point as well, so pretty much everything went towards that for the first six months. That was actually probably the most gratifying debt that I paid off, because I knew that we were
striving towards a goal. When that one was paid off, it was pretty cool, but I never paid any interest on that loan. Then the other debts I was building up because I knew that they were coming up when she was going to be finishing her training.

WCI: Now, you did something that’s very unusual for doctors. You put everything toward the debt as you came out of training. Most people have had this deferred gratification for years and years, in your case, 12 years since you started college, and feel like maybe the world owes you something. You’re a doctor and now you want to spend something. But you didn’t do that. Why didn’t you?

Periodontist: Honestly, I think that that’s one of the most powerful messages you get from a group like the White Coat Investor. Not only the podcast, hearing it from the book, but just having a community of people around you. I think for me, a couple of my close friends have done a pretty good job on the financial side as well, one of whom is a dentist in the local area that originally got me onto your information. Periodontist: I think just hearing that and knowing that other people are doing that, you see the reason as to why you would want to get some of the debt paid off versus jumping into some of the stereotypical things. I think the ones that I try to avoid as best as possible was purchasing a home, so holding off on that for a little while, and the cars. I figured if I could do those things, I could give up on some of the smaller things at different times and you’d still be okay.

WCI: Yeah, I think that’s exactly right. You just have to remember the big rocks is where you make the big difference, for sure.
Periodontist: Right.

WCI: Now, your wife had an interesting pathway. Can you tell us about your wife’s pathway? You alluded to her studying in Mexico and how she ended up being able to practice here.
Periodontist: My wife is from Mexico. Small town in Mexico. It’s where her dental school was. Dental school in Mexico, you go straight from high school right into dental school, so it’s a six-year track instead of a four-year, but it combines some college with it and has an internship tag on the very end of it, and she got interested in prosthodontics when she was back in her hometown.

Periodontist: She had some family friends who were practicing in the States, working for a corporation here, and so she had gone and shadowed them and saw that she wanted to do it. Fortunately, she finished top of her class and got into the specialty and had a scholarship for it, so the three years of the prosth program, two of it was covered by a scholarship for her.

Periodontist: Then she finished that program. Again, we were in the accompanying classes the same year. Then for Florida, her specialty training doesn’t give her the equivalent of what would satisfy the license, so certainly she had to take part one and part two national boards to qualify for that, but she did that during her specialty training and then she did a two-year.

Periodontist: For the medical people, the easiest way to think about it would be like an internship. I’m sure some of the dental folks wouldn’t want to think about that, but it’s probably the closest comparison, I think, to the medical side of the world. So those two years basically showed two clinical years of general dentistry that were done, so that satisfies the equivalent of the second two years of a US dental training program, and so she just did that and then just took the state boards and then she just finished up and started in practice.

WCI: Now, are you all in the same family practice, or …

Periodontist: No, no, no.

WCI: She’s in a separate practice. Was that difficult for her
to get a job in the US, having gone to school in Mexico? Was there a prejudice there or what kind of issues did she run into with that?

Periodontist: No, actually, that didn’t seem to be too much of an issue, actually. She’s Spanish-speaking, which I’m in Florida, and so having a Spanish-speaking doctor is actually a huge positive in most situations. She’s working in a general practice. There just aren’t a lot of prosthodontists around, so unless you’re purchasing a prosthodontics practice, it’s difficult to truly get an associateship of one. There are people that do it, it’s just not that common.

Periodontist: So the fact that she had additional training and she was a Spanish-speaking dentist was always a positive. I think in terms of pay, though, most offices you’re going to get paid based off of the production that you produce in the office, so it’s not necessarily that they’re going to pay you more because you got the specialty training if you’re working at a general practice.

WCI: Where does prosthodontics stack up among the dental pay scales? Do they get paid like orthodontists? Do they get paid less than periodontists? What’s a typical prosthodontist make?

Periodontist: Prosth, again, is the smallest group of them, so data isn’t as easy to come by, but from what I’ve seen from the ADA data it seems like somewhere in the 200 to $250,000 range is the median, whereas perio probably runs in the 250 to $300,000 range in terms of the median once you’re up and running.

WCI: Let’s talk a little bit about some of this stuff, and listeners don’t know I’ve got some more information here in front of me from some email exchanges we had. I’m just picking and choosing from the information I have that I know about you, and they’re wondering how I know this information, but the reason why is I got some other information on the side
Tell us a little bit about how you selected your financial advisor and how happy or unhappy you are about that decision.

Periodontist: Sure. Thank goodness I read the book ahead of time to know, ironically, when you’re stuck in a bad situation. I think a lot of people, you just end up in a spot. In this case, I was talking with a patient at the time of the exam, and the patient mentioned that he moved down to Florida because his daughter was a financial advisor. It was right around the time that I had just finished paying off the debt. I figured, it’s about time that I get a financial advisor. I said, “Sure, I’ll go to basically an evening seminar.”

Periodontist: In this case, the seminar wasn’t particularly tailored towards young professionals. It was more like annuities and that sort of thing, but he said, “Look, come enjoy the dinner and meet her, and she can probably get you set up.” So that was originally how I met her, and then once you did you just get with one meeting and the next and the next, and it’s hard to break away. I think that’s actually going to be one of the things that I’m going to need to do here pretty quick.

Periodontist: I see I’m not that happy with her. We can get into some of the reasons why. I just don’t think that she knew a lot about physician-specific or dentist-specific finance and didn’t tailor the plan towards that.

WCI: Let’s get into that. Let’s talk about some things you’re not happy about.

Periodontist: Sure. I think one of the things, and I’m not sure how this stacks on the medical side, maybe you can help me with that, but I know on the dental side, I think a couple of things that are probably really important in the first couple years out, certainly paying down the debt is important,
and obviously I did that, but I also knew that if I had some kind of an emergency or something along those lines, I did have family that I think would have been able to help, and so I could put more money towards debt, not necessarily building liquid savings, and as quickly as some other people would.

Periodontist: I think another big aspect is building a baseline of liquidity, because for dentists, getting into practice ownership in most scenarios, not always, but in a lot of scenarios, improves your ability to earn money. So a lot of people who are in the dental-specific space will say, “Look, we want to get you to the point where you can take out a loan so you can go and purchase a practice, because that may increase your income by 30%, and if you can increase your income by a dramatic number, that’s much better returns than you’re ever going to get with an investment. So get yourself to a point where you can do that.”

Periodontist: Most banks want to see somewhere in the range of 5 to 10% of the purchase price of a practice in some form of a liquid account, if at all possible, so they’re hoping to see it outside of your 401(k) and that sort of thing. The thought process is that if you are cash loan negative for a period of time that you’ve got something that can float you by.

Periodontist: I would say that was one of the big pushes that I’ve been wanting to get to, because we knew that for my wife, maybe purchasing a practice would be something that might happen at some point in the next couple of years. Certainly, I think that her perspective was quite different. I think her thought process was not very physician- or dentist-specific. I think she pretty much just gave a plan ... I think the thought process was very, very simple, and I think it was just like, “You have more income than you’re spending. It’s beyond X number,” and so she just wanted to go into a life insurance product, like a permanent type of life insurance product.

WCI: Let’s talk about that. Let’s talk about the life
insurance product your advisor wanted you to get into, and have you made a decision about this yet?

Periodontist: Yeah. I think the decision that I’m going to do is I’m going to go to a different advisor pretty soon, so I think really just getting the recommendation. Really, a lot of these things have to be done before the end of the year, because we’re going to want to set up a 401(k) for my wife and an HSA, which we have the plan that qualifies for it. We’re going to have to get all of those things set and ready to go.

Periodontist: You can probably chime in a little bit more on the details. The policy was a variable universal life policy, and basically the way that she described it is that in a policy like this, she says that term insurance is actually the more expensive way to go, and she says the reason why is because you’re just paying for the insurance and then the insurance goes away, where with this policy, there’s a cost of the insurance, but if you override it by a significant amount you’re going to have significant tax benefits within the policy. So it’s better for you to put all of that money in the policy versus just getting term insurance and then putting the money into the taxable account.

WCI: Yeah, sounds like the classic sales lines that they give you to sell these to you. You know, I think part of it is I think most of the people selling it really do believe what they’re telling you. The problem is they just don’t have the financial background to really compare it to your alternatives and the actual situations where it makes sense to use a variable universal life as another retirement account are pretty limited.

WCI: Even at physician and dentist incomes, certainly anywhere near the averages, it’s very hard to make a case for this sort of a policy. For the most part, these are getting sold to people that still have student loans, that aren’t maxing out their retirement accounts, and to make matters worse, the
policies often aren’t even a good policy.

WCI: The thing with a variable universal life policy is it’s not quite the same as a whole life insurance policy. There’s lots of guarantees in whole life. Now, the returns are really pretty low. Even if you hold onto it for 50 years, it’s probably projected to have a return of around 5% a year with a guaranteed return around 2% a year. But there’s a certain number of guarantees in there that they provide.

WCI: With a universal life policy, there’s a lot fewer guarantees, and with a variable universal life policy, instead of this money being invested by the insurance company and then sent, and then they basically decide what they’re going to pay out as a dividend each year, you actually get to pick the investments from what’s available within the policy. So there’s lots of available investments, and they’re basically mutual fund-like, is probably the best way to think about the sub-accounts in a variable universal life policy. So you can sometimes compare them to mutual funds.

WCI: The problem is they’re often lousy mutual funds inside these policies. It’s not unusual to have an expense ratio that’s basically 2%, which would be a terrible, terrible mutual fund. I see a lot of people that are kind of like you and run into what sounds like a not very experienced advisor who’s recommending one of these, and the one they’re recommending is just the one the company they’re associated with has, or that pays the greatest commission, and isn’t even a good VUL policy.

WCI: I think if you’re one of those rare people for which this sort of thing makes sense, you have to have a really good policy. It definitely doesn’t make sense at any time if it’s a lousy policy, and so if the funds that are in it aren’t Vanguard index funds and DFA kind of funds, if you’re stuck with lousy mutual funds, basically, inside it, it’s never going to work out well.
WCI: But I just hate seeing this sort of thing get pushed to somebody, especially at the beginning of their career when they have so many other competing needs for their limited cash. It might be a home down payment, buy a practice, pay off student loans, start maxing out retirement accounts. Most of us come out of training with a beater, and honestly, it’s okay to upgrade a car at some point in those first few years, and we just have all these needs for cash, and all of a sudden now we’re tying it up in some big fat permanent life insurance policy premiums. That’s the problem.

Periodontist: Right. You literally hit it all. Like you said, we’re currently saving up for the down payment on the home. The practice purchase, we wanted to have liquid savings for that. My car is 12 years old. It has 120,000 miles on it, and I think we’ll probably wait until we have kids and switch to a different type of car at that point, but even with an older car that you’re planning to keep, you could end up with significant repairs on that sort of thing too. There’s a lot of competing uses for the money.

Periodontist: I think one of the lucky things was there were a couple of red flags with this financial advisor that went up pretty early. One of them was I mentioned even at the initial time we were going to start investing money into it that I was personally opposed to doing some type of permanent life insurance policy. She pitched also to my wife as well. I mentioned using Vanguard ETF and stuff like that.

Periodontist: This person’s name is Lauren, and she said, she literally made the joke, “No load, no Lauren.” That’s what she said for the ETF. I don’t mind paying somebody a fair amount for a fair amount of work, but I just want to know that there aren’t biases in the way, that this person is being compensated. I think that was really one of them.

Periodontist: Another red flag, and maybe because some other people will hear this in the pitch of life insurance, but I
think I was educated against, but I think could sound good to somebody who’s hearing it for the first time, was she said that she has clients who are in their 50s and 60s all the time that don’t need the insurance but feel they want the insurance, meaning that it never made sense. If you’re financially independent and your money, if you were to die, were to go to your heirs anyway, what is the point of having life insurance at that point? It just didn’t make sense to me.

Periodontist: But she literally used that as a pitch, and I was like, “Okay, I don’t think that this is the fit. You know, I think we have a slightly different view.” If anything, I want my life insurance that we’re going to be purchasing to go down as we get closer to financial independence, not for it to go up.

WCI: Sounds like she’s not that good at pitching it, honestly, but that’s probably a good thing for you. She basically told you right there, “No load, no Lauren,” right? What she’s saying is, “I am a commissioned salesman. I make money when you buy things. If you buy annuities…” That’s why she’s having the steak dinner, pitching annuities. “If you buy annuities, if you buy a variable universal life policy, if you buy loaded mutual funds, that’s how I get paid for my advice.”

WCI: The problem with that is that Lauren faces, every day of her career, this terrible conflict of interest where she has to look at something and say, “Do I do what’s right for this person’s finances or do I do what pays me the most?” I think even good people can’t resist that for decades on end. It’s just asking too much, even of very good people.

WCI: The other problem is, I think the advisors that aren’t as educated about it, less likely to have relevant certifications, less experienced, the ones who have had most of their training in sales rather than any sort of financial planning or investment management, are the ones who are more likely to be in that model, so I think not only do you end up
paying for this terrible conflict of interest, and sometimes paying a lot for it, especially if you buy some huge VUL policy, but you end up with worse quality advice, so it’s just a bad thing all around. I think you’re a lot better off going to a fee-only advisor than really dealing with a commissioned agent.

WCI: There are times when we have to buy stuff for which people are on commission, and that’s okay. You go buy a car at the dealership, that guy gets a commission, but when you walk in the door, you know the guy is trying to sell you every upgrade on there, he’s trying to sell you the most expensive car on the lot. He’s not pretending that he’s giving you unbiased investing advice, unbiased car-buying advice, and so you know what he is when you walk in there.

WCI: I think it’s the same way if you need to buy some term life insurance, you know that agent’s going to get a commission. If you need disability insurance, you know the agent’s going to get a commission. It’s the same with a lot of things that you buy, a lot of financial products, but I think it’s important to realize the difference between a salesman telling you about their product and unbiased financial advice.

WCI: I think when people need advice, my mantra is, “Good advice at a fair price,” and the fair price is more than a lot of people think at first. It’s going to be a four-figure amount, but unbiased advice, there’s no price too low for bad advice, so the most important thing is to get good advice and then work on getting it at a fair price.

Periodontist: Right, yeah. There’s one thing I could still say to the listeners here, is that I knew a lot of this information because I’d already read the book even when I went into those pitches. It’s a lot easier to hear it the first time than when you’re living through it, in terms of actually firing your financial advisor and all that sort of stuff. I know exactly what I need to do, and I think I will make that choice at this point, but it’s so much simpler just to go with
the flow on a lot of these things, and I think that’s where a lot of people, unless they really have a framework of people around them or they’ve really heard this information multiple times, will really pull away. I think maybe just beating the drum with anything will continue to help people make the right call.

WCI: Yeah. Let’s talk a little bit more personally about where you’re at financially in your life. You’re a couple years out of training. Your wife’s a few months out of training. Let’s talk about your income and savings rate and what you’re doing with your savings right now.

Periodontist: Sure. Yeah, it was interesting going back and looking at the overall savings rate. I guess I’ll start with the income. I think this is a very typical track for people coming out of residency. I was on base salary basically the first six months. My base salary was 180,000, so making about 90,000 for that first six months.

Periodontist: That was the time frame when I paid off the student loans. That was pretty much where everything went, so I wasn’t doing anything in terms of a backdoor Roth or anything at that point. I think, looking back, I probably could have.

Periodontist: And then in 2017, my income rose from what would be the equivalent of a base salary of 180 to about 260, $270,000, over the course of that year. That was really where I hinted that we were starting to get our savings together for a number of different things. Certainly, the payoff on the condo was part of that. Getting money ready for the payoff on my wife’s soon-to-be student loans was a big part of that. Saving for the wedding was part of that, and the engagement ring, and all that sort of stuff. My wife was going through the green card process of getting the attorneys and everything set up, for that was a big part of it.
Periodontist: Then since I was eligible at this point to begin a 401(k), I started the first two years as Roth contributions, but we started … I funded the 401(k) at the office fully, and then we did backdoor Roths, essentially. I know she could fund directly into traditional, but we did those that year as well.

Periodontist: Then I started to build some liquidity at that same time, and every time that we’ve had additional liquidity, because I’ve always heard people say that having too much liquid cash is a bad thing … Typically, when you’ve got a little bit of extra liquid sticking around, you usually have a good use for it. That’s at least what I have found in the first couple years out, is every time that I’ve had a little bit of extra cash, there’s always been a good place to put it, some kind of debt.

WCI: What percentage of your gross income in the last two years do you think has gone toward building wealth, either building up that cash buffer, going into retirement accounts, paying off debt? What percentage of it do you think it was?

Periodontist: Going back and looking at everything, it seems like the number’s between 30 and 40% total.

WCI: So 30 to 40%. That’s pretty good, considering you’re paying, what, 25% of it in taxes, something like that?

Periodontist: Right.

WCI: That’s about half of your net income, it sounds like.

Periodontist: Right, yeah. Obviously, right when I moved home I was literally living with my parents for the first year out of residency, and I kept costs pretty far down and avoided a lot of the big purchases, so I think that there was a lot of help there, but there’s no question it was a big priority to get some of that stuff taken care of so that we’d have the freedom to do things when it comes to purchasing a practice and whatnot down the line.
WCI: Are you glad you did it?

Periodontist: Yeah, for sure. It’s funny-

WCI: You don’t miss driving a Tesla?

Periodontist: You know, the person who introduced me to the White Coat, to the podcast and the book and everything, I was just talking with him this morning, and he actually just purchased a Tesla Model 3, and he’s happy with it, but he-

WCI: Hopefully he’s in a position that he can afford it.

Periodontist: He is, yeah. He’s paid off all of his debt except for, I think, his primary residence, and he’s done everything, I think, just right by the book. He’s got a long drive to and from work, and that’s what he wanted to do, and so I’m honestly just happy for him.

WCI: I hope he enjoys the Tesla. I’m not picking on Teslas. I’m only picking on buying Teslas when you can’t afford them.

Periodontist: Yeah. No, but obviously a lot of those things would be fun, and I think the biggest thing for people to hear while they’re still in residency, you’ve talked about this on past podcasts, is that paying down that debt, it’s not fun. I think the first 34,000 that I paid off, it was the first debt. I was really, really excited when I paid that one off, but even making what I think is a very fair income and having a lot of family help, it still took a while to get that stuff paid off, and when you’re just paying check after check after check, you’re putting it somewhere and it feels like it just evaporates into thin air. It’s tougher on the back side, and I had a relatively easy situation by comparison to what a lot of people have coming out now.

WCI: Yeah, a lot of listeners are going, “Only a hundred grand? How hard could that be?” Right?

Periodontist: For sure. A lot of people, I think, are coming
in with three, four, five, or in the specialty programs significantly more than that.

WCI: Yeah. We talked on a podcast a little while ago about somebody with over a million.

Periodontist: Sure, yeah.

WCI: It certainly can be much higher. Let’s talk about your insurance plan. What kind of insurances have you put in place in the last couple of years, and what insurance policies do you carry?

Periodontist: This actually will be interesting. Part of this, I may ask you a question on this too. I guess I’ll go with all the basic policies. Obviously we have renters’ insurance on the condo unit and auto insurance for us, and we have a high-deductible health insurance plan that we’re on a married plan at this point. Being in the dental field, my wife and I both have to have disability insurance and malpractice insurance.

Periodontist: One thing that’s probably unique to our situation with multiple doctors, and I’m not sure how common this is on the medical side, I’m sure it happens, do you guys use key man insurance? I’m sure there’s a different name for it.

WCI: No, I don’t think there’s another name, but it’s an important insurance for practice owners. The idea behind it is that if the practice owner becomes disabled the business doesn’t go under, so it’s not just a matter of keeping the doctor’s family going, it’s also keeping the practice going while you’re disabled. That’s the typical use for key man insurance, and it’s paid for by the business, and the nice thing about that is it’s pre-tax.

Periodontist: In our case, we have a policy like that, and the business is paying for half of it and we’re paying for half of it, so that’s an expense as well on our end of things. We do
have an umbrella policy, and then, let me think. Then I’ve actually got a couple of staggered life insurance policies.

Periodontist: I think the questions that I will end up having is, I actually asked the person who I was buying the umbrella policy, how do you choose how much? She really didn’t have a great answer. For the life insurance, I basically have three policies. One’s at 20 years, one’s at 15 years, one’s at 10 years. The idea is that as I get further along a financial path, that I’ll need less and less term insurance.

WCI: Yeah, and I like that idea. Let’s walk through each of these individually. Let’s first talk about an umbrella policy. How big’s your umbrella policy?

Periodontist: It’s 1 million at this point.

WCI: Mine’s 2 million. I may up it a little bit, but the key to an umbrella policy is to have a seven-figure amount. You know, these things aren’t that expensive. They’re 2 or 3 or 4 or $500 a year, and you want to have a seven-figure amount, because you want, if something bad happens, you want the insurance company on the hook for enough money that they’re going to send you very good representation. You want to get their best attorneys and they’re defending you from whatever it is you’re being accused of.

WCI: I don’t know that you can get that for the $50,000 that a lot of people are carrying around on their auto insurance policies. That might be the minimum in your state. If you actually look at the requirements, it might only be 50 grand. About 80% of the umbrella policy claims are auto-related. Most of these, it’s like extra auto insurance is what it is, for your liability when you run into somebody that’s worth a lot. So I think that’s the key.

WCI: I keep seeing people trying to relate the amount of umbrella insurance to your net worth. Like if you’re a net worth of a million, you need a million in umbrella insurance.
If you’re a net worth five million, you need five million in umbrella insurance. But there is no reason I can think of to put those two numbers together. There’s no relationship there. The only relationship you have is between the liability and the amount of insurance you have.

WCI: Having more doesn’t necessarily give you additional liability. I suppose it makes it a little more easy to afford a more expensive policy, but the truth is is you need enough for whatever the claim’s going to be, so if you get a $2 million claim, you need $2 million. If you get a $20 million claim, you need 20 million. It doesn’t do a whole lot of good if you have $2 million in net worth and $2 million in liability coverage if you get a 20 million claim against you. You’re just as bankrupt as if you didn’t have the policy in the first place. So I think the key’s a reasonable amount, and I’ve defined that as one to five million.

Periodontist: Sure. Do you know, and you probably have some information on this, then, for those types of claims … Because like you said, it’s mainly auto. Disability insurance and malpractice insurance, those really cover pretty much every scenario that would happen in a professional environment, other than something criminal, I think.

WCI: Which there’s a lot of things that could happen in a professional environment.

Periodontist: Yeah, right. But what is the average number, then, for a claim? Do you have any idea in terms?

WCI: I don’t know, but we can make a few assumptions based on the cost of the coverage, right? My malpractice coverage is … I get a little discount now. Before I went to half-time, I think this was about 15 or $16,000 a year. That’s in a state where liability’s relatively low. Even among emergency physicians, it’s a pretty good environment as far as malpractice liability.
WCI: So I’ve been paying $15,000 a year for 1 million coverage. It’s a 1 million/3 million policy, so basically for $1 million coverage, and that costs me $15,000 a year. My umbrella costs, I don’t know, $300 a year for 2 million in coverage. I think that tells you an awful lot about how often this coverage is used. You know what I’m saying? If it was getting used all the time, it would cost $15,000 a year, whereas the fact that it’s pennies, almost, pennies a day, dollar a day, whatever it is, that tells you it doesn’t get used very often.

WCI: So I think there are probably a fair number of claims in the low six figures, would be my guess, and some people may not be able to cover that if they only get minimal coverage or no auto coverage whatsoever. I think it’s much less likely to have larger claims. But can they happen? Sure. That’s why we buy the insurance.

Periodontist: One thing I guess we’re a little bit luckier on on the dental side, our malpractice is a little bit less expensive, I think, than a lot of the medical colleagues. I think for most of us we’re running somewhere between 2 and $3,000 a year for-

WCI: Yeah, wouldn’t that be great. I’m not sure there’s any medical specialties that are paying that little. Maybe in peds and family practice you can get that low, but I don’t think so. I think even most of them are paying 5, 6,000.

WCI: A quick Google search on the average umbrella insurance claim, it says 13% of personal injury liability awards are a million or more, is what … This is somebody trying to sell you umbrella insurance, of course, so I don’t know how accurate that is, but if you Google around there you’ll see that there are some larger ones, but they’re definitely small percentages. It’s certainly not as big of risk for the typical professional as malpractice is, but is there risk there? Sure, and it’s cheap to insure against it, so you might as well.
Periodontist: Right.

WCI: All right, so the next policy is, you are laddering your term life insurance policies. How big are each of these policies? You said you had a 20-year, a 15-year, and a 10-year?

Periodontist: Yep. Three policies. The longest-term one is for 2 million, the one for 15 years, the second, the middle one, is for a million, and then the one for 10 is a million. So right now I have 4 million in coverage.

WCI: 4 million on you?

Periodontist: Yeah, and then it’ll drop to 3 million, then drop to 2 million at 10 and 15 years out respectively, and then at 20 years it’ll just drop.

WCI: And how much on your wife?

Periodontist: Right now she doesn’t have any, and that’s actually one of the discussions that it would be interesting to have. She’s only been out a couple of months. We knew we still needed to get something. Honestly, though, at least right now while she’s an associate in a practice, I’m not dependent on her income in any way, and so I actually … If she were going to stay an associate long-term, I wouldn’t be completely opposed to not having life insurance on her, but I do think that when she purchases a new practice, that debt is still going to be there, and so I’d imagine that we’re going to need to get some probably term life insurance on her, relatively soon as well.

WCI: Yeah, this is an interesting question I get fairly frequently that really has no right answer. I get a two-doctor couple writing in going, “Do we need life insurance? Do we need disability insurance? Can’t we just be each other’s life insurance and disability insurance policy?” I think you can. I think you can actually justify having no insurance at all.
WCI: The big risk there, of course, is that you both become disabled or you both die. The truth is that a lot of us are spending enough that it really would have a pretty significant hit on us if we lost one of those incomes. So I think what most people end up doing is rather than having both partners buy a policy that is as big as a single doc married to a stay-at-home parent would have, I think they pick something in the middle, something between zero and what I would call full coverage for each of them, and so maybe they both carry a million dollars or they both carry $2 million or whatever.

WCI: But how much life insurance you carry really comes down to your spending. You basically, if the goal, if one spouse dies, is for the other one never to work again, at its biggest need that you could have, you want to be able to take what you get from the term life insurance policy plus your portfolio, and have that partner that’s left behind be financially independent between those two. You can’t really come up with a number unless you know how much you spend to determine how much you need to be financially independent.

WCI: But the usual answer for most docs is a seven-figure amount. One to five million, somewhere in there. If you’re married to another doctor, you can probably get away with less. But I think in your situation, I think I would put a policy in place for her. It’s so easy to get a million-dollar policy for 20 years that you might as well get it in place.

Periodontist: Yeah, I think … Honestly, she just finished residency, so I do think that we’ll do something relatively small. Like I said, once she gets into a practice ownership position, if she were to pass away, there’s likely going to still be debt on it, so if for no other reason than just for that, it’s in place.

Periodontist: I think the tricky part for young people like ourselves is, how do you project what our spending is going to be in a couple years? One of the knocks that this old financial advisor that I had said was that our savings rate
was basically too high. What I wanted to say was, “Look, our savings rate is high right now, but what happens once we buy a home and have a couple kids and get some new cars and stuff like that?”

Periodontist: Likewise, when it comes to term insurance, you almost have to project out what you think you’re going to be spending in five to seven years and then base it off of that, because obviously your spending’s never going to be lower than it is right now when we’re a two-doctor couple living in a one-bedroom apartment.

WCI: For sure, and here’s the thing, too. It should be a seven-figure amount. This isn’t something you figure out and “I need a 740,000 versus 780,000,” you know. It’s like, “I need 1, 2, 3 million.” If you could calculate out a number, round up to the next million. This stuff just isn’t that expensive, so get it in place and that way if, heaven forbid, you actually need it, you got plenty. I think that’s the goal when it comes to term life insurance.

Periodontist: Sure.

WCI: Let’s talk about disability insurance. You mentioned you each have a disability insurance policy. Let’s talk about yours first. What do you have?

Periodontist: It’s linked to income, and so basically when I went for the disability policy initially, you had to have proof of income in your contract and then they basically base it off of that. I want to say, the last time I looked at it, that it went up with 7 or $8,000 a month or something like that in disability, but they link it based off of your prior W-2.

WCI: You mean how much they’ll sell you?

Periodontist: Yeah.

WCI: So this is an independent policy? This is an individual
policy that you can take with you to any job, correct?

Periodontist: Right.

WCI: Which company did you get yours through?

Periodontist: I’m trying to think. Let’s see, Brown & Brown’s for malpractice.

WCI: It’s probably Standard or Principal or Ameritas or Guardian.

Periodontist: Yeah, I want to say it’s through Principal.

WCI: Principal, okay.

Periodontist: I think it’s two policies, and they did it so that you could increase both and one’s through Principal and one’s through Mass Mutual.

WCI: Sounds like you saw an independent insurance agent and put a pretty good plan in place. It’s probably not very cheap, but it’s probably your most important coverage you have right now.

Periodontist: Right, and this will be interesting too. I think, especially when we’re young, it’s really important that we have it. What are your thoughts as people get older? Let’s say you’re a 55-year-old doctor and you know that if you were disabled you’re pretty much financially independent? Do you think you doctors taper it down or do you think you leave it in as long as you practice?

WCI: I’ll tell you exactly what I’m doing. Today, as we record this, it’s October 29th, and I just got letters in the mail yesterday from the Standard, who has my individual insurance policies, and is basically telling me they’re going to take money out in about a month out of my account to pay for them for another year. One of my chores for today is to call them up and tell them I don’t want them to take that money out,
because I’m done. I’m 43 years old. I don’t need disability insurance anymore.

WCI: Now, in my case, it’s a little bit unique, because I’ve got this other source of income with the White Coat Investor, and so the truth of the matter is even if I was disabled from being able to practice medicine, I’d still have most of my income. So I’m canceling a little bit earlier than I probably would have otherwise, but I see little reason to carry this thing to the grave for a couple of reasons.

WCI: Number one, it’s expensive. Most of us are spending thousands a year on disability insurance, and that money can be used for other stuff. That’s the number-one reason why you want to get rid of it. Number two, if you’re financially independent, if you have enough money to live the rest of your life, you don’t need to insure your income anymore. It just doesn’t make sense. Insurance is not a profit-making enterprise for you. The only person making profit off the insurance is the insurance company, and that’s because they can charge you enough that they can cover all their expenses, make all the payouts they need to, and still have a little bit left over for profit. Any time you don’t need insurance, you probably shouldn’t be carrying it.

WCI: But the last reason is because these policies only pay until you’re 65 or maybe 67, and so if you’re 61, you’re still paying the same amount in insurance that you were paying at 35 for 30 years of coverage for only four years of coverage. It’s only going to pay for four years, so the closer you get to retirement, yes, the more likely you are to be disabled, but also, the less you’re going to get paid out from it. At a certain point, you got to go, “This just isn’t worth it anymore.” I think for a lot of people, that happens in the late 50s and 60s.

Periodontist: Yeah, it’s actually the situation my parents are in in practice, is they’re right around that age and they’re
beginning to ask themselves that question. A piggyback onto that question, too, is what happens with doctors who have not taken care of their personal finances well and they’re in their 60s, because now their ability to get that kind of insurance … If you’re 67 and you say, “I’m going to work until I’m 80,” what happens if you have a back injury?

WCI: Yeah, the problem with those policies is they usually only pay for two years and they’re expensive.

Periodontist: Right.

WCI: So it’s not nearly the deal you’re getting at 30.

Periodontist: Right. I think that’s one of the reasons why taking care of finance on the front end’s so important. I think a lot of people say, “I like my job. I’ll work until I’m 75.” At least on the dental side of things, a lot of the policies won’t even … They won’t let you go past about 65 or 67, so after that you’re riding on your own.

WCI: Let’s change subject a little bit. I wanted to get into a few of the topics we talked about on email that are unique to you. A lot of this disability insurance and term life insurance is the stuff that all our listeners are dealing with, but you wanted to talk a little bit about some considerations when purchasing your doctor home and a practice, and I wanted to get into what you meant by that. What were some of the considerations you’ve been thinking about the last couple of years as you look into these two big purchases?

Periodontist: I think the biggest one for most dental people, although we want to get the home first, it seems like you should actually get the practice first, because-

WCI: Totally agree with that. Absolutely.

Periodontist: Yeah. I think one is, when you purchase the practice … Practices can be bought and sold, and I think as
more corporations are doing it, they’re doing it more quickly, but typically when a dentist or dental specialist purchases a practice, it’s pretty much a decision to anchor down on that area, more so than a home would be. When you’ve bought that practice, the likelihood that you’re going to move, unless something major happens, is pretty unlikely.

Periodontist: Now, a lot of times, the purchase is actually going to cost more as well, and so you want to make sure that your financing is available to do that. I think the big consideration there for young doctors is making sure that we have the ability to certainly get enough leadership and management training so that we can take on a practice like that, but the big thing is making sure that we can get the loan, because there’s a lot of, I think, young dentists who want to purchase a practice that aren’t going to necessarily be given a loan for ... Some of these practices go for 1.5, $2 million. It’s not uncommon to have a large practice selling for that amount, and so getting ourselves in a financial situation where a bank would be willing to lend you that money is the biggest consideration there.

WCI: I think what happens is people come out of school with half a million dollars in student loans, and then they get a half million-dollar mortgage, and then they try to get a half million-dollar loan for the practice, and then just, at a certain point, they go, “You want all this on an income of 150,000?” It’s just not going to happen.

WCI: A house is mostly a consumption item. Yes, there’s some investment aspects. You get the saved rent is a dividend, and maybe the house will appreciate, so in some ways it has some investment aspects, but for the most part a big fat doctor home is a consumption item, and the practice is actually increasing your income, so it’s an investment more so than a consumption item. So I think it’s important to buy the investments before you buy the consumption items.
Periodontist: For sure. Yeah, I think if you look ... You don’t have to go any farther than looking at some of the information that people who do real estate for a living. They typically do one of a couple of things, right? They’re either forcing appreciation in some way by knowing something about the market, or realistically a lot of times they’re flipping it, or they’re getting a very good amount of rent to what the purchase price of that asset was.

Periodontist: Typically, I don’t think they’re buying, like you said, big doctor homes on golf courses. They’re buying duplexes and triplexes in middle areas where you get better rent and that sort of thing. The big doctor home on the golf course or on the lake is not always the best investment. Not that that doesn’t mean you don’t get it, but like you said, it truly is mainly a consumption item.

WCI: Now, you guys got married not that long ago, and decided to do something unique with your gift registry. Tell us about what you did and why you did it.

Periodontist: We got married just a few months ago, and one of the things we did is we didn’t want to actually have regular gifts, we just wanted to ask for cash when it came time for the gifts. It wasn’t that we wanted a lot of money or anything along those lines, it was really just that if you think about how the traditional registry works, Bed, Bath & Beyond or Restoration Hardware, or whatever store you’re at really owes you a check because you’re basically forcing your friends and family to buy stuff at retail price. Sure, they’re things that you want, but they’re certainly not the biggest needs in terms of your financial goals, especially in the short term.

Periodontist: In our case, we’re in a one-bedroom apartment right now. We’ve got pots and pans and that sort of thing. There just wasn’t that many consumption items that we legitimately needed, so I figured the money was much better spent on other things. Realistically, where it went, her
parents helped with some of the wedding, but the gifts actually paid the rest of that off, and some of the honeymoon. Then there was a little bit that was left over and that basically went right into her student loans.

Periodontist: It just felt like it was a more efficient use of the money, which if somebody truly cares about you, that’s really what they should want in a gift, to go to the most efficient place.

WCI: For sure, and that’s what we tend to do as well, because in your 20s in general, and particularly when you come out of training, cash is king. You just have so many uses for it, and such a limited amount of it, that it’s really helpful, so I can see why you did that.

WCI: All right, let’s get into our last topic. This is a little bit more of a controversial topic. We interacted about this on email a little bit. Let’s talk a little bit about biases in dental, and for that matter, medical treatment. Biases that sometimes lead us to recommend courses of treatment for a particular patient. You want to give your thoughts on that?

Periodontist: Yeah. I’d be interested to get your thoughts, too, on how that happens on the medical side. I don’t know if they’re more insulated, but I think one of the things that’s great about your group is that you guys are very … You do a lot of … How do I put this? You’re very retrospective in thinking about the biases that other professionals have. I felt like if we’re going to do that for a financial advisor, I do think we should put the microscope on ourselves in the same way.

Periodontist: Really, no matter what, whether it’s dentistry or different aspects of health care, I think that we’re all likely to have some form of biases. The way that typically most dental professionals are paid is basically a percentage
of what is essentially collected by that particular practice. A number of things will vary on that. What procedures are done, how often they’re done, what the practice has the ability to bill for, whether in the fee-for-service model or some type of an insurance plan, all in some way, shape, or form affected.

Periodontist: But I know as a young doctor, there was definitely a temptation to do additional types of treatment for financial gain. Again, everybody has their own biases, but I do think that that’s one of those things that comes up, I think, more often, I don’t think that patients or other health care providers are necessarily aware of.

WCI: Yeah, I think for sure the medical side is more insulated from this. That’s because of the role of health insurance, honestly. It’s all so opaque. We don’t even know the prices of half the stuff we’re prescribing or tests we’re ordering. So in some ways, there’s an advantage there on the dental side, because you actually know what things cost and what you’ll get paid and et cetera, et cetera.

WCI: The downside is I think you face that conflict of interest much more readily than a physician does. It’s staring you in the face every day, and just like for a commissioned salesman that we were talking about earlier, you’ve got that temptation all day long that you have to resist to do the right thing for the patient, and only the right thing. Maybe that’s X rays once a year instead of twice a year or maybe it’s … I don’t know what it is in your particular field, but I think it’s something that we have to realize that we have a duty to the patient that we’ve sworn, and it’s a duty not just to their health but also to their pocketbook, is quite frankly the way I look at it.

WCI: It’s very difficult in medicine, though, because you literally cannot find out the price for a particular treatment for a particular patient in their insurance plan. Insurance
really mucks it up quite a bit.

Periodontist: Sure. I think in my specialty, just based off of ... Patients don’t typically feel periodontal diseases happening or a lot of times they won’t see it if it’s in the back of the mouth, so it’s pretty difficult for us to truly over-treatment plan. I guess you could do it, but it-

WCI: Because nobody wants to treat it, because it’s not bothering them?

Periodontist: Right, yeah. A lot of people, it doesn’t hurt them, doesn’t bother them, or that sort of thing. Honestly, I think for a lot of dental practices, not everybody of course, but for some, anyway, there’s the temptation to treat just what’s bothering them or treat just what they want or just treat what I can do as a general practitioner. Like I said, definitely not always the case, but with some dentists I think that can happen.

Periodontist: That’s true, I think, from specialty to specialty as well. I think that as a periodontist I’m going to always see the patient walks in the door. I’m going to notice all of the periodontal concerns, the dental implant concerns, but if that same patient went to an orthodontist, they might say, “Hey, we could probably do some things on the ortho side as well.” Everybody, for the most part, has some work that could benefit the patient.

Periodontist: So it’s not necessarily that treatment gets truly over-treatment planned, it’s more that we just have our slant towards what our background and our training is. I think that’s the most common bias that tends to come out. Not necessarily something bad for patients per se, but just that if you were a general practitioner versus being a periodontist versus being an oral surgeon, you would probably prioritize some of those things slightly differently in some scenarios.

WCI: What do you personally do, knowing that you’re only a
couple years out of residency and nowhere near financial independence, still with lots of cash flow needs? What do you do personally to keep from over-prescribing or over-treating?

Periodontist: I think one of the things in our practice that’s really helpful, we get to separate the day that we do our examination from the time that we actually make treatment recommendations, so you can really go back and think about when and why you’re going to recommend treatment. I do think that evidence-based treatment’s really important. In dentistry it’s not as clear-cut, I think, as it can be in certain aspects of medicine, and so really going back and reviewing the evidence, saying, “Which treatments are truly needed?” and having criteria set for different classifications of things really goes a long way to eliminate some of that bias.

Periodontist: Then we have a sit-down with the patient where all we’re going to do is review everything in terms of the radiographs, photographs, the whole nine, and come up with a treatment plan with the patient there, so I think some of those things do tend to help in terms of bias. But a lot of it is just having conversations with the practitioners that we’re working with on the case to see if there are other needs that are out of our purview, what are they and how urgent are they and how do we make sure that we ensure that that other work gets done as well? Even if it’s not necessarily something that we’re going to do, we just want to make sure that it makes the most sense for the patient. So I think the split time between the initial exam and the recommending of treatment for most patients is actually the most helpful thing.

Periodontist: One of the questions was, in my 401(k), currently I’m doing it with Roth. The idea was I didn’t have any Roth contributions prior. I probably want to have a mixture of both. You can effectively put more money in when you’re doing it as a Roth contribution, but at some point I think probably the tax benefit … A lot of people say to switch over to traditional, and I just want to know where you think
that teeter-totter point is for most dental people.

WCI: I think the teeter-totter point here is the same for everybody in that when you get into your peak earnings years, you should prefer tax-deferred 401(k) contributions. Now, in your case, your wife’s just coming out of residency this year, hasn’t really gotten to peak earnings yet, and that might not even be next year, but it certainly isn’t this year, when for half the year she wasn’t working.

WCI: So within a couple of years, though, the two of you are going to be at your peak earnings level, in which case you’re going to want just about every tax-deferred dollar you can get. But in these early years when only one of you is working or half your year you’re on resident salary and half the year on full professional salary, that’s when you want to be taking advantage of the opportunity to get things into a Roth 401(k) at a lower tax rate. Does that make sense?

Periodontist: Sure. Yeah, a couple other ones, though. I think you’ve hinted on some podcasts before about minimalism and decluttering and really prioritizing just the things that you need versus the things that society says you want. You’ve owned a couple of homes. We’re going to be purchasing a home and, at some point, having kids. What would your recommendations be on how to prioritize the things that you truly need in a home that you’re going to make a lot of use out of versus the things that look really nice when you’re buying the fancy doctor home that you won’t necessarily use a lot of?

WCI: You know, Cindy, who manages these podcasts, is meeting with a realtor in about an hour and a half, and so she’s giving me the evil eye as you ask me that question. The truth of the matter is, the vast majority of what we, as doctors, buy in a home, is a want, not a need. I had my friend, the contractor, over here, the other day, and we were talking about maybe doing some changes and stuff, and he’s like, “What
are your needs?” I’m like, “I have no needs whatsoever. None of this we’re talking about is a need.”

WCI: So I think it’s important to realize that upfront, that almost everything you’re talking about is a want and it’s just what you want the most. But I’ll tell you what, I’ve got a lot of space in my basement. This place is 4,400 square feet on three floors, and the only thing I ever come down to this basement for is to record podcasts. So I don’t need 1,500 square feet to record a podcast. I just don’t need it.

WCI: I think being careful how much you really want and need down the road is probably my best advice, just because every square foot you buy has to be furnished and carpeted and painted and insured and heated and cooled and landscaped and so on and so forth. So sometimes I think we get these big eyes at what we really think we want, and two or three years from now we’ll feel a little bit differently about.

WCI: I know one regular on the White Coat Investor forum feels imprisoned by his house. At first it was great to have a doctor house, and now 20 years later he feels like he’s a slave to it because he’s always doing maintenance stuff and upgrading stuff on it and landscaping it and stuff. So I think the main thing is just don’t overestimate how happy the fancy doctor house is going to make you. It probably won’t be as much as you think.

Periodontist: Yeah, one more, and this is on behalf of that friend, the guy who got the Tesla, the friend who introduced me to the White Coat Investor group.

WCI: Thank you so much, friend, Tesla driver.

Periodontist: He’s got everything paid off except for his debt paid down on the practice and on his primary residence. He’s paid everything off. I don’t know all his personal details, but I would go with the working assumption that he’s maxing out all of his available tax-deferred things. He’s on the
other end of it. He’s already buying a Tesla.

Periodontist: He wanted to know if he’s got additional money, where do you recommend it go? He’s got … Again, I don’t know the amounts on the homes and the practice, but he said that both interest rates were in and around 4%, so they’re both at really good interest rates. Do you just blast money into the taxable account? Do you do equipment upgrades or do you do debt paydown? What would your recommendations be for him?

WCI: I think in this sort of a situation, it’s not clear. When you’ve got 30% credit cards, there’s an obvious answer to the debt versus invest question. When you aren’t even putting enough money into your 401(k) to get the match, you’ve also got a definite answer to this question. The rest of the time you’re in some sort of a gray zone, and I did a blog post on this recently, just because it’s literally the most common question I get.

WCI: And some things to consider, like the interest rate and whether you’ve got other tax-advantaged accounts available to you … But assuming you don’t, and your question is really, “Do I take a guaranteed 4% paying down my mortgage or my practice loan, or do I invest in taxable and hope to do better than that?” There’s no right answer there, and sometimes the right thing to do when you’re not sure what to do is just split the difference, which is perfectly reasonable as well.

WCI: It does take away the power of focus a little bit. If you were focused completely on the debt, you’d probably pay it off a lot faster, but it’s a reasonable thing to do either way, to pay on the debt, to invest, or to do both at once. So no totally right answer there.

WCI: You mentioned equipment upgrades, though. If there are equipment upgrades you can do that will boost your income, I view that as a pretty good investment. Investing in yourself and your practice is oftentimes the best thing that you can do
with a dollar, and so if it’s just putting in a TV because you think people like it, that’s one thing, but if it’s something that’s actually going to earn you more money, I would definitely look into that first before investing in a taxable account or paying down 4% debt.

Periodontist: Sure. Okay, yeah. I mentioned this before. Hopefully more people will come on and do something along these lines in terms of going through their finances, because I think that when you’re by yourself, getting through this stuff without a community, you feel like you’re on your own, and so I think hearing more people talk about their personal situation, I’m sure a lot of people will relate to it, for sure.

WCI: I agree. I’m waiting to get more people emailing me and saying they want to come on, so if you’re one of those people out there, please do.

WCI: We’re starting to run a little bit short on time here, but this is your opportunity. You’ve got the ear of 10 or 15,000 high-income professionals, the vast majority of whom are physicians or dentists or their trainees, but what advice do you have for them? What would you tell them that you’ve learned that you’d like to pass on?

Periodontist: I think in terms of if you’re to say advice, I think it’s more just what was my experience going through it. I think that’s the biggest, the most helpful thing that I can help provide, and that is probably the most important thing you could do would be to track your spending. Get on a Mint or something along those lines and be very intentional about what your spending is and don’t relate that to the level of income.

Periodontist: I think if you can do those couple of things that really will help, and that’s going to be one of the things I’m going to go through with my wife here in January, is we’re going to do a review of this past year and see where
our spending goes. I think of any tool or anything along those lines, that probably made a bigger impact than anything.

WCI: Thank you so much for being on the White Coat Investor Podcast. It’s been wonderful having you here.

Periodontist: All right. Thanks so much.

WCI: Hope you guys enjoyed that. I’d like to do more segments like that with regular listeners. We do our best to keep you anonymous if you want to be. Obviously if somebody recognizes your voice that’s going to be a little bit hard, but it should keep your patients from being able to listen to the podcast when they Google your name, anyway.

WCI: Make sure you’ve signed up for the newsletter if you haven’t yet, and when you start getting the newsletters, add our email address to your safe senders list or to your contacts list so you make sure you get them. Unfortunately, when you’re sending out as many emails as we are, a lot of times some of the email services like to add us to their junk mail spam filter kind of list, so you have to actually tell them sometimes that you want our emails if you want to be getting them. Obviously you can unsubscribe at any time and there’s no price for them. It’s totally free.

WCI: When you sign up for the newsletter, you also get our Financial Boot Camp, which is 12 emails you get once a week for 12 weeks that will help you get your finances in line and get up to speed with the rest of the White Coat Investor community.

WCI: If you’re like many of your peers, your heart probably drops when you see how much you owe in medical school loans. But it doesn’t have to be this way. You don’t have to live life with high payments or high interest. CommonBond lets doctors take their old, expensive medical school loans and trade them in for one at a lower rate, saving, on average, $50,615. You’re also protected by an industry leader in
borrower protections, because life is unpredictable. You’ll have an award-winning service team helping you every step of the way, and the commitment-free application will show you your savings in two minutes.

WCI: As a member of the WCI community, you’ll get a $500 bonus when you refinance with CommonBond. Apply today at whitecoatinvestor.com/commonbond to lock in your savings before interest rates go up. CommonBond is a licensed lender, NMLS #1175900.

WCI: Head up, shoulders back. You can do this. If you need help, we will connect you with someone in the White Coat Investor community to help you. See you next time on the White Coat Investor Podcast.

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7 Tips to Avoid Investment Scams

[Editor’s Note: The following guest post was submitted by Mark Pugsley, a lawyer who specializes in recovering losses for victims of investment fraud, unsuitable recommendations, and Ponzi schemes. He is a local attorney here in Utah. We met over lunch one day and lamented the prevalence of financial scams in the world, the epicenter of which seems to be right here in Utah. Mark is now an advertiser here at WCI and can be... ]
I have represented a number of doctors and dentists over the years in disputes with their stockbrokers and in Ponzi schemes and investment fraud cases.

My medical professional clients are typically intelligent and savvy with respect to managing their money, but because they are often too busy to dig into the details they can often be taken advantage of by unscrupulous investment advisors, and in some cases, they fall victim to fraud.

Below are a couple of war stories. Of course, most investment professionals are good and well-qualified – but not all of them. A keen intellect cannot substitute for taking the time to read the documents carefully. The devil may really be in the details.

Some basic tips on how to avoid fraud are at the end of this article.

**Scam #1: The Falls Event Centers**

Utah-based entrepreneur Steve Down had been pitching investments in The Falls Event Centers since 2011. He raised approximately $120 million from more than 300 investors – the majority of whom are dentists throughout the United States.
On May 11, 2018 Down and his event centers were [sued by the Securities and Exchange Commission](https://www.sec.gov) for defrauding investors.

### So why did so many dentists fall for this scheme? How did he do it?

Steve Down is a gregarious 61-year-old promoter who billed himself as an “an innovative entrepreneur and successful business owner, is passionate about creating companies and providing jobs.”

One of Mr. Down’s companies was called [CE Select](#), a continuing education provider for dentists. According to the [detailed complaint](#) filed by the SEC, dentists attending CE Select seminars were pitched an investment in The Falls during their lunch break.

I honestly cannot figure out how he managed to make a pitch for a wedding reception center investment seem like a normal part of a dental continuing education seminar. But I digress.

The investment was basically a hard-money loan to fund the purchase and construction of more event centers and was supposed to pay returns of 10 to 14% per year to investors.

Down’s investment pitch remained essentially the same for years. The SEC alleged that Down made the following
representations to his captive audience of unsuspecting dentists:

- The Falls had 8 profitable locations and was growing at a rapid pace,
- The Falls would have 200 event centers by 2022
- After The Falls had 12 centers, it would be able to obtain institutional loans to replace the hard money loans,
- Many of the event centers were profitable even before they opened, because they were accepting event bookings before they opened, and continued to be profitable after they opened,
- Each event center would earn gross revenues of $1 million per year and cover expenses of approximately $650,000, leaving a profit of approximately $350,000, or 35% of revenue, per year.
- The 200 projected centers would bring in net income of $70 million per year
- The Falls would be worth $2.8 billion by the time it had 200 centers in 2022.

The problem, according to the SEC, is that many of these representations were false, and Down knew it.

The Falls’ own accounting records showed that the event centers had never been profitable. Down also allegedly knew that his business model was unsustainable because of crippling debts owed to investors and mortgage holders. But he nevertheless kept on pitching this “profitable” investment to dentists and other investors until the SEC finally shut him down.

Down did not admit or deny the allegations in the SEC’s complaint, but he and The Falls did consent to the entry of a final judgment permanently enjoining them from future violations of securities laws and Down paid a civil penalty of $150,000. A final judgment was entered against Down and The
Falls on May 11, 2018, by United States District Court Judge Jill Parrish.

Despite all this, according to an article in the local paper, Down planned to continue building his wedding center empire, and “The Falls will continue to conduct business as usual.”

But that won’t happen; The Falls filed for bankruptcy soon thereafter.

**Scam #2: A Bad Broker and His Fake Investments**

Tom Andrews was a respected member of the small community of Nephi, Utah (population 5,784) where he was born and raised. His father Earl had prepared tax returns for many of the residents of Nephi for many years. When his father retired Tom took over his father’s role as tax preparer and began preparing tax returns for his father’s clients, including several local dentists and veterinarians.

At about the same time he took over his father’s tax practice, Tom obtained a securities license which permitted him to act as a stockbroker. He realized that he could solicit investments from the people whose tax returns he was preparing, and over time many Nephi residents began to rely on Tom for investment and retirement advice, as well as for their
taxes. They opened investment accounts with LPL through Tom Andrews and placed some or all of their retirement funds into his hands.

But beginning in 2011 Tom Andrews began to make other plans for their money.

Andrews formed a fake trust which he called the “Jackson Living Trust” and made himself Trustee. Andrews then opened a bank account at a local credit union under the name of the “Jackson” or the “The Jackson Living Trust.” It is unclear what paperwork he presented to the credit union, but they nevertheless opened up an account for this fake trust and gave Tom the full signatory authority as the trustee. This meant that he could cash or deposit checks that were made out to the “Jackson Trust.”

At about the same time, Tom began counseling his clients to invest in an annuity with Jackson National (which does actually exist). He told them that this investment would pay a guaranteed rate of return between 5 percent and 8 percent annually. Critically, he advised them to liquidate most or all of their investments and put the money into this “annuity.”

Andrews provided real marketing materials from Jackson National Life and even used the company’s application forms. The victims filled out the applications, and gave Andrews checks for their entire life savings made out to “Jackson Trust” which they believed would be invested in the Jackson National Life annuities. But the money was never sent to Jackson National Life.

Andrews deposited each of the checks into his fake account at the Cyprus Credit Union and then use the funds as he saw fit. He basically stole $9 million from his clients.
But the victims needed to continue to believe that their money was safe and secure in the annuity they thought they had purchased so Andrews generated fake quarterly statements for them. He pulled a Jackson logo off the internet and made up fake account statements that he mailed out to all of his clients. Of course, the fake statements showed that their investment was safe and growing as Andrews had promised. In October of 2015, several of his clients became suspicious when they had a hard time withdrawing money from their accounts. Several contacted Jackson National Life and learned that in fact they had no account with the firm, and the account statements they had received were fake.

After several of the investors reported his conduct to the SEC, he was sued civilly and criminally. On December 15, 2016, Tom Andrews was sentenced to 97 months in prison — the maximum under sentencing guidelines — and was ordered to pay $8.3 million in restitution. The location of the money he took is unclear, and it’s unlikely that his victims will ever see a dime of restitution.

There are several troubling aspects of this story. First, unlike many of the stories I’ve written about, this one it appears to be a deliberate fraud from the outset. Andrews set up the bank accounts with a name that was deliberately similar to the name of a well-known annuity company. He used marketing materials and account applications for a real investment, and his investors would not have known that their money was going
into a personal bank account as opposed to a licensed, verifiable company.

Another troubling aspect of this story is that the financial institutions involved dropped the ball and did not implement oversight and compliance procedures that could have protected the interests of the victims in this case. Banks, brokerage firms and others should be watching for red flags and alerting state and federal authorities when they see suspicious activity. In this case, that oversight never happened, and millions of dollars were lost as a result.

On February 12, 2016, FINRA barred Tom Andrews from associating with any brokerage firm in any capacity.

7 Tips to Avoid Being Scammed

I have been helping people recover losses from investment fraud for 25 years, so I often get asked how to avoid one. Here are a few things you can do to avoid getting scammed:

1. Do your homework.

Run a simple Google search on the company and its managers, or the individual pitching the investment. Steve Down had a prior settlement with securities regulators that should have been a red flag, among others.
2. **Hire an attorney.**

An experienced lawyer can help you perform due diligence into the company and individuals offering a private investment. You need to carefully evaluate the risks and determine whether the offering complies with state and federal statutes. It is far cheaper to hire an attorney on the front end of an investment like this – when your money is gone it gets very expensive.

3. **Scrutinize the financials.**

In this case, the company’s financial statements were not prepared in accordance with generally accepted accounting principles (GAAP). Sophisticated investors (and good accountants) would have discovered this problem and seen it as a huge red flag. According to the SEC, proper accounting would have shown that The Falls was losing money and likely insolvent.

4. **Get it in writing.**

I am amazed at how often people will give hundreds of thousands of dollars to someone on nothing more than a handshake. The terms of your deal should always be put in writing, and those terms should be reviewed by the competent attorney you hired.

5. **Read the Paperwork.**

Investors in a private investment opportunity should receive a detailed lengthy disclosure document called a *private placement memorandum* (PPM). Take the time to review it before you invest. Like a prospectus, a PPM contains detailed information about all aspects of the business including the business model, financial history, risk factors, biographical information on the managers, and the terms and conditions of the private investment, among other things.
6. Work through licensed stockbrokers or investment advisors.

Even private (unregistered) investments generally need to be sold by licensed stock brokers. Every investor should look at the employment and disciplinary history of their broker or investment adviser, which is available on FINRA’s BrokerCheck website.

7. If it sounds too good to be true it probably is.

If you are thinking about putting money into an alternative, unregistered, or unusual investment that promises abnormally high returns (like, ahem, 10 to 14%), watch out. And if someone promises you a “guaranteed” return on any investment that ought to be a red flag — investments are rarely guaranteed and investments that offer unusually high returns are more risky, not less.

What do you think? Have you been a victim of investment fraud? Why do you think doctors often fall prey to fraudulent investments? Comment below!