Private Real Estate Funds – Podcast #93

Podcast #93 Show Notes: Private Real Estate Funds

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-yourselfers, 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.

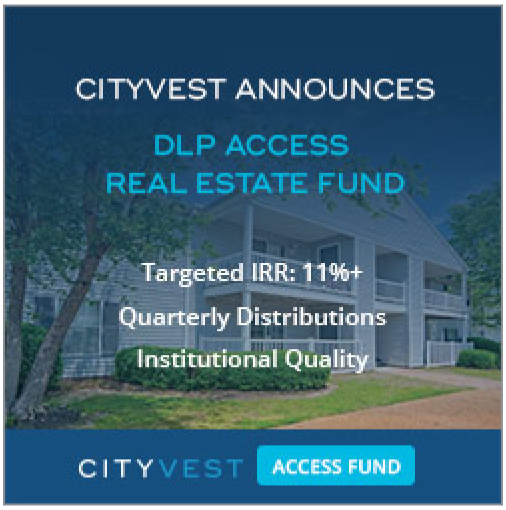
Investing with CityVest

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 with 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 atherecotmy. 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 actually an advertiser on my website term4sale.com. 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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