TOP 5

FINANCIAL MISTAKES RESIDENTS MAKE

1. Buy the wrong type of disability insurance.
2. Buy whole life insurance.
3. Pay off low interest debt too quickly.
4. Miss opportunities in the year of transition into practice.
5. Contracts

Investing more.

1

Buy the wrong type of disability insurance.

Buy the wrong type of disability insurance. Residents often come to us with what they think is “own occupation” disability insurance that a “financial planner” (insurance agent working for a large insurance company) sold them. It is true that many of these policies are “own occupation” such that they will pay you if you cannot do the “material and substantial duties of your own occupation.” But this is not the whole truth. In fact, all but about 4 insurance companies will eliminate the disability benefit if you are “gainfully employed in any other occupation.” In other words, these policies will pay you if you cannot do your own occupation but if you choose to work somewhere else to supplement your disability income, they will reduce and then eliminate your disability benefit.

It is important that you procure “true” or “double-dip” own occupation coverage which allows you to work elsewhere to supplement your disability benefit without reducing the benefit. Over the last decade, we had several clients grateful for the ability to supplement their disability benefit as the disability payment was not sufficient to cover their bills and retirement and education expenses. The good news is that with proper residency discounts, “true" own occupation policies are often cheaper than the “regular” own occupation policies.

2

Buy whole life insurance.

Whole life insurance is one among several types of permanent life insurance where the death benefit will last your entire life. The alternative form of life insurance is term insurance where the death benefit only lasts for a specific term. Term insurance premiums are a fraction of the price for the same death benefit as a whole life policy. Whole life insurance is sold to residents and fellows with the promise of future, tax-free growth of the investment portion of the policy. But they carry large fees and there are more efficient ways for residents and fellows to grow money in tax-advantaged ways without incurring these large fees. You should avoid these policies, especially while in training.

Investing more.

3

Pay off low interest debt too quickly.

Debt incurs a large emotional burden, especially during residency. Residents often respond to this emotional toll by setting up student loan repayment plans and home mortgages with the shortest repayment period and smallest interest rate. One extreme example is when one resident refinanced his $200,000 into a 5-year repayment plan. This saved him about .5% per year in comparison to a 10-year repayment plan. But the downside was that his payments were significantly higher. In fact, it meant that his entire savings plan for the first 5 years was allocated to pay off 3.75% debt as opposed to investing in the market at a potentially higher rate of return. In this way, there is an “opportunity cost” to paying off low interest debt versus investing at a return that is potentially higher than the debt is costing you.

4

Miss opportunities in the year of transition into practice.

The year of transition between residency and entering practice provides rare opportunities. This is the last year (possibly for the rest of your life!) of lower tax brackets. Many residents are overwhelmed with interviewing, negotiating contracts, completing training, house-shopping, etc… and miss the most important tax-planning year of their careers. The transition year offers opportunities to convert qualified money to Roth IRAs, fund Roth employer plans and Roth IRAs. But these opportunities must be done before the end of the year and often much sooner if you want to max your Roth 401ks or 403bs through your new job.

Investing more.

5

Contracts

There are many considerations when choosing where you will enter practice. Residents will often engage an attorney to help review the terms of the contract like tail coverage and termination clauses but neglect to understand and negotiate the compensation structures from signing bonuses to wRVU versus collection-based bonus incentives and how expenses are shared at partnership, etc… You should find a professional that is experienced reviewing the financial terms of your contract but avoid firms that charge a % of your first year's base salary to review the financial terms. This can result in tens of thousands of dollars in fees versus a flat or hourly fee for similar review and services.

Investing more.