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The Physicians Dilemma: Retirement Shortfall

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Physicians face financial challenges that are unique to their profession. While they are generally considered to be "highly compensated," their compensation does not necessarily guarantee financial security. The following outlines several obstacles facing physicians that may prevent them from amassing enough wealth to maintain their lifestyles after they retire. This article also highlights several important issues that should be addressed and actively managed in order to increase the probability of achieving enough wealth to retire comfortably.

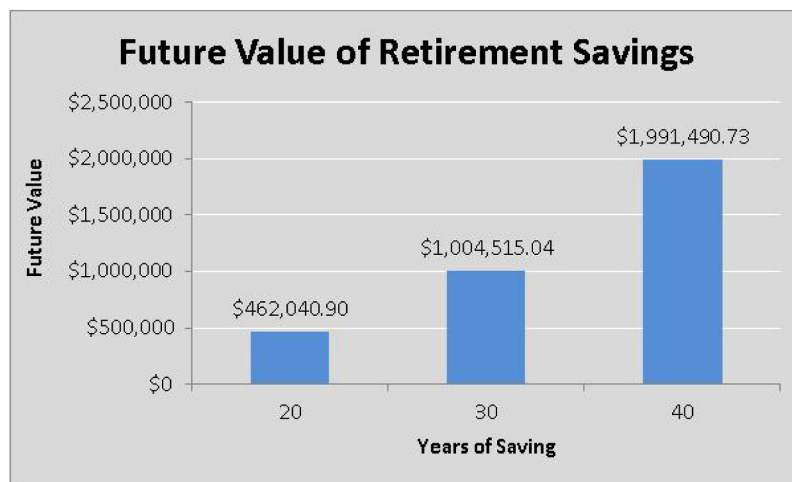
According to the Association of American Medical Colleges, the 2011 medical school class graduated with average debt of more than $161,000. This is a large debt burden, especially when you consider the modest salaries earned during residency. The median salary for residents is less than one-third of their education debt burden. In most cases, physicians defer making payments on their medical school debt until after they complete their residency. However, the interest continues to accrue and the debt increases. The significant cost of servicing medical school debt dramatically reduces disposable income and in many cases prevents physicians from adequately saving for retirement. Depending on the payment plan, it is not uncommon for physicians to be well into their 30's or 40's before they retire their medical school debt. Therefore, assuming a retirement age of 65, physicians generally have a relatively compressed period to fund their retirement needs.

Most physicians are compensated based on production. Therefore, unlike most of their peers in other professional services industries, tenure and longevity do not equate to higher earnings. In fact, it can become increasingly difficult to sustain the hours and demands required to maintain their compensation over the course of their career. It is also very difficult to gradually reduce hours and take on a part time role as the costs of support staff and resources are significant so most clinics require a full time commitment. The threat of lower reimbursement levels and additional

business costs, such as electronic medical records systems, add to the difficulty in maintaining stable compensation. A compensation survey conducted by The Medicus Firm in April and May of 2012 found that 2011 marked the second year in a row that physician salaries declined. This is an alarming trend because as income has flat-lined the cost of medical school has steadily increased.

In many professions an established client base can be monetized at retirement. However, with physician practices this is seldom the case. In general, when physicians retire they are no longer compensated and must rely on savings to support their retirement spending needs. Given a relatively high compensation level, social security payments will only replace a small portion of pre-retirement income. Therefore, a significant portion of retirement income needs to come directly from savings.

Despite the difficulties faced, there are several actions that physicians can take to help improve their probability of retiring comfortably. The first step is to develop a plan that balances debt repayment and retirement savings. There are a host of factors that should be considered when determining the optimal approach for retirement saving. The after-tax interest expense of the education debt should be compared to the expected return of investing for retirement. Retirement deferrals reduce income and can potentially reduce the overall tax burden, especially if they prevent the onset of the Alternative Minimum Tax (AMT). Many retirement plans include matching contributions that immediately generate a positive return on deferrals. For example, a 50% company match generates an immediate 50% return on money invested. Clearly foregoing the match to retire student debt is not advisable as the interest rate on the debt is minimal compared to the after-match return. A majority of discretionary income should be allocated toward the option that is projected to provide the best net return.



Although the investment industry utilizes significant marketing budgets to promote performance, when it comes to saving for retirement it is the time and the amount saved that has the biggest impact on achieving a successful retirement nest egg. As an example, $1,000 invested each month for 40 years at a 6% annual return grows to more than four times the same amount invested for 20 years at the same rate and nearly twice as much than the same over 30 years. Since physicians may not be able to count on rising incomes they should focus on establishing a lifestyle that allows them to begin saving an appropriate amount toward retirement as early as possible. Physicians should consider working with a financial planner that can help develop a financial plan and budget and clarify the amount that should be saved for retirement.

There are several different types of retirement plans that by their design allow business owners and highly compensated individuals the ability to contribute more than traditional retirement plan annual limits. In general, cash balance plans work best for those that want to save more than $50,000 a year for retirement; employers that are already contributing or are capable of contributing to all employees; a consistent and fairly predictable profit stream; and partners or owners over the age of 40 that want to accelerate retirement saving. Cash balance plans support tax deferred savings, asset protection, and allow for accelerated retirement savings. Therefore, medical groups and physicians are good candidates as the benefits of cash balance plans address several of the unique challenges physicians face in saving for retirement.

Saving for retirement is a difficult and long journey. However, there are actions that physicians can take to greatly increase the likelihood of achieving a successful retirement. Developing a plan and saving early will greatly improve the likelihood of accumulating enough wealth

to retire comfortably. As business owners, physicians can also address retirement savings at the plan design level and utilize options that encourage pre-tax savings and tax-deferred growth. Although saving for retirement isn't easy, a proactive approach and the assistance of outside professionals should reduce the anxiety and stress and greatly improve the prospect of meeting retirement goals.

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