Monetary Decisions for Medical Doctors

Table of Contents

I. General Financial Skills Every Resident Needs

A. Financial Planning during Residency

By Don Germano, ChFC
The Mony Group, Rochester, New York

Setting and monitoring your financial objectives during residency is not a complex process. For most residents, investing will not be a high priority since disposable income is low and the demand for cash is high. Those who do have funds to invest should consider applying the money to either debt reduction or saving for a downpayment on a home. That being said, the following should be addressed while a resident:

1. broaden your understanding of the financial planning process,
2. prepare a household budget,
3. protect your credit rating, and
4. open your mail.

First, **open your mail and verify that creditors are being paid on time**. Make sure that deferments, forbearance, or loan consolidations have been processed correctly. Most importantly, pay your bills on time regardless of what circumstances may tempt you to let things slide. Keep in mind that debt exerts an enormous amount of control. After you complete your training, the amount of debt you carry will influence some key future decisions, such as: how many patients you see per hour; whether you choose private practice or academic medicine; and whether you work full-time or part-time. For these reasons, it is highly recommended you reduce your debt as quickly as possible.

Life insurance and disability insurance are two components of a sound financial strategy that can be addressed while in residency. You should purchase a sufficient amount of life insurance to allow your loved ones to maintain a lifestyle your family deems important should you die prematurely. Placing a dollar figure on that lifestyle is a function of your budget. Residents typically purchase between $250,000 and $500,000 of coverage; however, after training is completed, most physicians carry between $500,000 and $2,000,000 of protection.

Term insurance makes the most sense for residents. These contracts provide a death benefit to the beneficiary of your choice at an affordable cost during the early years of the policy. If you are single, consider life insurance if: 1) someone co-signed a loan for you; 2) you are concerned about future insurability (medical approval by the insurance company); or 3) you anticipate the need for coverage and you want to lock in a cost at your present age. The following features are important to understand before purchasing a life insurance contract: portability, convertibility, and the number of years the premium (your cost) is guaranteed.

Disability income protection is extremely important to physicians and, for many residents, is the first insurance contract they purchase. Disability insurance can pay you an income if you’re sick or injured and cannot work, in accordance with the terms of the contract. Although the cost of the policy is an important factor, do not overlook the insurance company's definitions of disability. If you discover substantial difference in cost between two different companies, you may not be reviewing comparable programs.

There are generally two types of disability protection: group contracts and individual coverage. Group insurance can be secured through your employer and/or various associations. Individual contracts are purchased directly from an insurance company and can be non-cancelable (on the part of the insurance company) and/or guaranteed renewable. The balance of my remarks will address these contracts.

It's been my experience that approximately 50% of all residents purchase an individual contract. This coverage is quoted as a monthly (income tax-free) benefit. The maximum amount of coverage you will be allowed to purchase as a resident is typically $2,500. Upon request, the contract can include a feature allowing you to expand the protection without providing new medical history; however, financial underwriting will be required. The amount of coverage available is always dependent on your income at the time you request coverage. Having this ability to expand your coverage is important because many physicians in practice carry between $2,500 and $10,000 of monthly coverage.

Before you purchase a contract, understand the key definitions of the policy: total disability, residual disability, residual pay out calculation, waiting period, recurrent disability, future income options, and exclusions. It is important to know that substantial changes have occurred within the industry since 1995. These changes have affected the definition of disability, as well as the cost.

Ask your employer if they have an arrangement with any specific insurance company. Employer-arranged programs can be voluntary; the residents are responsible for premium payments. These programs typically provide a more favorable cost than you can secure on your own, as well as liberalized underwriting – which means that coverage will be issued as long as you are not currently disabled or in the elimination period (disabled but not yet collecting benefits). Premiums are calculated using unisex rates and a discount which can be as much as 30%! Without unisex rates, women are required to pay substantially more for coverage than men – as much as 40% more!

Lastly, none of the financial decisions you make as a resident will be complex. Yet, all decisions should take into consideration your short-term and long-term goals. These goals will be affected by the five main stages in your career: 1) medical school, 2) residency/fellowship, 3) the first 3 to 5 years of practice, 4) your maturation years, and 5) your retirement years. To receive correct advice in any particular stage, it is important to work with professionals who understand the overall picture. You can find such professionals by asking your colleagues (residents and attendings) for the names of those with whom they feel comfortable and whom they trust.

I. General Financial Skills Every Resident Needs

B. Selecting a Financial Advisor

By Mary Jean Allen
SUNY Stony Brook School of Medicine
Deanna Filosa, CLU, ChFC
Island Financial Group, Woodbury, New York

You may be considering seeking help from a financial planner for a number of reasons—for example, deciding whether to buy a new home, setting up a practice or partnership, planning for retirement or your children's education, or, more commonly, simply not having the time or expertise to keep your finances in order. Whatever your needs or reasons, working with a financial planner can be a helpful step in securing your financial future.

There are several questions you should ask, and steps you can take on your own, before choosing the financial planner who will help you meet your short-term needs, as well as your long-term goals. Following these steps should result in a successful partnership.

You should ask:

1. What experience do you have?
Find out how long the planner has been in practice, as well as the number, and types, of companies he or she has worked with. Choose a planner with a minimum of three years' experience in counseling individuals on their financial needs. Most important, you want to choose a planner who has extensive experience in, if not specialization in, working with physicians.

2. What are your qualifications and credentials?
Many financial professionals use the term "financial planner." Ask the planner whether he or she holds a financial planning designation, such as CLU (Certified Life Underwriter), ChFC (Chartered Financial Consultant), CFP (Certified Financial Planner), RIA (Registered Investment Advisor), or PFS (Personal Financial Specialist). If the planner holds one of these designations, check on his or her background with the CFP board or other relevant professional organization. You may also ask for references, from current clients and other professionals, such as accountants and attorneys that the planner has worked with. Find out if the planner has ever been fined, reprimanded, or suspended by contacting your State Insurance and Securities Departments, the NASD, or the SEC (see the listing of these agencies at the end of this section).

3. What services do you offer?
These will vary, depending on a number of factors, including professional credentials, license, and areas of expertise. Ask yourself if this planner offers services that are compatible with your immediate and long-term needs. Review a sample of a completed plan, to determine whether the planner offers the particular services that meet your personal financial needs.

4. What is your approach to financial planning?
Ask the planner about the types of clients and financial situations that he or she typically likes to work with. Make sure the planner's viewpoint on investing is not too cautious, or too aggressive, for you.

5. Will you be the only person working with me?
The planner may work with you alone, or have others in the office assist. You may want to meet everyone who will be working with you. If the planner works with professionals outside his or her practice (e.g., attorneys, insurance agents, tax specialists), get a list of their names and check on their backgrounds.

6. How will I pay for your services?
Planners can be paid in several ways. They can be salaried, commission-only, fee-only, or compensated through some combination of commission and fee. As part of your financial planning agreement, the planner should disclose to you clearly—in writing—how he or she will be paid for the services to be provided.

7. How much do you typically charge?
While the amount you pay will depend on your particular needs, the planner should be able to provide you with an estimate of possible costs, based on the work to be performed.

8. Could anyone besides me benefit from your recommendations?
Some business relationships that a planner already has in place could bias his or her professional judgment while working with you, thereby inhibiting the planner from acting in your best interest. Ask the planner to provide you with a written description of his or her conflicts of interest. Don't hesitate to walk away from any planners who promote only their own financial products, or those of the companies with whom they have a business relationship or partnership.

9. Can I have it in writing?
Ask the planner to provide you with a written agreement that details the services that will be provided. Keep this document in your files for future reference.

A qualified financial planner will have a proven track record, and should welcome these questions. It's critical to feel confident that you can to trust the planner to handle your personal and business finances in an ethical, confidential manner. Keep in mind that you want to be working with this person for many years—perhaps, for the rest of your life. Above all, you should feel comfortable in the relationship.

To check on the professional record of a financial planner, you can contact the following organizations:

Certified Financial Planner Board of Standards
1700 Broadway, Suite 2100
Denver, CO 80209-2101
888-CFP-MARK
FAX: 303-860-7388
http://www.cfb-board.org/

Securities and Exchange Commission
800—732-0330

North American Securities Administrators Association
888-84-NASAA

National Association of Insurance Commissioners
816-842-3600

National Fraud Exchange (fee required)

800-822-0416

National Association of Securities Dealers
800-289-9999

To find a financial planner in your area, you can contact the following organizations:

Institute of Certified Financial Planners
800-282-PLAN

International Association for Financial Planning
888-806-PLAN

National Association of Personal Financial Advisors
888-FEE-ONLY

American Society of CLU and ChFC
800-392-6900

References:

- "Financial Planning Tips" (Society of Financial Services Professionals)
- "Talking to Your PFP. Client Checklist" (Journal of Accountancy)
- "10 Questions to Ask When Choosing a Financial Planner" (Certified Financial Planner Board of Standards)

I. General Financial Skills Every Resident Needs

C. Maintaining Financial Records

By Barbara Warren
Mercer University School of Medicine

Accepting the fact that repaying a medical school debt is your responsibility is the first step toward meeting your goal of repayment. Do not shift the tasks of filing deferment and forbearance forms or making payments on time to others. Although your medical school financial aid officer will be happy to help you understand and organize your borrowing portfolio, do not expect your medical school's financial aid office to do your record-keeping. Once you graduate, you must be able to handle this on your own. The following are suggestions on the best way to do this.

Keep up with your exit interview information.

Prior to graduation from medical school, you probably received from your financial aid office a detailed accounting of all your educational loans. When you start your residency, keep that information with you, not in Mom's attic or in a storage unit somewhere. Be sure that folder or notebook makes every move with you throughout your years of internship, residency, fellowship, and practice.

Keep up with your mail.

As previously noted, open and read all your mail when it arrives. Do not miss a deadline or a notice regarding a change in the status of your loans by tossing an unopened envelope into a drawer or a box. Lenders expect you to stay abreast of the details regarding your loans. Missing a deadline can eventually throw you into a default status.

Set up a logical filing system that works for you.

Up to now, you have probably filed all your financial aid papers by academic year so they would be easy to refer to while you were in school. It is time now to change that filing system so that it will help you remain aware of lenders and due dates. Make a file folder for each lender/servicer. (Note: you may deal with a servicer hired by your lender to service your loans). Put into this file the promissory note and other papers relating to each loan you received from that lender. Keep a record of each lender's address and phone number(s) in the file.

Keep accurate, complete records.

Put a log sheet into each lender's file, and use it to make notes about every phone call you make or receive and each form you mail to the lender/servicer. Jot down the date, amount, and number of the check you write when you make every payment. These canceled checks can prove when payments were made, and they may be essential for taking advantage of tax benefits for loan repayment. Keep track of the dates, the names of people you contact, what was discussed, and who is supposed to do what next. Knowing the name of the person you spoke with the first time will make follow-up calls easier and less stressful for you, and for the customer service representatives as well.

Always, always keep a photocopy of any form you mail to your lender/servicer. Note the date when you mailed it. Consider using registered mail, and a return reply card, so that you know when your mail was delivered and who signed for it. This may require a little more time and a little extra expense up front, but it may save you lots of money and anguish later on.

Set up a long-range calendar.

Set up a calendar that covers at least enough years to get you through residency. Mark on the calendar the dates you need to submit forbearance and deferment forms. Keep in mind that grace periods and deferments vary in length. Remember that most forms must be submitted annually, and you are not likely to get a reminder from your lender/servicer. Do not wait until the last possible minute to request from your school or your hospital the information you need to send in with those forms. Keep this calendar in a prominent place, and make a habit of referring to it regularly.

Keep your lenders/servicers informed of changes.

Be certain that you notify your lender/servicer when you change your address, telephone number, or name. Undeliverable mail can quickly become stumbling blocks for your financial future. Below is an example of a Lender Contact Log.

Lender Contact Log

Date	Talked with	Regarding	Outcome or Pending Action

II. PGY-1—Financial Management

A. Managing Your Money: The Importance of Budget Planning

By Jeffery E. Hanson
The Access Group, Inc., Wilmington, Delaware

Budget planning is a very important part of managing your money if you want to achieve your financial goals. In fact, the first step many financial planners will take in advising you about your investments and finances will be to help you develop a comprehensive personal budget. It is also an important element in applying for personal and business loans. If you do not plan how you spend your resources, you may find that you develop a lifestyle (and a budget) you cannot afford. Your budget should provide you with a financial roadmap. It should tell you about the person you are—in financial terms—at the present time—and where you aspire to be, at some later point. The key to developing your budget is to determine how much you can afford to spend each month, given your available resources and your need to save for the future.

Steps to Successful Budget Planning

Here are some of the basic steps in preparing a budget that you can live with.

- Identify your goals.
- Quantify your financial resources, (e.g., income, savings).
- Estimate your expenses.
- Determine your savings and investment needs.
- Do the math.
- Adjust as necessary to eliminate any surplus or deficit.

Step 1. Identifying Your Goals

Answering questions like the ones listed below can help you identify your goals and set you on the path to achieving financial success.

- How do I want to use what I have learned?
- What do I want to accomplish in my career?
- Where do I want to work?
- How much do I hope to earn?
- Where do I want to live?
- When do I hope to buy a home?
- What kind of lifestyle do I want?
- What are my hopes for a family?
- When do I want to retire?
- What kind of lifestyle do I want once I retire?
- When, where, and how often do I want to travel for recreation?
- What will it cost to pursue my hobbies?

Step 2. Quantifying Your Resources

Once you've identified your goals, the financial resources available to you need to be quantified. You also should have some understanding about the ways that these will change over time (for example, after you've completed your residency and fellowship training). These resources may include any of the following:

- Your income
- Income from someone else in your household (e.g., your spouse, if married)
- Savings
- Investment income, trust earnings, etc.
- Financial gifts and other resources.

It's important to be realistic in estimating your financial resources. If you overestimate, you may end up with a budget plan that is unsustainable, and likely to cause financial stress. Estimating your future salary can be difficult, given the changing nature of the medical profession. This, too, is a reason to be conservative. You may find it helpful to discuss potential salary levels and income-growth rates with other members of the housestaff, the attending physicians you work with, and/or with physician recruiters. You also can check with any appropriate professional associations or agencies, and/or review published salary data.

Step 3. Estimating Your Expenses

Household expenses generally fall into two major categories: (1) fixed and (2) discretionary. Within the category of discretionary expenses there are both *necessities* and *conveniences*. The list below shows the general structure of the expense portion of your budget.

Fixed Expenses: Legally Binding Payments

- Taxes
- Debt payments (e.g., education loans, credit card debt, car loan)
- Court-ordered payments (e.g., alimony, child support)
- Other contractual payments.

Discretionary Expenses: Necessities

- Shelter
- Food
- Clothing
- Transportation
- Recreation

Discretionary Expenses: Conveniences

- Cable television
- Cellular phones
- Etc.

You can't avoid paying for the necessities; the "conveniences" are things you don't need—but may want. It is also possible to obtain many of your necessities without expending your financial resources to get them. This may sound absurd, but technically, it's true. For example, you could live with your parents or other relatives during residency. Then, you might not need to pay for housing. It might not be desirable, but it could be an option. The same could be said of many of the other things that you consider essential items in your budget.

In reality, however, you will spend some portion of your money to secure these necessities. The important point to note is that you will be paying for them, along with any conveniences you want, from the resources that remain *after* you have paid your fixed expenses.

Once again, be realistic. Underestimating your expenses can result in a budget plan that won't work. Consider what you spent on a given expense category when you were in school, and increase the amount, where appropriate, in light of your new situation (e.g., you may have higher clothing costs because of requirements for employment). You can use receipts or monthly billing statements to help quantify your expenses.

Another approach is to keep a daily journal of how you spend your money. Record each purchase, including a brief description and the total amount paid. Then, develop a worksheet with columns corresponding to the major items in your budget and a row designated for each day in the week. At the end of every week, enter the data from your daily journal onto the worksheet. Continue this process for an entire month; then, tally each column on your worksheet. Repeat the process for several months to get an average, if that seems helpful. Or, do it every month.

Step 4. Determining Your Savings and Investment Needs

Many financial planners suggest that individuals begin investing at least 10 percent of their gross monthly income starting at age 21, if they plan to retire at age 65 and want the same lifestyle in retirement as they had when they were working. This can be quite sobering financial news if you have passed the age of 21 and haven't been able to follow this advice. It is important to remember, however, that it probably isn't as ominous a problem as it might seem, if you make certain to include your long-term needs in your budget planning once you begin earning an income. Your income potential as a physician should allow you to meet your goals, if you make good choices and seek the advice of certified financial planners as you need it.

There are many financial planners who specialize in helping physicians plan for their future. Your housestaff colleagues and the attending physicians where you work may be good resources in identifying a Certified Financial Planner (CFP) who can guide you.

Step 5. Doing the Math

Once you've quantified your resources, estimated both your mandatory and discretionary expenses, and determined your savings and investment needs, you are ready to do the math. This will allow you to determine if your plan balances, or leaves you with some surplus or deficit. If the resulting balance is zero, after you've subtracted your expenses and savings/investment needs from your available resources, you have a balanced budget, and you've finished. On the other hand, if you have a surplus or a deficit, you have more work to do; you must adjust your budget plan in some way.

Step 6. Adjusting Your Budget Plan

You will need to make adjustments to your budget plan if you end up with a surplus or a deficit once all the numbers are analyzed. The adjustment process is an individual matter; how you adjust your plan is up to you. A few suggestions, however, are given below.

With a **surplus,** your resources exceed your expenses/investments. You could:

- Invest more for retirement
- Select a different loan repayment plan that requires larger monthly payments
- Make loan prepayments
- Spend more on your lifestyle

With a **deficit,** your expenses/investments exceed your resources. You could:

- Reduce the amount you spend on your lifestyle
- Select a different loan repayment plan that allows for lower monthly payments
- Consider federal loan consolidation
- Adjust your investment and savings plan.

Also remember that you may have the option to postpone repayment of one or more of your loans temporarily, by requesting a deferment or forbearance on your loan(s). Although this will help with your deficit problem for only a brief interval, it may be all that's needed in the short run. Remember, though, that this may increase the total cost of the loan(s) to you. See your loan promissory note(s) and the section in this manual on deferment and forbearance for eligibility information.

Budget Planning Tools

The best way to develop your budget is to use a worksheet or spreadsheet. There are many self-help books that include budget-planning worksheets. You also can use one of the available money management or personal finance software products. Whichever approach you use, it is important to do the planning *before* you spend your income.

Important Budgeting Tips

- Get input from others in your household.
- Give the process sufficient time to help you.
- Base your budget on your needs, not on what others spend.
- Use your budget as a tool to help you manage your funds more effectively.
- Develop realistic financial and budgetary goals.
- Manage the paperwork to fit your organizational style, but keep it efficient.
- Be flexible; recognize that some months you may not achieve your budget goals.

Can You Follow Your Budget Plan?

Developing a good budget plan is very important, but if you don't stick with it, you may have more trouble achieving your financial goals. You also run the risk of increasing your consumer debt, and that debt can be both costly and undesirable for several reasons (including potential problems with credit applications).

One method for testing your ability to follow a budget is to try doing it for a very short time period—say, a weekend. You can do this by trying an experiment called "The Big Chill."

"*The Big Chill*"—An Experiment

On Thursday Night

- Determine how much you can afford to spend from Friday morning until Monday morning (i.e., your budget).
- Withdraw that amount from your account.
- Place all of your credit cards, debit cards, ATM cards, etc. (i.e., your "plastic") in a metal bowl.
- Fill the bowl with water.
- Freeze it, and keep it frozen all weekend.

Friday through Sunday

- Go out and do whatever you want with the **cash** you have available.

On Monday Morning

- Thaw out the metal bowl, and retrieve the cards.

If you run out of money sometime before Monday morning, you have only two options: (1) you must do without, or (2) you thaw out the metal bowl, and use one or more of the cards to get more cash or to buy with credit. If you have to use Option 2, you have exceeded your budget for the three days; you have not been able to live within the budget you set for yourself for this short period of time. If you are unable to live on a budget for three days, how will you be able to live on a budget for a week, a month, or a year? This is an important question to think about.

One possible solution is to "keep your plastic on ice," and live only on cash. Withdraw the cash you'll need each week based on your budget, and then put your plastic cards away so you won't be tempted to exceed that budget.

Sticking with Your Budget--Key to Financial Success

Developing and following your budget is an important key to your future financial success. The decisions you make now about your spending will have a long-term impact on your future. Your education and training have given you important tools for achieving your career and professional goals. How you use the financial resources you gain from the use of those tools will determine how well you achieve your personal goals.

II. PGY-1—Financial Management

B. Managing Educational Debt Repayment

1. Loan Repayment Terms

By Paula Abernathy
Johns Hopkins University School of Medicine

The first step toward managing your educational debt is to be aware of the repayment terms of each loan in your portfolio, including deferment or forbearance options.

"Deferment" indicates a period of time when the borrower is not required to make payments on the loan. You must apply annually for a deferment with your loan servicer. Subsidized loans will not accrue interest during a deferment period. Unsubsidized loans will accrue interest during deferments.

"Forbearance" means a period of time when the borrower is not required to make payments on the loan, or the regular payment amount is reduced. You must request forbearance from your loan servicer, and it may be granted for up to 12 months at a time. Interest accrues on all loans during a forbearance.

The most common federal loan programs, and the provisions in them that directly affect medical residents, are listed below. Refer to your promissory note for the specific terms of the loan. Your loan servicer should also be able to answer questions and help you determine if you qualify for a deferment or forbearance.

Federal Subsidized and Unsubsidized Stafford Loans

If you received your first Stafford Loan before July 1, 1993:

1. Deferment for up to 2 years while serving in an internship or residency program
2. Deferment for graduate fellowship program, unlimited number of years
3. Forbearance for economic hardship
4. Standard 10 year repayment schedule

If you received your first Stafford Loan after July 1, 1993:

1. Deferment for up to 3 years for economic hardship*
2. Deferment for graduate fellowship program, unlimited number of years
3. Forbearance while serving in an internship or residency program
4. Standard, graduated, and income-sensitive repayment plans available, but loan must be repaid within 10 years

5. Minimum monthly payment is $50

Federal Direct Subsidized and Unsubsidized Stafford Student Loans

1. Deferment for up to 3 years for economic hardship*
2. Deferment for graduate fellowship program, unlimited number of year
3. Forbearance while serving in an internship or residency program
4. Repayment options include standard 10 year, and up to 30 years for graduated, extended, and income-contingent plans
5. Minimum monthly payment is $50

Please note: Borrowers with an outstanding balance on a Stafford Loan made before July 1, 1993 are eligible to receive up to 2 years' internship/residency deferment on their Stafford or Direct Loans made after that date.

Federal Perkins Loans

For Perkins Loans borrowed <u>before</u> July 1, 1993:

1. Deferment for up to 2 years while serving in an internship or residency program
2. 10-year standard repayment plan, minimum $40 monthly payment
3. Forbearance for hardship.

For Perkins Loans borrowed <u>after</u> July 1, 1993:

1. Deferment for up to 3 years for economic hardship*
2. Deferment for graduate fellowship program, unlimited number of years
3. Standard 10-year repayment period; minimum $40 monthly payment.

Health Education Assistance Loan (HEAL)

1. Deferment for internship/residency for up to 4 years
2. Deferment for graduate fellowship up to 2 years
3. Deferment for practicing primary care up to 4 years after residency
4. Repayment may be extended up to 25 years.

Watch out for "capitalized" interest, if you decide to defer or forbear. Any unpaid interest that has accrued on your loans may be capitalized (i.e., added to the principal of the loan) before, during, or after a deferment or forbearance period. Check with your loan servicer to see how often interest is capitalized on your loan.

To qualify for an economic hardship deferment, you must meet these two criteria:

1. Your total monthly payments on your federal educational debt (estimated over a 10-year period) must exceed 20 percent of your gross monthly income, and

2. Your gross monthly income minus total monthly payments on federal debt must be less than a specified amount. This amount changes annually; check with your servicer for the precise figure.

2. Comparing the Relative Expense of Different Loan Types

By Veronica Van Gulick
University of Colorado School of Medicine

Many factors influence the "relative expense" of different types of loans. It is of utmost importance that you understand these factors, for two reasons: (1) so you understand how expensive your loans really are, and (2) so you can make informed decisions about paying back your loans (i.e. which loans(s) should you try to payoff or pay down first, second, etc). The most significant of these factors are discussed below.

Interest rate: You should know how the interest rates of your various loans are determined, as well as the current interest rates. Pay attention to whether the rate is based on the value of "prime", or the "T-bill" or another pricing index. Find out if there is a cap on the rate of interest you are being charged. Many loans that are not regulated by the Federal government do not have an interest rate cap.

Loan fees: In many cases, lenders charge fees to borrowers at the time loan proceeds are disbursed. You should find out if your lender also charges "back-end fees," which are charged to you when you begin repayment and are added onto your principal loan amount. Sometimes, "back-end fees" are a set percentage rate for all borrowers; at others, they are based on your past or present credit history. Find out how much your lenders charge.

Capitalization: Know how often your lender capitalizes interest on your loan. Some capitalize only once, when you enter repayment, while others capitalize yearly or even more frequently than that. On large loan balances, the frequency of capitalization can make a significant difference in the amount you owe.

Prepayment Penalties: Most student loans do not have prepayment penalties, but some may. Make sure that you double-check with your lender(s) to make sure you won't be penalized for paying off a loan early.

Cancellation Provisions: While all student loans that are regulated by the Federal government have provisions for cancellation of the loan if you die or become totally and permanently disabled, this is not necessarily the case with all other student loans. Check the terms of your loans. If they don't have cancellation provisions it may be wise to try to pay them off so that your family won't have to assume responsibility for your loan debt if something should happen to you.

Repayment Incentives: Some loan servicers offer repayment incentives. For example, if you are willing to have monthly payments automatically deducted from your checking account, or if you make a series of on-time payments, your percentage rate is reduced. Find out what incentives are available to you, and try to take advantage of them.

Servicing: Find out what agency will be responsible for servicing your loans. Some lenders and universities service loans "in-house"; others contract with a company that specializes in servicing student loans. It is this company that you will deal with, as you manage and repay your loans. Find out if you will be required to keep all the loans you borrowed from one lender with one servicer.

Once you understand all of these factors, you should be able to rank your student loans from most to least expensive, and thereby determine the most cost-effective plan for repayment.

3. Evaluating Loan Repayment Schedules

By Desh Hindle
Boston University Medical Center

Before choosing repayment schedules for your loans, you will first need to know what your salary is likely to be and develop a preliminary budget. You will then have an idea of how much you can afford to pay toward your student loans and can choose an appropriate repayment schedule. Conversely, you may have a particular timeframe in mind for repaying your student loans (related to anticipated family, education, or other expenses). Ideally, you should choose a plan that maximizes flexibility, while minimizing cost. Although options may vary from lender to lender, there are several basic types of repayment schedules. Keep in mind that the longer you take to repay a loan, the more costly it will be.

Standard Repayment

This is the "default" schedule that will be assigned to you if you do not request otherwise. For Guaranteed Student Loans (GSL), Stafford Loans, Direct Loans, and Supplemental Loans for Students (SLS), payments are made over 10 years. For HEAL loans, the repayment period is 25 years. You may request a shorter term on HEAL if you wish. Payments under a standard schedule change only as the interest rate fluctuates.

Graduated Repayment

Graduated schedules vary, but they all seek to accomplish the same thing: to give you payment relief when your income is lowest. This is accomplished by requiring only interest payments for some initial fixed period, followed by principal and interest payments over the remainder of the term. With some graduated schedules, the payment amount increases in several "steps." When the payment amount levels off, it is higher than it would have been under a standard schedule, to make up for the amounts that were not paid early on.

Income-Contingent Repayment

This is a variation on the graduated schedule, and is not available on every educational loan. Payments are calculated as a percentage of your adjusted gross income, and only increase as your income increases. Payments are sometimes capped at an amount slightly less than that required under a "standard" schedule. As with graduated repayment, lower initial payments are balanced by inflated payments later on.

Extended Repayment

If you are looking for a lower required payment, but can afford to make extra payments occasionally, an extended schedule may work best for you. By extending the term from 10 years to 25 or 30 years, you significantly decrease the required payment amount. Of course, you also significantly increase the total amount of interest paid over the life of the loan. You could combine the cost advantages of the standard schedule and the convenience of the extended schedule by signing up for an extended schedule with a low required payment, but making a payment equivalent to what you would have paid under a standard schedule (with the excess credited to the principal balance). You will pay the loan off in about 10 years, and gain a good measure of flexibility, since you can opt to make only the lower required payment if emergency expenses arise. Keep in mind that making extra monthly payments requires some footwork, as lenders do not always credit unscheduled payments correctly. You might consider making a large lump-sum payment to principal each year.

Take a look at the comparison illustrated in the table below. In each example, we assume that total debt at the start of repayment (original principal borrowed, plus accrued interest during school, grace and deferment) is $150,000. The interest rate ordinarily could be variable, but is fixed at 8 percent for the purpose of this example. Keep in mind that these figures are approximate, and that the specific provisions of graduated and income-contingent schedules can vary by lender and loan program.

<table>
<tr><td>Repayment Schedule</td><td>Payment Amount</td><td>Total Cost to Repay</td></tr>
<tr><td>Standard - 10 years</td><td>$1,820 for 120 months</td><td>$218,400</td></tr>
<tr><td>Graduated - 10 years</td><td>$1,000 for 24 months
$2,121 for 96 months</td><td>$227,616</td></tr>
<tr><td>Income Contingent - 15 years*</td><td>$413 for 6 months
$434 for 12 months
$1,575 for 12 months
$1,633 for 150 months</td><td>$ 2,478
$ 5,208
$ 18,900
$244,950
$271,536 total</td></tr>
<tr><td colspan="3">*Assumptions: Repayment begins in January of the PGY-3 year of a 4-year residency, when AGI is $33,057; 5 percent salary increase in PGY4; starting salary in the first year of practice $126,000 with 5 percent increases thereafter. Payment will cap at the amount required to pay original loan under a 12-year schedule ($1,633). Different lenders will have different ways of calculating the income-contingent amount.</td></tr>
<tr><td>Extended - 25 years</td><td>$1,158 for 300 months</td><td>$347,400</td></tr>
</table>

Some Web sites include payment calculators to help you compare various repayment options:

- The Crestar Bank Student Lending Page has calculators at this site: http://www.student-loans.com/
- Sallie Mae, a student loan secondary market, has calculators at this site: http://www.salliemae.com/
- The FinAID Page contains a number of calculators at this site: http://www.finaid.org/
- A Federal Direct Loan calculator can be found at this web site: http://www.ed.gov/offices/OSFAP/DirectLoan/calc.html.

If you prefer doing your own calculations, refer to the following chart, which appears courtesy of the Department of Health and Human Services Division of Student Assistance. With a little planning now, you can save thousands of dollars in loan repayment later, while minimizing the stress that can accompany loan repayment.

DIRECTIONS TO ESTIMATE YOUR MONTHLY AND TOTAL EDUCATIONAL LOAN REPAYMENT

1. Column A lists the federal loan programs and provides space for your non-federal loans. Write the interest rates in Column B that apply to your loans. Note: Certain programs are listed twice in case you have multiple lenders/holders.

2. Put principle borrowed in Column C. For loans accruing interest before you begin repayment (e.g., HEAL & SLS), add the interest to the principal. (Your financial aid officer or lender/holder can help you estimate the interest accrued.)

3. Place the applicable loan repayment ratio from the chart below in Column D. The ratio is based on the interest rate of the loan and the number of months to repay (e.g., a 9% Stafford loan with a 120-month repayment period has a ration of .01267). To estimate repayment ratios for variable interest rate loans, check with lenders/holders or the financial aid office.

Loan Repayment Ratios Chart

Interest Rate	60 Mons.	120 Mons.	180 Mons.	240 Mons.	300 Mons.
5%	.01887	.01061	.00791	.00660	.00585
6%	.01933	.01110	.00844	.00716	.00644
7%	.01980	.01161	.00899	.00775	.00707
8%	.02028	.01213	.00956	.00836	.00772
9%	.02076	.01267	.01014	.00900	.00839
10%	.02125	.01322	.01075	.00965	.00909
11%	.02174	.01378	.01137	.01032	.00980
12%	.02224	.01435	.01200	.01101	.01053
13%	.02275	.01493	.01265	.01172	.01128
14%	.02327	.01553	.01332	.01244	.01204
15%	.02379	.01613	.01400	.01317	.01281

4. Multiply the entries in Columns C and D to calculate the estimated monthly repayment. Place the results in Column E. (Monthly repayments may not be less than $50 per month for Stafford, SLS and HEAL; $30 or $40 for Perkins; or $15 for HPSL, NSL, LDS and PCL). These are estimates and not exact amounts, especially for variable interest-rate loans.

5. Complete Column F by filling in the maximum number of months you have to repay each loan. The federal loan programs listed have standard maximum 10-year (i.e., 120-month) repayments, but HEAL and federal consolidation loans permit repayments up to 25 years (i.e., 300 months).

6. Multiply the entries in Columns E and F to calculate the estimated total repayment on each of your loans. Place these results in Column G.

4. A Basic Primer on Loan Consolidation

By Paul Garrard
Association of American Medical Colleges, Washington, D.C.

One of the least understood repayment options for student loan borrowers is loan consolidation. Whether or not a borrower should consolidate his or her loans is a very personal decision, and while the decision to consolidate loans may be the right decision for some, the decision can be quite wrong for others. So, students are encouraged to ask some key questions before making the decision to consolidate their loans.

1. What exactly is "loan consolidation"?

Loan consolidation is a way to refinance, or pay off, multiple loans with one brand-new loan. In fact, in the HEAL program, loan consolidation is actually referred to as "HEAL Refinancing."

2. Why do borrowers consolidate their student loans?

Borrowers consolidate loans for many different reasons, but three of these are particularly common.

First, they do it for **convenience.** Borrowers who have multiple loans serviced at multiple loan servicers may find it easier to deal with one loan servicer than several. Remember the key element here is multiple loans at multiple loan servicers. Borrowers with multiple loans serviced at the same loan servicer likely already have the convenience of making one payment against all their loans. This is often referred to as the "serialization" of loans. Technically, this means that the same organization owns all the loans, but some also use the term to refer to a borrower who has all of his or her loans serviced at the same loan servicer.

Second, borrowers consolidate to **improve their cash flow**. Some borrowers may be find that they can save money by securing a lower interest rate through loan consolidation. Others may be forced to consolidate to access repayment terms beyond ten years (which, although improving their monthly cash flow, will most certainly add to their total repayment costs).

Third, borrowers consolidate to access **additional deferments**; some discover that they can to gain access to additional deferments when they consolidate all of their student loans. This actually helps improve "cash flow," but is still listed here as a separate reason a borrower might consolidate.

3. How do I actually consolidate my student loans?

In general, you should probably consider contacting the organization(s) that currently services your student loan(s), referred to as the "loan servicer" or the "holder" of your student loan(s). The holder is the organization who actually owns your student loans and to whom you owe repayment. The holder may or may not be the same organization as your loan servicer, but this is usually a good place to start. Many loan servicers list a toll-free number in their routine borrower correspondence.

4. What kinds of loan consolidation programs are available?

In general, there are three kinds of loan consolidation available for borrowers. Technically, "federal" loan consolidation includes both FFELP and FDSLP, but they are listed here separately. The three types of loan consolidation include:

- **Federal Family Education Loan Program (FFELP) or "Federal Loan Consolidation,"** as offered by what some would call "traditional" programs such as Sallie Mae, banks, and other lenders.
- **Federal Direct Student Loan Program (FDSLP) or "Federal Direct Loan Consolidation,"** the government's loan consolidation program, available only to (1) borrowers with Direct Loans, (2) borrowers who attended a school that participates in the Direct Loan Program but who only have Stafford Loans in FFELP, or (3) FFELP Stafford loan borrowers who cannot find an acceptable income-sensitive repayment consolidation option in FFELP.
- **HEAL Refinancing**, available to HEAL borrowers who want to consolidate their HEAL loan(s) into one new HEAL loan.

5. When is the best time to consolidate my student loans?

The answer to this question will vary by borrower. However, those who view loan consolidation as a "repayment option" might encourage you to consider loan consolidation once you have exhausted any grace and deferment options for which you or your loans may already be eligible. However, once again, the best time to consolidate will vary by borrower and may, in addition, vary according to the types of loans you are considering consolidating.

There will be more details on this later; one example will suffice for now. A borrower with a lengthy residency who is eligible for additional deferments when he or she consoliates, may want to wait and use up all available deferment options first before gaining access to additional ones through consolidation. However, a borrower with a 3-year residency may not need additional deferments and, for other reasons, might choose to consolidate earlier.

6. What are some of the advantages and disadvantages to loan consolidation?

This is a difficult question to answer, which requires a lengthy answer. It will be considered in more detail in the section, "Some Questions to Ask Before Consolidating Your Student Loans," which follows. However, when weighing both the advantages and disadvantages of loan consolidation, you may want to consider what you "give up," as well as what you "get,'' when you consolidate your student loans.

7. So, how can I tell if loan consolidation is right for me?

Once again, you may want to read the section, "Some Questions to Ask Before Consolidating Your Student Loans," before making your decision. Remember, loan consolidation is a very personal decision, and just because loan consolidation is right for someone else doesn't mean it's right for you. Also, remember that although there are some exceptions, in general, all the loans you consolidate take on the characteristic(s) of the new consolidation loan, including interest rate and deferment eligibility, so be sure you know what you new consolidation loan will "look" like before you consolidate.

Get Details on the Terms Involved before Consolidating Student Loans

1. What is the interest rate on my new consolidation loan? Is this rate fixed or variable? If the rate is variable, is there an interest rate cap?

Effective for new consolidation loan applications received on or after February 1, 1999 in either the FFELP or FDSLP loan consolidation programs, the interest rate will be a weighted average of all the loans being consolidated rounded to the nearest higher one eighth of one percent, fixed for the remainder of repayment. This weighted average rate can never exceed 8.25 percent. Once again, whatever rate is assigned to the new consolidation loan is fixed for the remainder of repayment.

The interest rates for HEAL Refinancing vary according to lender, but all are variable and are tied to the 91-Day Treasury Bill (the 91-Day T-Bill or 13-week T-Bill).

Two important notes for HEAL borrowers who consolidate HEALs into FFELP consolidation: First, the interest rate on those HEAL loans being consolidated is not used in the weighted-average calculation for the new FFELP consolidation loan. Second, even though the borrower technically has one new consolidation loan, the interest rate assigned to the HEAL portion of the new consolidation loan is the 91-Day T-Bill plus 3.0 percent, regardless of the interest rate on the HEAL loan(s) being consolidated.

Two similar, and equally important, notes for HEAL borrowers who consolidate HEALs into FDSLP consolidation: First, the interest rate on those HEAL loans being consolidated is used in the weighted-average calculation for the new FDSLP consolidation loan. Second, there is only one interest rate in effect for the new FDSLP consolidation loan, even when HEALs make up part of the mix. Therefore, HEAL borrowers who are eligible for FDSLP consolidation can get their underlying HEAL loans at the same fixed, capped rate since they are "part" of the new FDSLP consolidation loan.

2. How long will it take to consolidate my student loans? What happens to the status of my student loans if they are in grace, deferment, or forbearance while I am applying for my consolidation loan?

The length of time required by a lender to consolidate your student loans depends on several factors, not least of which is how many different loan servicers have to be contacted for payoff information on the loans you are consolidating. You should ask your consolidating lender this question, but don’t be surprised if the process takes between 45 and 60 days.

Borrowers are well advised to keep their loans in their current status, be that grace, deferment, forbearance, or actual repayment, while waiting for the consolidation process to be completed.

3. What repayment options are available to me with my new consolidation loan? Do I have access to standard, graduated, income- based, and extended-repayment options?

Standard, graduated, income-based, and extended-repayment options should be available to all borrowers who consolidate in either FFELP, FDSLP, or HEAL Refinancing.

4. What is the both the monthly payment amount as well as the total repayment amount of my new consolidation loan?

This is a question you should ask of your new consolidating lender, as the answer will obviously vary depending on both the type and amount of loans being consolidated. Remember that as your monthly loan payment goes down, in all likelihood, your total repayment dollars will go up, often quite substantially if you extend your repayment over many years.

You may be able to estimate your repayment amounts with loan consolidation through the use of loan calculators available on various lender or servicer web sites. In addition, your loan program may have debt management software available to help you run the numbers for loan consolidation.

5. Can I pay off my consolidation loan early without penalty, and how are early payments applied?

There is never an interest penalty for early repayment on student loans. You can expect any payments on Federal student loans, including FFELP and FDSLP Loan Consolidation, plus HEAL Refinancing, to be applied to outstanding interest first, then to principal.

6. What happens to the grace, deferment, and forbearance provisions of my student loans when I consolidate? Do I either lose or gain deferment options when I consolidate my student loans?

This is a tricky question, and requires a lengthy answer, with a request that borrowers always check with your loan servicer about this.

In general, with the exception of refinancing HEAL loans into one new HEAL loan through HEAL Refinancing, borrowers who consolidate their student loans in either FFELP or FDSLP lose their current grace, deferment, and forbearance provisions when they consolidate. Just remember that when you consolidate, your old loans "go away," and in general, so do the provisions attached to them.

This is especially important for HEAL borrowers to remember, as HEAL borrowers who consolidate their HEALs with Staffords through FFELP or FDSLP lose their grace and deferment provsions on the HEALs being consolidated.

"Old" borrowers who consolidate all their outstanding Stafford Loans at the same time may gain access to additional deferments through both FFELP and FDSLP Consolidation. In general, these borrowers may apply for the economic hardship deferment on their new FFELP consolidation loan. In addition, these borrowers may "refresh" or extend their two-year residency deferment if they consolidate through FDSLP Consolidation, in addition to being eligible to apply for the economic hardship deferment on their new FDSLP Consolidation Loan.

"New" borrowers who consolidate in FDSLP loan consolidation may apply for up to an additional 3 years of economic hardship regardless of whether or not they have already exhausted their economic hardship deferment eligibility, but this is not the case for "new" borrowers who consolidate through FFELP.

7. Do I have access to repayment incentives and "borrower benefits" with my new consolidation loan?

Once again, in general, the underlying loans you are consolidating are "gone" when you refinance or consolidate them. Therefore, in general, any repayment benefits you had associated with those loans are also gone, as the loans are gone.

Some consolidating lenders may offer repayment benefits on the new consolidation loan, but this is not routinely the case.

8. Who is the servicer of my new consolidation loan? Should the lender of my new consolidation loan sell my consolidation loan to another lender, will the servicer remain the same?

This is a question to ask your consolidating lender, and although it is unlikely that your consolidating lender will sell your new consolidation loan to another lender, you should ask if the loan servicer will remain the same should this occur.

9. Do I lose the interest subsidy on my subsidized loans when I consolidate?

Effective for new consolidation loans in either FFELP or FDSLP for applications received on or after February 1, 1999, Federal Subsidized Staffords maintain their interest subsidy as long as the new consolidation loan is in deferment. This has always been the case for Subsidized Staffords consolidated in FDSLP, but is now also the case in FFELP loan consolidation.

Federal Perkins Loans consolidated through FDSLP maintain their interest subsidy as long as the new FDSLP consolidation loan is in deferment. However, such is not the case for Perkins Loans consolidated through FFELP.

HPSL loans consolidated in either FFELP or FDSLP consolidation do not maintain their interest subsidy.

10. I have a spouse with student loans. What are the implications should we decide to consolidate them together?

There are many in both the financial aid community as well as the lending community who would strongly caution borrowers against joint spousal consolidation. In general, both parties become jointly and severally liable for repayment on a joint spousal consolidation loan, something that could result in one or both borrowers' credit rating being adversely impacted in the event of separation or divorce. In addition, although borrowers should check with their loan servicers, both borrowers in a joint consolidation loan have to meet the same requirements in order for the new consolidation loan to be eligible for additional deferments.

11. Which of my loans can be consolidated, and which cannot?

The following loans can be consolidated: Federal Subsidized and Unsubsidized Staffords (FFELP and FDSLP), GSL, SLS, HPSL, HEAL (together or with Staffords), Perkins.

12. Are there any fees or hidden costs when I consolidate?

Your lender should not charge you anything to consolidate. However, some look at the increased interest cost on consolidation loans that often results from extended repayment as a "hidden" cost, as remember, for the convenience of a lower monthly payment, you may pay substantial additional interest charges, depending on how long your repayment terms are. In addition, many unsubsidized loans, perhaps most, capitalize accrued and unpaid interest at "repayment," which would include at the time the borrower consolidates his or her loans.

5. Loan Repayment and Forgiveness Programs

By Teddie Milner
University of California, Los Angeles, School of Medicine

Loan repayment and forgiveness programs (in which your loans are paid in exchange for work or military service) offer an option for easy repayment. Several options are available to eliminate or reduce your student loans. This section provides information on federal and state initiatives for loan repayment and forgiveness programs.

Federal Programs

Federal programs, which are always subject to change, are intended to recruit quality candidates who are primarily interested in service to the under-served. For residents with certain career goals, these programs can be an excellent opportunity to eliminate or reduce educational debt.

Disadvantaged Health Professions Faculty Loan Repayment Program

The purpose of the Disadvantaged Health Professions Faculty Loan Repayment Program is to attract physicians from disadvantaged backgrounds to become, or to continue to be, full-time or part-time faculty members at health professions schools.

The Department of Health and Human Services defines an individual from a disadvantaged background as someone who: (1) comes from an environment that has inhibited the individual from obtaining the knowledge, skill, and abilities required for access to higher education; or (2) comes from a family with an annual income below a level based on low income thresholds. Students who meet one of these criteria often receive certain federal grants or loans when they are enrolled in medical school. If you were the recipient of an Exceptional Financial Need (EFN) Scholarship, a Financial Assistance for Disadvantaged Health Professions Students (FADHPS) Scholarship, a Scholarship for Disadvantaged Students (SDS), or Loan for Disadvantaged Students (LDS) while in medical school, you qualify as a physician from a disadvantaged background.

The Department of Health and Human Services pays up to $20,000 per year for each year of eligible service; there is a minimum two-year commitment. This amount is paid in addition to the faculty salary or other payments by the school. Loan repayments are considered taxable income. Upon written request, the Department also pays 39 percent of the loan repayment to cover increased Federal, state, and local income tax liability resulting from the loan repayments.

Contact: Mr. Jeff Potts, Accountant
Division of Student Assistance
Bureau of Health Professions
Health Resources and Services Administration
Parklawn Building, Room 8-34
5600 Fishers Lane
Rockville, MD 20857
(301) 443-1700

Indian Health Service (IHS) Loan Repayment Program

This program provides residents or physicians up to $30,000 per year (for a two-year minimum commitment) toward repayment of health professions educational loans while working for the IHS. This is in addition to a salary and benefits. IHS also will pay up to 31 percent of the increased federal tax directly to the Internal Revenue Service on your behalf. Priority is historically given to residents and physicians in the fields of Family Medicine, Internal Medicine, Obstetrics-Gynecology, Pediatrics, Geriatric Medicine, Podiatric Medicine, and Psychiatry. You will be required to fulfill your contract service agreements through full-time clinical practice at an Indian health program site determined by IHS.

Contact: Indian Health Service
Loan Repayment Program
12300 Twinbrook Parkway, Suite 100
Twinbrook, Metro Plaza
Rockville, MD 20852
(301) 443-3396

National Health Service Corps (NHSC) Loan Repayment Program

The NHSC, a component of the Health Resources and Services Administration, offers forgiveness programs to physicians who agree to practice for a set number of years in areas that lack adequate medical care, including remote and/or economically depressed regions. Eligible medical disciplines include Family Practice, General Pediatrics, General Internal Medicine, General Psychiatry, and Obstetrics-Gynecology. This program provides up to $50,000 for loan repayment for a two-year commitment, and up to $35,000 for each additional year of service. This is in addition to your salary and benefit package. Furthermore, NHSC pays 39 percent of the loan repayment to cover income tax liability.

Contact: Division of Scholarships and Loan Repayments
Loan Repayment Programs Branch
Bureau of Primary Health Care
4350 East-West Highway, 10th floor
Bethesda, MD 20814
(800) 435-6464 or (301) 594-4400
E-mail: feedback@hrsa.dhhs.gov
http://www.bphc.hrsa.dhhs.gov/

National Institutes of Health (NIH) Educational Loan Repayment Programs

NIH offers three loan repayment programs:

- The NIH AIDS Research Loan Repayment Program is designed to attract highly qualified physicians to HIV/AIDS research and research training.
- The NIH Clinical Research Loan Repayment Program is designed to recruit highly qualified physicians from disadvantaged backgrounds to serve as clinical researchers.
- The NIH General Research Loan Repayment Program is designed to attract highly qualified physicians to conduct research at the NIH.

The programs pay a maximum of $35,000 a year toward outstanding eligible educational debts for a minimum two-year commitment in the AIDS and Clinical Programs or a minimum three-year commitment in the General Program. This is in addition to your salary and benefits. You also may apply for annual contract renewals and continue to receive loan repayment benefits. In addition, the AIDS and General Programs make tax payments directly to the Internal Revenue Service on your behalf, and the Clinical program provides for Federal, state, and local tax reimbursement benefits to offset increased tax liability.

Contact: National Institutes of Health
Marc Horowitz, J.D.
Director, Loan Repayment
7550 Wisconsin Avenue
Federal Building, Room 604
Bethesda, MD 20892-9121
(800) 528-7689 or (301) 402-5666
e-mail: LRP@NIH.GOV
Web site: http://www.training.nih.gov/

Resident Repayment Program

This program reimburses first- or second-year family practice residents who desire to work as physicians in a rural or inner city area or serve as full-time family medicine faculty members. The program pays up to 75 percent of the interest accrued on educational loans while you are in residency and in the first year of practice in an under-served area (up to $2,500 per year; maximum of $10,000 over a four-year period).

Contact: The American Academy of Family Physicians Foundation
P.O. Box 8418
Kansas City, MO 64114-0418
(800) 274-2237 ext. 4470
Web site: http://www.aafp.org/aafpf/

U.S. Air Force, Army, and Navy Financial Assistance Program

The Financial Assistance Program (FAP) is offered to medical residents and is designed to supplement your residency salary and reduce the necessity for incurring further debt. You will receive an annual grant of over $19,800 and a monthly stipend of more than $930, a total of more than $30,000 for each year you participate. You will be commissioned as a medical officer and will have a minimum obligation of two years' active duty service upon completion of residency training for your first year of participation. Additional years of participation will extend your active-duty commitment year for year.

Contact:

Air Force:
Headquarters, US Air Force Recruiting Service
Medical Recruiting Division
Randolph AFB, TX 78150-5421
(800) 423-8723

Army:
Headquarters, Department of the Army
ATTN: SGPS-PDF
5109 Leesburg Pike
Falls Church, VA 22041-3258
(800) 872-2769

Navy:
Commmander, Navy Recruiting Command
4015 Wilson Boulevard
Arlington, VA 22203-1991
(800) 872-6289

U.S. Army and Army Reserve Loan Repayment Program

Participating physicians are eligible to receive payment toward the outstanding balance of their student loans in exchange for service in the Army or the Army Reserve.

The Army pays up to one-third or $1,500, whichever is greater, on the outstanding loan balance for each year of successfully completed active service. The maximum benefit repaid is $55,000. When a loan exceeds $55,000, one-third of $55,000 will be paid for three years. The unpaid principal balance will be paid, but no payments are made for delinquent charges or interest that has accrued because of default.

The Army Reserve pays up to 15 percent or $500, whichever is greater, on the outstanding loan balance for each completed year of satisfactory service. The maximum benefit repaid is $10,000 except for selected specialties that have a maximum of $20,000.

U.S. Army Reserve Health Professionals Loan Repayment Program (HPLR)

This program seeks to attract health professionals with certain combat medical skills to serve in the Selected Army Reserve. You receive up to $3,000 per year, for each year of service, toward repayment of your student loans. The maximum benefit repaid is $20,000.

U.S. Army Reserve Health Professional Bonus Program

This program seeks to attract board-certified/board-eligible physicians to serve in the Army Reserve. You receive a $10,000 bonus per year for each year of service. A maximum of three years' participation is allowed, for a total of $30,000. Eligible specialties include Thoracic Surgery, Orthopedic Surgery, Diagnostic Radiology, Family Practice, and Emergency Medicine.

U.S. Army Reserve Specialized Training Assistance Program (STRAP)

This program seeks to attract residents who are specializing in Thoracic Surgery, Orthopedic Surgery, Peripheral Vascular Surgery, Neurosurgery, Urology, Diagnostic Radiology, Family Practice, or Emergency Medicine. You will receive a monthly stipend which will total over $12,000 per year of participation. You will be commissioned as a Captain in the Army Medical Corp. Upon completion of your residency, you will owe the Army Reserve Medical Department two years for every year you receive the stipend. You will train at a local Reserve medical unit. The degree of participation required varies between programs that best fits your needs.

U.S. Naval Reserve Loan Repayment Program

The Naval Reserve is a force of highly trained people available in a national emergency to meet the expanded needs of the regular Navy. It offers a loan repayment program to certain physician specialists who have completed their advanced training. Most reservists serve in a part-time status consisting of two days a month and an annual two-week period of duty called Annual Training (AT). You can earn loan repayment of up to $3,000 after each year of satisfactory service performed. The maximum loan repayment is $20,000.

State or Community Programs

Many individual states or communities have initiated loan forgiveness or repayment programs for health care professionals. Many states also have programs in which the states get matching funds from the Federal Government to assist physicians in public clinics or private non-profit practices. Each program will be unique and will require careful investigation before you make a commitment. Some of them are restrictive in terms of specialty choice; others are not. Most limit practice location for a specified period of time to the specific community or state affiliated with the program.

State Offices of Rural Health, State Rural Health Associations, and State Departments of Public Health

These offices may offer loan forgiveness or repayment programs based on state legislature. Contact your state’s office for additional information. If legislation is approved by the state, these approved programs may be administered through one of these offices.

State Primary Care Associations

Many states have Primary Care Associations, which often receive listings for jobs in primary care that include loan repayment in their benefit packages. Primary Care Associations can usually be reached through State Departments of Public Health.

National Health Services Corps State Loan Repayment Program (SLRP)

The NHSC State Loan Repayment Program is a part of NHSC's overall strategy to improve access to primary and preventive health services for under-served communities and vulnerable populations. NHSC provides funds directly to states for the operation of Loan Repayment Programs. Currently, 36 states participate; however, the terms of the programs vary considerably from program to program. Consult the Association of American Medical Colleges (AAMC) Division of Student Affairs and Education Services book entitled, "State and Other Loan Repayment/Forgiveness and Scholarship Programs," for detailed information on state programs. This is available on the Web at the AAMC home page: http://www.aamc.org/

6. Developing a Loan Repayment Strategy

By Desh Hindle
Boston University Medical Center

The most important requirement for a successful educational loan repayment strategy is that it should reflect your own personal goals and circumstances. This "customization" of repayment requires some background on the basic tools that are at your disposal. These include vehicles for postponing payments, extending or graduating payments, consolidating loans, and accessing loan repayment programs – all discussed earlier.

Now, it's time to take a broader view. Think about these issues, as you ponder your many options:

- How long do you expect your training to last?
- Do you expect a gradually increasing salary—or could there be significant leaps and dips as you move from one training or practice activity to another?
- Are there any assets available for debt repayment?
- What kinds of changes do you anticipate in your personal life that could impact your financial situation (i.e., marriage, having children, moving)?
- Is it important to you that you repay your educational debt prior to a child entering high school or college?
- Are you motivated to minimize the total cost of your educational debt, or to keep finance charges within a certain ratio relative to your original principle balance?
- What other kinds of expenditures will be competing for your attention? Purchasing a house? Raising a child? Buying into a practice? Saving for your retirement? Purchasing life insurance? Paying off credit card bills?

A successful debt repayment strategy will take these kinds of issues into account. Because repaying student loans is so inextricably tied to the rest of your life goals, it is best to review your options within the context of an overall financial plan. While developing a repayment strategy, consider following these steps:

1. Set some initial repayment guidelines:

- What amount can you afford to pay per month?

- How much are you willing to pay in interest? Or said another way, how much are you willing to repay for each $1 you borrowed?
- What is your target deadline for repaying your entire educational debt?

2. Express your guidelines in specific terms:

- See the section, "Estimating Monthly Payments," for a listing of the repayment calculators available on the Internet, and a chart for estimating payment amounts manually.
- If you have access to Microsoft Excel, or comparable spreadsheet software, utilize its amortization function. In Excel, the formula reads:
- =PYMT(R,T,-P)
- when R = annual interest rate, expressed as a decimal, divided by 12 (this yields the monthly rate)
- T = term (length of repayment) in months
- P = principal balance at the start of repayment.

3. Use the results to evaluate the feasibility of your original guidelines:

The following example helps to illustrate the planning process. Mai, a third-year resident anticipating entry into practice in PGY-4, has the following educational debts:

$20,000 institutional loans

$34,000 subsidized Stafford loans

$80,000 unsubsidized Stafford loans ($113,000 by the start of repayment)

$20,000 private loans ($27,150 by the start of repayment)

TOTAL at the start of repayment: $194,150

Deferment: During residency training, Mai’s institutional and private loans have been in a grace period. She has applied each year for an economic hardship deferment on her Stafford loans. Her debt-to-income ratio qualified her for deferment each year, so interest has not been accruing on her subsidized Stafford loans.

Current Interest Rates: Mai's unsubsidized Stafford loans charge various rates, averaging about 7.5 percent, and have a lifetime cap of 8.25 percent. Her private loans are currently charging 6.5 percent, and have no cap on the rate. The institutional loans will begin to charge a fixed rate of 7 percent when she enters practice.

Payments: Mai has been saving up money each month, and has occasionally made voluntary payments on her private loans. Even though her private loans are charging a lower rate right now, she knows the rate is not capped. The prospect of the private-loan rate rising in the future has been causing her some worry, so she elects to target it for all extra payments. She is also considering consolidating her Stafford loans together to "lock in" their current rate.

Goals: Looking ahead to repayment, Mai decides to group all of her debt into one lump sum, for estimating her payments. Since all of her current interest rates are within a 1 percent range, she decides that this would make her job simpler.

After meeting with a financial planner to review her broader goals and estimating a starting salary of about $120,000, Mai decides she can comfortably afford to pay about $2,500 a month without neglecting other things that are important to her.

She'd also like to try to pay back no more than $2 for every $1 that she borrowed.

Finally, she wants to pay off all of her student loans within about 8 years, because she doesn't want her educational debt to interfere with possible family-related expenses that may exist by that time.

Results: Monthly payment required over 8-year term at 7.5 percent rate: $2,640.02

In Excel: PYMT(.0063,96,-190150)

The balance at repayment of $190,150 reflects a $4,000 reduction, because of the 36 voluntary monthly payments of $100 that Mai made on her private loan during her residency. The extra $400 savings results from interest that will not be charged during each month of repayment on the $3,600 of principal that was paid off during the interest-free residency years. This lowers the monthly repayment amount by $56.

Repayment Ratio is $1.67 for each $1 borrowed.

Finance charge = $103,041.92.

Total of payments = ($2,640.02 x 96) + $3,600 = $257,041.92

Original amount borrowed = $154,000.00

$257,041.92 / $154,000.00 = $1.67

Decision: Mai now has to decide whether she can afford an extra $150 per month above the amount stipulated in her original projection. Her decision will depend on how important it is to her to have the debt repaid within 8 years. Using the Excel formula again, she calculates that it would take about 8-1/2 years to repay her debt at $2,500 per month. This would also mean about $1,800 in extra interest charges.

Mai remembers that her private-loan interest rate could increase over time, and, if they did, her payment amount would increase proportionally. Therefore, to play it safe, she decides to go with a 10-year repayment schedule on all loans – the total monthly payment projected by her lenders is $2,260. While rates remain low, she will pay an extra $380 per month to her private lender. This way, she will pay enough to eliminate her total debt within 8 years at current interest rates, while distributing a larger proportion of her early payments to the debt that carries the most risk. Once the private loan is paid off, she will divert the extra payment to her Stafford loans.

Mai is also planning to negotiate some educational debt repayment with her prospective employers as a signing bonus, which could remove some of the burden of repayment during her early years of practice.

Someone else could easily come up with a completely different strategy, given the same set of circumstances. For instance, some would choose to pay Stafford loans more aggressively, since their current rate, in this example, was higher. Whatever your personal preferences, the decision-making **process** might well follow a similar pattern.

Seek advice from both a financial planner and a debt management counselor who works with residents and young physicians. More and more hospitals are offering debt management counseling services, as a benefit, or through an associated medical school's financial aid office.

The Association of American Medical Colleges (AAMC) offers many resources through its Web site, at http://www.aamc.org/. Also, the AMA offers assistance in resolving difficulties with lenders, through its office of Resident Services (312-464-5529).

II. PGY-1—Financial Management

C. Saving and Investing for Short- and Medium-Term Goals

By Mid Tilghman
Dennis M. Gurtz and Associates, Bethesda, Maryland

This section offers suggestions about saving and investing for the first five years after medical school.

Your Cash Reserve

The first savings goal for every physician should be to have an adequate **cash reserve.** This will provide you with sufficient funds should an emergency, such as an unexpected car or home repair, or an opportunity, such as deciding at the last minute to go on a vacation or buy a VCR on sale, arise. While the wide availability of credit cards lets individuals make most purchases without having the money to pay for them, the objective of every medical school graduate should be to get out of debt as quickly as possible—and not to add to a potentially staggering debt/interest load. These cash reserves, therefore, are the means that will allow you to purchase the things you want or need and pay for them without incurring new debt.

Your cash reserve dollars should be held or invested in safe (i.e., with no attendant risk to your principal) and liquid (i.e., easily accessible) instruments that will work as hard as possible for you within the confines of limited risk.

The amount in your cash reserves depends on your personal objectives, combined with a sense of how much financial comfort you require. Some financial advisors suggest a cash reserve amount equal to three to six months' of your monthly expenses or take home pay; others suggest a fixed amount of $3,000 to $15,000. Based on a typical resident's salary, we usually suggest an amount of $5,000 to $10,000. You don't have to accumulate the money for your reserves right away. You can start out with just a few dollars, and then increase the balance each month with a systematic savings program. The key here is to select a dollar amount for your cash reserve that feels right for you, and then establish a time frame for trying to reach this goal. If, in the interim, you find that you need to spend some of the cash reserves, that's okay. The most important point here is to start saving today and keep on saving, every month.

Your Primary Reserve

Your Cash Reserve should be divided into two parts: your "primary reserve" and your "secondary reserve." Your primary reserve dollars should be in a companion/complimentary savings or money market account in the same financial institution as your checking account. This may reduce or eliminate service charges. These dollars are your first line of "debt defense." Once this account is opened, an automatic monthly payroll-savings deduction should be established, at a minimum of $25 per pay period. In addition, any extra funds that you earn or are given might initially be deposited here. Your goal for this account is to have a balance of $2,000 to $4,000.

Your Secondary Reserve

Ideally, your secondary reserve dollars should be held in a higher-yielding instrument, one that you can add to, or withdraw from, without a penalty. These accounts still need to be relatively liquid. Some suggestions for this account are 3-, 6-, or 12-month Certificates of Deposit, credit union money market or term accounts, and taxable or tax-exempt cash management mutual funds. The best type for you will depend on your familiarity and comfort with a particular account and, possibly, your marginal tax bracket. This account should hold those funds that you do not anticipate needing for day-to-day expenses or as your first line of "debt defense" dollars. Based on your previously assumed cash reserve target level, this account should have a balance of $5,000 to $8,000.

Your secondary reserve account should be funded by two methods. The first is a monthly payroll savings deduction, of at least $25 per pay period. This deduction is in addition to the one intended for your primary reserve account. The second source of funding is any excess dollars that you earn, money you receive as gifts, or money that is between investments. If you accumulate funds in your primary cash reserve account that exceed your desired target, you should periodically transfer them to your secondary reserve account.

Funding Short- to Medium-Term Financial Goals

After both primary and secondary reserve accounts have been established, and their funding programs put in place, you need to decide on the time frame and amounts of your next short- to medium-term financial goals. These are goals you'd like to accomplish within two to four years, such as the purchase of a home or a share of a medical practice. A general rule of thumb for investing your funds for the accomplishment of goals within this time frame is that the shorter the time frame, the less the investment risk (potential loss of principal) you should take.

Reasonable investments for these funds can range from adding them to your secondary reserve account to investing them in longer term certificates of deposit or short-term bond mutual funds. Remember the saying, "Pigs get fat; hogs get slaughtered." Don't put these dollars at undue risk, because you want them, and their earnings, to be available when you need them.

In summary, the critical components of achieving short and mid term financial goals are:

1. Establish a Primary and Secondary Cash Reserve level.
2. Implement an automatic savings program to fund these accounts.
3. Establish the time frame and amounts of your next most important financial goals.

The sooner you concentrate on all of these objectives, the sooner you'll achieve them. In developing your plan, remember to be realistic about what you can accomplish within your particular time frame, and be reasonable about your earnings expectations.

III. Financial Management--PGY-2 and After

A. Insurance

By Carol Gray
Physician's Financial Network, Waltham, Massachusetts

You can ensure your financial future by giving attention to the insurance portion of your financial foundation. The first thing to understand is that there are many types of insurance, including health, life, disability, liability, auto, and property coverage.

The road to financial security has many potholes that can slow your progress significantly. The surest way to wipe out years of hard-earned accumulation of money is to suffer an uninsured loss. Doctors usually have abundant professional liability insurance, but often have shortcomings in other areas, particularly life and long-term disability insurance. Deficiencies in these areas can prove to be disastrous.

Life Insurance

Although the primary goal of life insurance is to provide adequate resources for dependents, it can also provide for other postmortem financial needs, including paying estate taxes and assuring that a practice will continue to operate or can be sold in an orderly fashion.

Life insurance offers several additional benefits:

- Cash accumulates tax deferred and can be borrowed on a tax-free basis
- Death benefit passes tax free to beneficiary
- Death benefit is included in deceased's estate.
- There are several types of life insurance, including:

Term: Term insurance provides death protection, but does not build up a cash value. If the person insured does not pay the premium, the policy will lapse after a specified grace period. Premiums usually increase with the age of the covered individual, although there are also level-premium plans, which have premiums that stay the same for 5, 10, 15, 20 and even 30 years. Should be considered as "temporary" coverage.

Whole Life: Provides a death benefit, plus a cash buildup. Also, level premiums guaranteed over lifetime of insured, and the policy has a guaranteed cash value.

Universal Life: Provides a death benefit, cash buildup, and flexible premiums. The cash-value portion of the policy is deposited into an interest-bearing account. Designed for considerable flexibility, with regard to premiums as well as amount of coverage (can be increased or decreased).

Variable Universal Life: Provides for many of the same features as the universal life product, except that the cash value is invested in stocks, bonds, or market mutual funds. There is also a fixed or guaranteed account.

How do you determine how much life insurance you need? Here's one rule of thumb: you need $100,000 of death benefit for every $500/month of income required. For example, if your family needs $5,000/month to survive:

Projected income needed: $5,000/month

$5,000 divided by $500=10

10 x $100,000=$1,000,000 death benefit

Group Term Insurance: Group term insurance is usually obtainable as an employee benefit; the employer pays for coverage that can range from one to three times the annual salary. Additional insurance can be purchased; however, this is usually not recommended, because less expensive term coverage is available through other sources. Coverage may be portable, but if you leave your place of employment, the policy must be converted to a more costly cash-value-type policy. This alternative is definitely not advisable unless you are uninsurable.

Disability Insurance

One of our most important assets is our ability to earn an income, yet this is often the one asset we neglect to insure. Here are some common questions, with answers, about this type of coverage.

1. What is disability insurance and how much can you buy?

Disability insurance pays you a monthly benefit, based on the amount you purchase, if you become disabled, either totally or partially, due to an illness or accident from any cause, except a self-inflicted wound.

You can purchase up to 50 percent of your income’s worth as a base benefit, and this benefit is received tax free provided you pay the premiums. However, medical students, interns, residents and fellows can obtain a larger initial base benefit than they would qualify for based on their income (i.e., $2,500/month for students and interns, $3,500/month for residents and fellows).

2. What features/benefits should you look for?

Obtaining the right disability income policy has always been a bewildering task. Lately, it's become even more complicated, because many insurance companies no longer offer this important coverage, and there have been changes, since 1995, with regards to coverage features and benefits. Although the marketplace is changing, the following benefits are still available with a few top-rated insurance companies:

Own occupation: With this language, you are considered disabled if you cannot perform the main duties of your regular occupation or specialty, even if you are working at another occupation or specialty. A more restrictive definition is "any occupation," which pays only if you are unable to work in any job for which you are reasonably suited.

Non-cancelable: With this feature, the insurer can never change, alter, amend or cancel the policy as long as you pay the premiums. Additionally, premiums do not increase as you age.

Lifetime benefits: With ever-increasing life expectancy, it is important to have a policy that pays a benefit for a lifetime, rather than stopping when the insured reaches age 65. Consider: if you were to become disabled at age 35, and live to reach the normal limit of life expectancy, age 80, and your benefit ended at age 65, you would lose 15 years of benefits. Assuming a benefit of $5,000 per month ($60,000 per year), this feature of a policy could amount to more than $750,000 in lost benefits.

Future insurability: To make certain that your base benefit keeps pace with your increasing income, this feature enables you to increase your coverage without having to prove insurability, subject only to financial underwriting.

Cost of living: Protects against inflation, once you are disabled and collecting a benefit.

Residual and recovery benefits: Pays a proportional benefit, if an illness or injury prevents you from working full-time. Be sure that the policy does not require you to be totally disabled first, and that it bases the loss on income, not time. The recovery benefit pays you once you are back at work, and no longer disabled—provided you have had some loss of income loss (until you build your practice back up, for example).

3. What if I have coverage through my employer or through an association?

Even though you may have a plan through work, it is still important to buy individual coverage. This is a much stronger policy and also protects you wherever you work. (A plan obtained through employment may not be portable and, even if it is, you will have to convert to whatever the insurance company decides to give you.) In addition, benefits received from a group plan will be taxed in accordance with how much of the premium the employer pays (if, say, the employer pays 75 percent of the premium, 75 percent of the benefit is taxed). Supplement your group plan with an individual plan, because there are no guarantees about what features/benefits the plan will contain from one year to another.

Plans obtained through a group are not non-cancelable, which means they can be changed, amended, canceled or premiums increased at any time. An individual plan protects against loss of coverage. An individual disability plan will always offer more protection than a group plan.

In summary, disability income coverage is the cornerstone of any financial plan. Without disability coverage, everything you own is held hostage to your ability to earn a living. Purchase as much coverage as you can now, fit it into your budget as you do any other necessity, and get on with your life.

Property Insurance

Most people have insurance on their home(s) and automobile(s). Surprisingly, less than 25 percent have renter’s insurance, although every renter should. Take an inventory of your household possessions. The more valuable a given asset is, the more detailed the information you should keep for insurance records.

Auto Insurance

You may be paying more for your auto insurance than you need to. Look for association discounts and higher deductibles, and drop any expensive policy options that may be keeping your premiums too high.

Umbrella Insurance

Also called extended personal liability coverage, umbrella insurance is often one of the most overlooked gaps in insurance coverage. Given the ever-higher awards granted to plaintiffs in tort cases, injured parties have become more and more willing to sue. If your assets are insufficient to pay the claim, future earnings can be attached to satisfy this debt. Umbrella insurance pays after your homeowners or automobile insurance and can be obtained in increments of $1,000,000, for a low cost.

III. Financial Management--PGY-2 and After

B. Planning for Retirement

By Michael Goodman
Tulane University School of Medicine

Start Planning Now

When it comes to establishing your future financial security, an old adage bears repeating: "In preparing for retirement, no one plans to fail; they unfortunately just fail to plan." Don't fail to plan. It is never too early to start planning and saving for your retirement. The earlier you start, the easier it will be.

Previous generations thought of Social Security as their retirement nest egg. But today, people have to consider their personal savings as providing the core of their retirement income. Social Security is now simply a supplement. You'd do best to think of any government benefits as a bonus to your retirement plan, not as a substitute. Despite the increased popularity of company retirement plans or individual retirement accounts (IRAs), getting started is still the biggest hurdle for most individuals. Far and away, the biggest mistake is not taking retirement planning seriously enough. Inaction runs a close second. People know they need to do something; they just keep putting it off.

Many medical residents will unfortunately procrastinate by offering one of the following reasons to justify not starting their retirement savings:

- "I need every penny just to survive."
- "Retirement? That's years away. I'll think about it later."
- "I know I need to be doing something. And I will, one of these days...."

Don't postpone your retirement savings program. The wait can be costly. Notice what happens when saving for retirement is postponed in this example:

- If, for example, you were to start saving $165 a month at **age 25**, by the time you were 65 you would have actually contributed $79,200, but the account could be worth $579,856.
- If you begin saving $165 a month at **age 35**, you would have contributed $59,400 but the account could be worth $247,549.
- The same amount saved beginning at **age 45** would mean that $39,600 in actual contributions could be worth $97,836.
- If you begin saving $165 a month at **age 55**, 10 years later the account could be worth $30,387.

(All of the examples cited assume monthly contributions to a tax-deferred retirement investment and an 8 percent rate of return compounded monthly. Your actual results, in terms of dollars accumulated, may be better or worse than in these examples, and income taxes would be due when you begin to withdraw from your retirement plan.)

So it's always worthwhile to save, but the advantages of starting early are considerable. The earlier you start to save, the longer your money has to grow and reap the benefits of compounding.

Saving for retirement can seem difficult. By the time you meet all your monthly expenses, you have nothing left to save. The key is to pay yourself first before you pay the other bills. Put some money away each month specifically for retirement, and make a pact with yourself not to touch it until then. This way you aren't tempted to spend it.

Anticipate the Future

You don't need to gaze into a crystal ball in an attempt to predict the future, but you should take time to think ahead about your retirement. Most financial advisers suggest that you begin at the end. Try to identify what you want to do during your retirement and how you envision your retirement lifestyle. With your advisor's assistance, assign an approximate dollar value to that lifestyle. A general rule of thumb cites that in retirement you'll need 60 to 80 percent of your pre-retirement income. Those who are more affluent tend to need a higher percentage. Contrary to rules of thumb, many financial planners are realizing that people don't spend less money when they retire. In fact, thanks to travel and entertainment, they sometimes spend more. So carefully review your expected expenses, and plan to update your projection at least every five years. Numerous financial companies offer interactive online retirement calculators to help you estimate your future income needs, so take advantage of your available resources.

Write Down Your Goals

Write down your retirement goals on paper. Goals become much more concrete—more real—if they're formalized in this way. Without a written reminder, it becomes much harder to pay attention to goals. At least in the beginning, it's a good idea to put down everything you think you might want, no matter how farfetched it might seem. Acknowledging all your goals lets you assign each one its proper priority, in relation to all the other wants and needs in your life. You can then develop a game plan for pursuing it, or be honest with yourself about the fact that other things are more important.

Calculate Your Retirement Savings

Factor your current income, investments, and rate of savings to learn how much of your retirement dream you will be able to afford. This initial approach is admittedly the most sobering, and least fun, step in retirement planning. At this point, you will likely discover that your future dreams and current means may be, shall we say, more than a little bit out of synch. The question is, must you adjust your dreams to your means, or can you manage those means to realize your dreams? At minimum, the resources available to you upon retirement should be sufficient to provide adequate retirement income. Other important long-term goals, such as meeting educational and other dependents' needs, must also be considered.

Consider Your Life Expectancy

As the average life expectancy continues to increase, adding to the number of years spent in retirement, young investors will need to take special care to make sure they don't outlive their savings. If you retire at age 65 and live to be 90, you'll need enough money for 25 years of retirement. Inflation can also be a concern; the dollar amount you can live on at 65 will buy much less when you're 85. Thus, consider the impacts of inflation in determining the amount of retirement assets you'll need to accumulate. The inflation trend from 1927 to 1998 indicates that the average inflation rate has been 3 percent. Also, consider that if you plan to retire early, as many people hope to do today, you'll need even more assets, because (1) your monthly benefit from Social Security will be lower; (2) you'll have less time to save for retirement; and (3) your retirement savings won't have as much time to grow.

How to Maximize Your Retirement Savings

Retirement planning focuses on what can be done today to realize long-term financial goals. It's not a one-time act, but many related ones: budgeting, saving, investing, income tax planning, dependent needs planning, and estate planning. These endeavors revolve around one main consideration — the very essence of retirement planning — namely, taking action to accelerate the growth of wealth. What can you do to realize your retirement dreams? What can you do to increase the growth of your retirement savings?

The most obvious way to increase your savings is to increase your income. Planning constraints can often be eased by an increase in salary (whether this is achieved by negotiating a raise, assuming additional responsibilities--such as moonlighting--or finishing residency and starting one's medical practice). Employment or self-employment income earned by other family members can also make a significant contribution to retirement savings.

Adhering to a well-conceived and disciplined budget allows you to better anticipate how much money you'll have for retirement purposes, and how you can allocate it. Budgeting also enables you to control interest (debt) expenses. You can increase your income by repaying any credit card debts. You should also make a firm commitment to "forced savings." Take maximum advantage of any qualified pension plan offered by your employer.

One more suggestion: Take a good a look at your taxes. Tax planning lets you reduce tax liabilities — a worthy goal in itself — and also enhances your investment options.

In the end, there are but two (legal) ways to increase wealth — you can work for it and you can put it to work for you. You can earn, and you can invest. These two ways to increase wealth are not alternatives but complements. Indeed, the better job you do making money — maximizing income and controlling expenses — the greater are your options in making that money make more money for you.

Re-evaluate Your Goals Periodically

Recognize that your goals may change over time. A goal set when you're 25 may not be right by the time you're 40. It's a good idea to sit down periodically and have a conversation with yourself about whether you're really where you want to be and if not, where you'd prefer to be headed. Financial planners recommend doing this at least once a year, to see if you're still on track. Your financial situation will change and so will your financial concerns (such as debt obligations, children's college tuition, job stability, or aging parents), which will impact your financial goal priorities and affect your investment decisions.

Summary

In thinking about how to save for retirement, there are some basic principles to keep in mind:

- The best advice is to start retirement planning and saving early. Even a small individual retirement account begun in the mid-20s can make a phenomenal difference when a person reaches retirement age.
- The sooner you start saving for retirement, the easier and cheaper it is to build up a nest egg. Small amounts of money can grow dramatically over long periods of time, especially through the compounding of interest and reinvestment of dividends.
- A general rule of thumb is that individuals need a minimum of 60 percent to 80 percent of their pre-retirement annual income to maintain their lifestyle in retirement. The combination of pension and Social Security income typically falls short of this goal.
- Review your retirement goals, needs, expectations, and savings programs on a regular basis. Make adjustments as necessary.

III. Financial Management--PGY-2 and After

C. Vehicles for Retirement Saving

By Michael Goodman
Tulane University School of Medicine

Retirement Sources

In general, your retirement funds will come from four sources:

- Social Security
- Pension plans
- Tax-deferred savings
- Basic savings and investments.

Social Security

You don't have a choice about participating in this retirement program. You (and your employer) contribute to the Social Security program each year. While you'll most likely contribute a sizeable amount to Social Security during your career, don't count on getting too much help from the government in your retirement. At best, Social Security will contribute only a part of the monthly income you'll need.

Pension Plans

The type of pension plan you may participate in can vary, and often depends on type of employment. Self-employed physicians, or those that are partners in a medical practice, might establish a different type of pension plan than a physician employed by a hospital or clinic. Basically, pension plans (also known as "qualified retirement plans") generally fit into two categories: defined benefit plans and defined contribution plans. All of these plans are available to corporations, partnerships, and sole proprietors.

Defined Benefit Plan: An employer who establishes a defined benefit plan agrees to contribute sufficient funds to pay out a retirement benefit amount that is specified in the plan, in advance. Usually the amount specified is a certain percentage of the employee's average salary during the five years prior to retirement.

Defined Contribution Plan: An employer who establishes a defined contribution plan contributes an annual amount that may be determined using a specified formula. This formula may be a set percentage of each employee's salary, an amount determined by a factor of age and salary, or other criteria. Your employer may make contributions on your behalf, and/or you may also contribute a percentage of your salary to the plan. One common feature of all defined contribution pension plans is their flexibility in letting you choose how to allocate the funds.

There are a variety of defined contribution plans available. Your employer may offer one or a combination of the following common types of plans:

- Profit Sharing Plans
- Thrift (and savings) plans
- Employee stock ownership plans
- 401(k) plans
- 403(b) plans
- Simplified employee pension plans (SEPs)
- Money purchase pension plans.

With some of these plans, you can opt to have retirement savings deducted directly from your paycheck. This means you are able to invest pretax dollars, which are then deposited into a retirement fund where they accrue on a tax-deferred basis. A special benefit of these plans: some employers will match part or all of your contribution. That's free money. Take advantage of it. The downside is that you can't touch this money until you reach age 59 ½, or you will pay the IRS a heavy penalty.

Tax-Deferred Savings: You've decided to put money away, and not touch it until retirement. A great savings vehicle to consider is one that offers tax-deferred savings. In a taxable account, you pay federal tax on the interest your money earns before retirement. In a tax-deferred account, the government doesn't collect taxes until you retire, which means that more of your money can accumulate at a compound rate. Pension plans usually offer tax-deferred accumulation of retirement assets, but there are several other tax-deferred options you can consider in addition to a pension plan.

Individual Retirement Accounts (IRAs): Ask your financial advisor for the latest information on the IRAs that may be available to you. IRAs have different features and benefits, as well as restrictions on who can contribute. However, everyone who has earned income can contribute to at least one type of IRA, and IRAs of any type have a major advantage: tax-deferred growth of contributions and earnings. The tax-deferred compounding feature is one smart reason to establish an IRA and to add to the account consistently every year.

Retirement Annuities: An annuity is a contract between an individual and an insurance company and can be used for accumulating assets for retirement or as a method of providing an income stream at some future date. The contract owner makes lump sum or periodic contributions to an annuity. At some future date, the annuity pays out regular income (payable yearly or at other regular intervals). Federal income tax law limits how much you and your employer can contribute to your Retirement Annuity or Group Retirement Annuity each year.

The two common types of annuities are: (1) the variable annuity—the value fluctuates, because it depends on the performance of the underlying investment options managed in the separate account; and (2) the fixed annuity—which guarantees preservation of the principal, plus a fixed rate of return. Each type of annuity has its particular benefits and risks.

The variable annuity lets you increase your return by using a mixed portfolio of underlying investments—typically, stocks, bonds and money market funds. In this set-up, the inflation risk is minimal. However, the eventual distributions in retirement from a variable annuity could vary substantially, since the value of the annuity units you have purchased fluctuates according to the value of the underlying portfolio.

Since the fixed annuity offers a guaranteed rate of return by the issuing insurance company, it is generally considered conservative and stable. As a trade-off for this stability, the investor risks a loss of purchasing power due to inflation.

Cash-Value Life Insurance: Purchasing cash-value life insurance is another not-to-be-overlooked method of accumulating tax-deferred savings.

Basic Savings and Investment Vehicles

Stocks: Companies issue stock to investors to raise business capital. Shares of stock represent ownership in a company. How much investors own depends on how many shares they have purchased, in relation to the total number of shares that have been issued. Generally, investors may purchase two types of stock: **common stock** or **preferred stock**. Owners of common stock get to vote on key issues affecting the company, for example, selecting its board of directors. Common stock shareholders are the last group to be receive a share profits of the company's profits. However, if the company does well, they are likely to profit most from its growth. Preferred stock owners are entitled to be paid any dividend or compensation before the owners of common stock. However, they cannot vote on most issues, and the dividend they are paid is a fixed amount.

The major benefit from investing in stocks the potential gain from ultimately selling your shares for more than their purchase price. (The historical average annual return for the U.S. stock market since 1926 has been approximately 10 percent a year, higher than that of most other types of investments.) Investors also benefit by taking advantage of the growth of a company, profiting from overall economic growth of the economy, and sharing in a company's profits by receiving dividends.

But remember that what does go up, can also come crashing down—that is the inherent risk in stock investments. The value of stock can fall when the specific company does not do well, or if the overall stock market falls (even if the specific company is doing well).

Bonds: Bonds are commonly referred to as "debt securities"; that is, they represent a loan by an investor to the issuer. The issuer promises to repay the money it has borrowed, plus interest (generally set by the issuer at the time the bond is issued), at a specified date in the future (the "maturity date"). Corporations, governments or municipalities may issue bonds to raise money. A bond certificate details the amount of the loan (principal), the rate of interest to be paid on the loan, and the maturity date.

Generally, investors may purchase two types of bonds: corporate bonds and government bonds. Corporate bonds have the full backing of the company that issues the bond. Government bonds are backed by the government agency that issues them. Government bonds typically tend to pay lower interest rates than corporate bonds, because they're usually considered safer.

The attractiveness of bonds is that they provide a regular source of income. The interest rates are usually higher than those of short-term investments. Investing in municipal bonds can often save you money in taxes, since the interest paid on them is usually considered non-taxable (tax-free) on your federal income tax return. The income provided can help give an investment portfolio some stability, to balance the ups and downs of stock investments.

Bond investments have their own attendant risks, however. For example, the value of an original investment can drop if interest rates rise (thus making older bonds, which pay lower rates, of lesser value). In some cases, an investment can be lost because the "borrower" (a company or government) doesn't repay the loan.

Mutual funds: If you invest your money in a single stock or bond, your return depends heavily on how that one company performs. One way to invest in the stocks or bonds of many different companies is with mutual funds. When you buy shares of a mutual fund, each share buys a small part of anywhere from dozens to hundreds of different securities; any problems with one of them should have very little effect on your return. Funds offer professional management of your invested dollars, as well as diversification. Many investors seek out mutual funds as vehicles for retirement savings as a means of trying to balance their portfolio and attempt to balance and/or control stock and bond risks.

Bank Deposits and Accounts: Banks offer several kinds of retirement investment vehicles, such as certificates of deposit, savings accounts, and money market accounts. Usually, investment opportunities offered by banks are at a fixed rate of interest for a fixed period of time.

Investment Options and Strategies

Asset Allocation: One of the first questions you will most likely ask when planning for your retirement (or any other financial goal) is: "Where should I put my money?" The answer isn't necessarily as difficult as it might seem. Asset allocation is the process of investing in different asset classes, to achieve a return with an acceptable level of risk. The decision about which asset classes you will to invest in will determine about 90 percent of your success as an investor. The more risk you accept, the more likely you are to earn a higher return in the long run. When setting your income goals, don't forget that your retirement savings will have to last a long time, especially if you retire before age 65. That's why many financial planners will recommend that investors concentrate their portfolios in growth investments like equities, even as they near retirement age.

Although every investor is unique, there are some general rules of thumb when it comes to retirement investing. For example, a typical allocation for investors in their 20s and 30s would be as much as 70 to 80 percent in stocks. A 40-something's portfolio would include 60 percent stocks, and a 50-year-old would still want to have half his investments in stocks. Many advisors recommend blue-chip stocks or stock mutual funds to their clients; market-matching index funds are another option for investors who have neither the time nor the expertise to choose securities on their own.

The Role of Inflation: When planning your investment strategy to build your retirement savings, it is important to recognize the risk associated with the stock market as well as the often forgotten risk brought on by inflation.

To understand the impact of inflation, let's say (hypothetically) that you have $100 in something that's absolutely safe; you're guaranteed you won't lose any of the money you put in. Let's also say that inflation is about 4 percent a year (that's the historical average in the Consumer Price Index, which the federal government uses to measure inflation). If your

$100 loses 4 percent of its value every year to inflation, after 10 years, it's going to be worth only $66. That's why inflation can be so dangerous over the long run. You've lost about $33 worth of what you've saved—even though you still have the same number of dollars.

If you're talking about money you're going to need soon, losing money to inflation isn't much of a problem. But over time, it can add up. If your money isn't earning enough to stay ahead of inflation, you're automatically running the risk of losing some buying power.

Countering Inflation with Aggressive Investments and Time: If you're concerned about having enough money for retirement, you may want to consider including some aggressive investments, such as stock funds, to try and outpace inflation. Conventional wisdom indicates that people who don't need their savings for many years should have a high percentage of their retirement money in aggressive investments. The longer you invest, the more time you have to ride out the fluctuations in the market. Even if you're nearing retirement, having a portion of your portfolio in these investment options may be a good idea. Your life expectancy at retirement will, most likely, provide you with plenty of time to ride out market fluctuations. Also, you'll still want protection from the erosion that inflation will inflict on your nest egg during those retirement years. So you may want to consider putting part of your savings in more aggressive investment options.

Remember, stock prices can go up or down, and there's always uncertainty about what will happen to your investments. But over time, the long-term direction for stocks has historically been up, despite the peaks and valleys along the way. Investing for the long term means that your money has more time and opportunity to benefit from that growth potential.

Advisors recommend taking advantage of as many investing opportunities as you can, whether that's a company-sponsored program or an IRA. Diversifying your portfolio helps to reduce the risks associated with the various classes of investments.

Final Thoughts

The time to start saving for retirement is now. You Social Security and pension checks won't be enough, by themselves. In addition, inflation, early retirement, and an increased life span will mean that even more retirement savings will be required. The sooner you start saving, the more compounding and tax-deferred growth can work in your favor. In fact, the specific investments chosen actually matter less than the simple act of starting to save. The more time your money has to compound, the bigger your nest egg. Planning ahead can make all the difference in achieving your retirement goals.

Ultimately, you alone are responsible for your investments and having adequate funds for your retirement. You can certainly seek out advice and input from professionals, but realize that there are no "one size fits all" solutions and that all final investment decisions are yours.

You **can** save for retirement. Set your goals, understand your investments, and take action now.

III. Financial Management--PGY-2 and After

D. Estate Planning

By Amir Viskin, CFP
PIAM Financial Services, Waltham, Massachusetts

Residents and young physicians face unique challenges as they begin planning for financial independence. For most people, the main concern at this early stage is debt management. However, because of the relatively long time horizon involved and your young age, you should try and devise a savings and investment strategy that maximizes the effectiveness of your limited resources.

Many people assume that estate planning is "only for the wealthy." It is true that some of the more popular estate planning strategies are designed to maximize estate taxes and ensure the efficient transfer of wealth. However, it is important to realize that the goal of protecting your loved ones is always relevant. Some understanding of the basics of estate planning may be particularly important at this early stage if you have significant liabilities and insufficient liquid assets.

The purpose of estate planning is simply to ensure that your estate reaches your heirs the way you want it to, quickly and efficiently, while incurring minimal federal and state taxes. To develop a plan to meet your needs, you should understand how your death will affect your property, and what it will mean to your survivors. You need to become familiar with the documents and concepts described below.

Wills: A will is the most basic document in estate planning. They direct your assets to those who should be receiving them, and they establish guardians for your children. If you die without a will, you give your state government the right to distribute your assets and decide who will raise your children. You may also be subjecting your family to a long, expensive wait in probate court.

Probate: Probate is simply a process whereby the courts oversee that the instructions in your will are carried out. The probate estate is made up principally of assets titled in the deceased's name alone. It does not involve assets that pass to a beneficiary by contract, such as life insurance proceeds or retirement assets, or assets that pass to a surviving joint tenant by right of survivorship, such as a residence or an account that is owned in joint names. Thus, in theory, probate serves an important need to facilitate the transfer of assets at death. Unfortunately, in practice it can result in additional cost and delay in the administration of the estate and in lack of privacy due to the fact that probate records are open to public scrutiny. Therefore, it is important to discuss with your advisors whether planning techniques should be used to avoid probate where appropriate.

Revocable Trusts: A revocable, or living, trust, created during your lifetime, is commonly used to avoid probate. You retain control over the trust assets by retaining the right to revoke or amend the trust, and by acting as trustee. Your assets will circumvent probate at your death, to the extent that they have been placed in the trust during your lifetime. Upon your death, the provisions of the trust, not your will, direct how the trust assets will pass to your heirs. This is why this trust is sometimes referred to as a "will substitute."

Your will document works in concert with the trust, by directing that all of the assets that remain titled in your name move into the trust upon your death. It is important to understand that this trust is not established for estate tax reasons. Rather, it is used to avoid probate as well as provide management assistance when needed, such as in the event that you should become incapacitated.

Sheltering Your Estate from Taxes. The marital deduction lets you leave all your property to your spouse estate tax free; however, estate taxes will become due at your spouse's death. The Federal Gift and Estate Tax Unified Credit for 1998 allows you to pass approximately $625,000 of your assets to your heirs free of federal gift tax during your lifetime and free of estate taxes at your death. Under the Taxpayer Relief Act of 1997, the unified credit equivalent is scheduled to gradually increase over the next years up to $1,000,000 in 2006 and thereafter. Proper titling of your assets and use of the unified credit could allow you to avoid estate tax liability during the early years of your career.

Professional Advisors: It is important that the work of your professional advisors is coordinated in a way that helps to ensure the achievement of your objectives. The following advisors should be consulted:

- Attorneys--coordinate and draft wills, trusts, power of attorney, and other documents, as well as advise you on how to title real estate and other assets.
- Financial Service Professionals—assist you on the purchase and ownership of investment and life insurance products.
- Retirement Plan Administrators—assist you on the beneficiary designations for qualified retirement plans.
- Accounts or Tax Advisors—provide tax advice.
- Trust Officers--provide investment management services.

IV. Career Planning and Preparation for Practice

A. Physician Compensation

By Laurel Weinstein
Medical Group Management Association, Englewood, Colorado

The Different Ways Physicians Are Compensated

Physician compensation plans differ from one group to another. It is important to understand what the compensation plan is and how you will be affected, both in your first few years with an organization and in the later years of your employment. There are five compensation methods that the Medical Group Management Association (MGMA) tracks in its annual publication, **Physician Compensation and Production Survey.**

1. **100 percent Productivity:** The entire compensation is based on some productivity measure. This could be a single productivity measure, a combination of productivity measures, or some sort of step productivity measure that is different at different levels.
2. **50 percent to 99 percent Productivity:** The majority of the compensation is based on some productivity measure and the remainder is guaranteed.
3. **50 percent to 99 percent Guaranteed Salary:** The majority of the compensation is guaranteed and decided on with some variability due to productivity or a bonus.
4. **100 percent Straight or Guaranteed Salary:** The compensation is completely guaranteed.
5. **100 percent Equal Shares:** At the end of the year all revenue that is left after expenses is divided and paid as compensation.

The portion of the compensation that is variable, based on productivity, could be linked to any one of several productivity measures. Some examples are:

- Gross charges
- Adjusted charges (gross charges minus contractual discounts/allowances)
- Medical revenue/receipts
- Number of patient encounters
- Number of procedures
- Number of Resource-Based Relative Value Scale (RBRVS) Units or Physician Work Relative Value Units (RVU's)
- Size of physician's patient panel (normally, for primary care physicians).

Other measures that may affect the compensation of a physician are not necessarily productivity based. Some of these may be used for bonuses or be used in the compensation formula. The following are examples:

- Patient satisfaction
- Peer review

- Administrative or governance responsibility
- Service quality
- Seniority in the medical practice

Trends in Compensation Methodologies

New Physicians: The type of compensation method used with new physicians (1-2 years out of residency) differs from the compensation method used with established physicians. Newer physicians tend to have more of their compensation guaranteed. From the 1998 data that MGMA collected, 35 percent of new physicians compensation was 100 percent guaranteed and 31 percent of new physicians were compensated with a formula that was 50 percent to 99 percent guaranteed. For new physicians, only 20 percent were compensated from a methodology of 100 percent productivity. However, as physicians become more established, it is less probable that they will be guaranteed their annual compensation.

Established Physicians: As physicians become established (after more than 2 years out of residency), the compensation method for them tends to be based more on productivity; relatively less of the compensation is guaranteed. Compensation trends differ for both primary care physicians and specialists, once they are established. Compensation also differs if the established physician works in a single specialty or multi-specialty group. "Single specialty" indicates that a practice focuses its clinical work in one specialty; a "multi-specialty" group is one whose practice consists of physicians practicing in different specialties.

The 1998 data collected by MGMA reveals differing compensation trends among established physicians. For established physicians, in both primary care and specialties, only about 16 percent of the respondents are paid a 100-percent-guaranteed salary. However, 30 percent of the established physicians were fully compensated (100 percent) according to their productivity. Among established physicians, 19 percent of those in primary care and 21 percent of those in specialty fields were compensated according to productivity, in a range of 50 percent to 99 percent.

Certain patterns appear only among specific groups:

- Equal shares was not used by a majority of practices, especially multi-specialty groups. However, 15 percent of non-primary-care single-specialty groups use equal shares as the compensation methodology, compared with about 2 percent for primary care single specialty groups.
- About 50 percent of multi-specialty groups use productivity as the sole criterion for establishing compensation; alternatively, 50 percent to 99 percent of their compensation was linked to productivity.
- Primary-care single-specialty groups have almost 60 percent of respondents compensated by salary plus bonus or straight salary.

As you consider whether you should a particular physician group, it is important that you understand the compensation method of the group. You must work with the group administrator to understand how your productivity will be evaluated in relation to your compensation. The following are questions that will help you do this:

- What are the physicians working for the group producing in order to justify their compensation?

- If physicians join under a guaranteed-salary arrangement, how will that arrangement change as they accumulate more years with the practice?
- As salary formulas change, how are they applied to physician productivity to determine what the compensation will be?

The MGMA annually produces a report called the **Physician Compensation and Production Survey**. This survey of MGMA member practices has been conducted since 1987. The survey will give you valuable information on compensation levels and job market trends in the disciplines that interest you.

Many factors affect compensation. The compensation methodology used by a particular practice group, your number of years of experience in your specialty, and the productivity of the physicians in the group are some of the most important. You should carefully consider these factors, as well as the practice characteristics, when you evaluate a possible compensation plan.

IV. Career Planning and Preparation for Practice

B. Practice Arrangements

By John Boltri, M.D.
Family Practice Center, Macon, Georgia

When residents contemplate the array of practice opportunities available today, they need to consider many factors before making any decisions that impact their personal and professional futures. There are many types of practice arrangements available in all fields of medicine. When choosing a particular practice setting, residents should be aware of the pros and cons of the practice's arrangement as well as alternatives that may be available. For instance, a pathology resident may find that, rather than following the usual route of becoming a hospital employee, physician ownership of a freestanding pathology lab that contracts with several managed care organizations is a better career option, because of its unique rewards and opportunities.

It is common to categorize physician practice opportunities into two categories: (1) employee opportunities, and (2) self-employed opportunities

Employee Opportunity Settings

- Hospitals or other institutions
- Managed Care Organizations (MCOs), which offer full- or part-time employment as a provider of care, or manager, of care
- Government or public health agencies at the Federal, state, county and city level
- Academic institutions that offer teaching, research, and service opportunities
- For-profit and not-for-profit associations that offer regulatory, scientific, educational, and challenging advocacy roles.

Employed physicians enjoy one or more of these benefits:

- You will have a defined and consistent salary and benefits, for a contracted length of service.
- You can focus on clinical opportunities without the hassle of administrative and management considerations.
- Many group practice and partnership arrangements offer quite good compensation packages to attract physicians, and then offer partnership/ownership equity for as an additional incentive for loyal, productive service.
- Many managed care organizations and other institutions offer leading-edge clinical opportunities and growth in such areas as utilization management, total quality management (TQM), disease management, and population health programs
- Many teaching and research institutions offer wide-ranging and often custom-tailored opportunities that let physicians expand their professional limits.
- Medical staff for Federal, state, county, city agencies such as the U.S. armed forces, USPHS, CDC, or state/local departments of health offer very satisfying careers in public service

Self-employed Opportunity Settings

There are three basic options in the self-employed category of practice:

- Solo practice as "Dr. Jones, M.D., P.C."
- Partnership in a group of two or more
- Group practice as primary care physicians (PCPs), specialty care physicians (SCPs), or mixed-care practices

Being self-employed or in a shared ownership arrangement also offers benefits:

- You can make all the decisions about management policies, as your own boss
- You receive the full reward of any financial gain that the practice incurs
- You have a chance to function not only as a physician, but also as a business entrepreneur, developing financial, marketing, management, and human resource skills.

Professional Compensation Issues

In any of the practice arrangements, salary may be paid out according to one of many methods. There are almost as many different salary-reimbursement methods as there are practice types. Because they are unique to every practice, compensation methods should be considered carefully. Salary reimbursement methods include the following:

- Straight salary
- Salary with productivity incentive. The percentage of straight salary and the percentage that serves as an incentive can vary, depending on the arrangements
- Productivity-based salary
- Equal-share salary. After overhead is paid, all of the remaining revenue is split equally among the physicians/partners.

Incentive arrangements also vary from one practice to another. The common types of arrangements are incentives based on:

- Total number of patients cared for
- Billings
- Actual work performed
- Revenues
- Revenues minus overhead
- Quality of care and efficiency of care indicators.

Other Considerations

Once residents/physicians narrow down the type of practice arrangement and compensation arrangement that is most desirable for them, there are a number of other questions to consider:

- What about location, location, location? Would you prefer a large city or a small town? Can your needs and the needs of your family be met in terms of education, social interaction, quality of life, religious affiliations, etc.?

- Is there a demand for your particular specialty in the area? What are the opportunities for your practice to thrive in terms of referrals, association with a PPO, etc.?
- If you are joining a practice or institution, is the "fit" a good one? The practice/institution you join should share your goals, both from the perspective of practicing medicine and from the perspective of business. Are your workload expectations congruous? Is there a real need for another physician of your specialty within the practice/institution?
- Can the practice meet your expectations? Does it have the equipment and technology you require? Is support staff adequate?
- Is the practice financially sound? What are the payor mix, the overhead, and the volume per provider? Do they have a good reputation in the medical and hospital communities and in the local community at large? How have they reacted to changes in health care and do they have any plans for future changes?
- What are the interpersonal dynamics of staff, physicians, administrators, patients, and vendors?
- How is the practice/institution governed? Will you have an equal say in practice operations? If not, how are decisions made and who makes them?
- What professional autonomy is granted in terms of patient care and use of guidelines, benchmarks, etc?
- How are the practice’s claims, payroll, accounts receivable, and accounts payable handled?
- What is the future growth potential for the practice and for you professionally?

Conclusion

The American Medical Association estimates there are nearly 700,000 physicians in the USA. (Not all are regularly seeing patients.) The private practice of medicine is still the bulwark of medical practice and is a style of working that continues to offer exciting opportunities for growth and rewards. But, in today’s turbulent marketplace, there is just as much opportunity and fulfillment to be found as an employed professional. Your challenge is to find the practice opportunity suited to your personality, skills, and goals.

IV. Career Planning and Preparation for Practice

C. Evaluating a Potential Practice Site

By Alan Dever, M.D.
Mercer University School of Medicine

This section presents an outline of what a physician should do to determine the economic feasibility of establishing a medical practice in a small- to medium-size community. It is intended to introduce the process to a new physician. To implement this process, a physician would need further training or professional assistance.

There are two situations that require physicians to have the knowledge and skills to evaluate a potential practice site in such communities:

- If the physician is looking for a location to establish a new practice
- If the physician is attempting to expand or determine opportunities within an existing practice setting.

In both situations, it is critical to examine basic community patterns related to demographics, utilization, health care resources, managed care influences, economic market forces, and behavioral characteristics. All of these factors must be examined within a given geographic or spatial context, based on a potentially defined market or service area for providing health care. The analysis of these factors in a spatial context will eliminate the "guess work" and the costly mistake of establishing a practice in an area where the economic feasibility and/or survival of the practice could be in jeopardy. The following outline gives the methods and steps required to facilitate a physician's decision in identifying a viable site for establishing a practice

1. Define the specifics of the selected specialty

- What type of specialty
- Determine standards for the specific specialty (i.e., the ratio of physician to population)

2. Demographics (population characteristics)

- Identify population trends within a realistic time and space distance for accessing the service (usually 5, 10, 20, or 30 miles from the proposed location) by age, race, gender, income, and educational attainment
- Make comparison of these variables for the proposed geographic distances and also compare to the state

- Perform this evaluation for at least two time periods (e.g., 1990-2000 or 2000-2005) to determine trends in population change. Ask a critical question to the success of a practice: Is the area expanding or contracting?

3. Utilization patterns (who uses the physician services?)

- Identify utilization patterns (patient characteristics) by age, race, gender, income, and education
- Additionally, identify the most frequent diagnosis and disease categories which may be representative of the practice population
- Relate the demographic (population characteristics) to utilization (patient characteristics) for the defined market/service area

4. Inventory of the current health care resources in the area (physician supply and characteristics)

- Identify the current numbers and rate of physicians by specialty and age for the defined market/service area
- Utilize appropriate standards for determining the approximate number of physicians needed in the geographic area

5. Managed Care Influences

- Determine the market penetration rates of the managed care organizations in the proposed service area
- Identify current rates of reimbursement and per member per month contract rates
- Assess the prevailing community issues concerning managed care

6. Economic Market Forces

- Identify the prevailing and future costs for physician visits by determining:
  - Average cost per visit
  - Economic conditions of the area (forecasts)
  - Reimbursement mechanisms of various health plans
  - Correlate economic forecasts with the demographic (population characteristics) and utilization (patient characteristics) trends for the area

7. Behavioral Characteristics

- Discern the attitudes and experiences of the community and other physicians (if present) concerning the potential of a new physician entering the community
- Ascertain the current policy of the hospital administration to obtaining staff privileges
- Be prepared to interview a few community residents, a physician, and the hospital administrator

8. Making a Decision

- Prepare a profile of the community utilizing the above information for determining the potential of the practice site

- Based on this analysis, answer the following questions:
  - Will the population support a new practice?
  - Are utilization trends encouraging?
  - Are demographic patterns supportive?
  - Is physician supply and access to health care an issue?
  - Are economic trends encouraging?
  - What is the attitude of the community and physicians to the prospect of a new physician?
- List the pros and cons for establishing a new practice at the identified site
- Make an informed decision based on the evaluation of this analysis.

IV. Career Planning and Preparation for Practice

D. Physician Employment Contracts

By Carolyn Cotsonas, J.D.
Boston University Medical Center

This outline offers a general discussion of physician employment contracts. It is not intended as legal advice. A resident who is considering an employment contract is urged to seek legal advice from an attorney.

Have a Written Agreement

A contract is a legally enforceable agreement between two or more parties. While it may be possible to successfully enforce an oral agreement, it is nevertheless important to have your employment terms in writing. Even if your employment arrangement is relatively straightforward, it should be written.

Contracts Serve Several Purposes

With written agreements, breakdown situations (like termination or conflict resolution) are more effectively addressed before a problem develops. Written agreements tend to produce greater clarity, cover a wider scope of issues, and define what the relationship is between the parties for tax, regulatory and liability purposes. Getting the agreement on paper in a way that is mutually acceptable to the parties is an important part of the negotiation process and can tell the resident (prospective employee physician) a great deal about his/her future practice associates. Often, the parties never have to consult the written agreement again because everything proceeds well. Nevertheless, the important preparatory work in building a relationship will have been done from the beginning.

Utilize Advisors

It is a good idea for residents to consult an attorney before signing a contract. The fee will vary with the amount of work necessary and the geographic location. The resident is encouraged to discuss with the attorney, at the outset, the basis and estimated charges for service. Typically, it will be less expensive for an attorney to review an offered contract and advise the resident. (It is rare for the prospective employee's attorney to draft the contract.) It is also common for the involved attorneys to stay in the background (reviewing drafts and advising parties), with the physician parties negotiating the terms face-to-face. This helps to keep attorney costs down, and, perhaps, more important, reduces the potential for the negotiation taking on a more adversarial tone.

Contract law is based on individual state laws, and there are some important variations. In addition, regulatory law (both state and Federal), as well as other Federal laws, have an important impact on contracts involving physicians. Many of the apparently straightforward terms in contracts can have multiple important implications for the resident. Finally, these factors must be weighed in the context of a particular resident's goals and needs. For these reasons, utilizing the services of an attorney is a good investment in the future.

Understand the Negotiating Environment

Physician-to-physician negotiation often creates two somewhat divergent dynamics. One is that the parties are attempting to forge a professional, collaborative relationship. The other is that they each want to protect their respective interests. The win-win model of negotiating is most appropriate to this situation. If either party feels that he/she struck a poor bargain, this can damage the future relationship. Preparation is important. Do research ahead of time about specialty-related salary ranges and benefits typical of the geographic area. The resident should carefully think about what things are most important to him/her and what things are more amenable to compromise. The resident should prepare by thinking about what is likely to be important to the other party as well. This reduces surprises.

The negotiation process is an important vehicle for the resident to explore whether his/her expectations are aligned with those of the prospective employer. An important issue will be whether both parties are committed to a long-term relationship in which at some future date the employee physician will gain an equity interest in the practice (i.e., by becoming a partner or a shareholder in a professional corporation, depending on how the practice is organized). There are a variety of contractual approaches to achieving these future arrangements (see below), but the key point here is that the primary goals of the respective parties should be complementary.

The size and complexity of the organization one is negotiating with usually has a significant impact on the negotiation. The resident who is negotiating with the physician employer of a solo or small group is likely to be negotiating with the actual decision-maker. This is not always true in large organizations. If a negotiation seems to be going too slowly, with the employer's representative not able to give answers, the resident might ask to include the person who can make decisions about contract terms in the next meeting. In general, it is harder to get a larger organization to vary the terms of an employment agreement. However, it is not necessarily impossible, and the resident should raise this question about important items. Often, large organizations will reference and incorporate other documents in their contracts (e.g., medical staff bylaws, personnel policies). These referenced documents have contractual force, and, for this reason, the resident should read and understand them.

Recognize that once the parties sign a contract, it becomes the full extent of the agreement. In other words, anything that might have been discussed and agreed to is not legally binding unless it is part of the written agreement.

The Contract Terms

Learn about typical contract terms, and understand their implications. (The following list is a sampling of some of these; it is by no means exhaustive).

Definitions: While the resident will have the assistance of an attorney, the language of the contract itself should be clear and understandable. If it is not, this increases the potential for divergent interpretations. Contracts often include a section that explicitly defines important terms used in the contract. Clarity on the issue of compensation is particularly essential.

Duration: Initial physician employment contracts tend to be from one to three years in duration. If the contract is for more than one year, consider adjusting the terms regarding compensation and termination for the subsequent year(s).

Job Description/Expectations/Coverage: As organizations employing physicians have become larger and more complex, detailed job descriptions have become more common. Productivity expectations are also becoming more explicit. Job descriptions are often included as attachments to the contract.

Compensation: There are a variety of formulae for compensation that include simple, straight salary, various productivity and incentive arrangements, or some combination of these. The resident should recognize that there is a relationship between salary amount and benefit package. The resident's own personal financial situation and goals should guide evaluation of what is offered.

Benefits: Benefits are an essential and often valuable part of the total compensation package. In general, benefits paid by the employer (a tax-deductible expense for the practice) are usually more advantageous for the employee. This is because even if the employee is paid a higher salary in exchange for purchasing his/her own benefits, the purchase will be with after-tax funds. In addition, many benefits are more expensive to purchase on an individual (as compared to group) basis. An example is one of the most essential benefits – health insurance.

Illness/Disability: Paid sick days, as well as disability insurance coverage, are important benefits. The resident should inquire whether the physician employer also has disability coverage, particularly in small private practices. Although obligated to pay the employee physician an agreed-upon salary, a disabled employer who owns the practice will still have a claim on the revenues of the practice. Disability coverage will help reduce financial pressure on the practice.

Other Paid Leave Benefits: These include vacation, paid continuing medical education leave (and usually some expense allowance for CME fees); maternity leave (governed by state and federal law; usually unpaid unless paid vacation and sick leave have been accumulated).

Professional expenses: Travel expenses, publications allowance, professional memberships, and other professional expense allowances may be included.

Other Benefits: retirement plan benefits and life insurance are also important benefits to consider.

Professional Liability: While some think of professional liability as a benefit, others view this coverage as a cost of doing business. Since an employer would be liable for the professional liability of his/her employees, it is in the interest of both employer and employee to have the employee adequately covered.

Future Intent/Buy-in Formulae: Often, an employment arrangement with a private practice is a "courtship" leading to the employee becoming a part owner of the practice.

Future intent is addressed in a wide range of ways in initial employment contracts – from silence on the issue (i.e., it is not mentioned at all) to an explicit buy-in timetable and financial arrangement. Advice of an attorney and accountant is especially important with regard to buy-in terms.

Termination: There are different approaches to termination. Some contracts permit either party to terminate merely by giving adequate notice (e.g., 60 or 90 days' written notice). This can be advantageous, although the resident should resist this type of arrangement if it is extended to the employer but not the employee. Another approach is termination for cause (e.g., loss of license to practice medicine). Some contracts combine both approaches (e.g., notification in year one, and solely for cause in year two). Termination clauses should address disposition of affected items such as any outstanding salary, incentive payment, and medical records.

Covenants Not to Compete: Also called "restrictive covenants," these restrict the employed physician from establishing a nearby competing practice in the event the physician leaves the employer. When included in physician employment contracts, these covenants are typically framed in terms of geographic area and time period. Restrictive covenants have been made void and unenforceable in many, but certainly not all, states. Clearly, such covenants are not in the resident's interest. If the resident is negotiating employment in a state where restrictive covenants are legal, it might be possible to mitigate the impact of the covenant by negotiating less burdensome terms (e.g., reducing the geographic scope of the restriction).

Miscellaneous: Employment contracts might also include stipulations regarding ownership of accounts receivable and medical records; merger or acquisition of the practice and whether the employment contract is assignable; dispute resolution terms.

RECOMMENDED READING

Fisher, R. and Ury, W. **Getting to Yes**; 2nd edition, Penguin Books, 1991.

Specialty societies publish helpful materials on physician employment and other practice management topics. Examples are:

American College of Emergency Physicians. **Contracts: A Practical Guide for the Emergency Physician**, 1990 et seq.

American Academy of Family Physicians**. Practice Management for Family Practice Residents**, 1989 et seq.

IV. Career Planning and Preparation for Practice

E. Operating a Medical Practice

By William Bina, III, M.D.
Mercer University School of Medicine

The variety of practice opportunities available to graduating residents is formidable. How to choose from all those available? After location, the next two categories of importance are practice characteristics and economic considerations. Issues of scope of practice, assessing your associates and their quality of care, observing office efficiency, staffing and facility function are important attributes to consider in your decision-making about whether you can practice the kind of medicine you desire.

The economic considerations are clearly important as well. These are developed further below. In this regard, the principal question for you to answer can be stated briefly as: Is the practice financially sound?

Is the practice busy enough?

How many patient charts per full-time physician equivalent are active? Each specialty will have a nationally accepted average number for comparison. Look at the final office and inpatient censuses and schedules. Look at the full day's workload. How does it compare to the national average for your specialty? How many new patients per month are being scheduled or turned down? This will reflect your new patient base. You want to know if the practice will be able to support adding an additional physician.

What is the payer mix?

Some simple frequency displays arranged by percent of revenue and percent of visits will be enlightening. How closely does the practice reflect the current market? Is the practice dependent on various payers and their fee schedules?

What are the billings?

Review the gross billings per full-time equivalent physician basis. Are they adequate to support a new practice? Use the practice overhead percent as described below to judge your potential salary.

A <u>net collection ratio</u> (net revenue divided by net billings expressed as a percent) should exceed 90 percent generally. This indicates how much of the practice's collectible dollar is actually being collected by the office.

An <u>accounts receivable ratio</u> (total accounts receivable divided by the average monthly collections) should be between 2 and 3. For example, a number 3 indicates that on average, it is taking three months to collect revenue measured from the time of service.

An accounts receivable aging report will show distribution of amounts and percentages by age from date of service. For accounts over 90 days, this number should be less than 15 percent of the total balance.

An insurance payment analysis report could show what each insurer pays by CPT code. Comparison with a normal indemnity fee by code can be used to decide on fee revisions for the future

What is the practice overhead?

What are the costs of running the practice? These include rent, leases, personnel salaries and benefits, administrative supplies and services, outside professional fees (legal, accounting, etc.), medical/surgical supplies, marketing, laboratory and imaging, taxes, etc. Personnel costs are usually the majority of these costs.

How much are these costs, expressed as a percentage of revenue? Each specialty will have national averages for comparison.

What is the number of full-time equivalent support staff per physician? Again, a national average is available. A lower average is not necessarily better as the practice could be either more efficient or under staffed.

What is the practice reputation?

What is its current standing in the community from a quality standpoint? Is the practice actively involved in leadership of group practice discussions in the medical community or is it resisting these efforts? Is this practice planning any new ventures, such as, mergers, satellite operations or practice management contracts? You should know what your role would be in any of these arrangements.