STANFORD BROWN
Financial Advisers

Financial Challenges of Medical Specialists

WHITE PAPER SERIES

The 8 Unique Financial Challenges of a Medical Practitioner

1

You are likely to be much older than your peers before you can commence a dedicated Wealth Plan. Those of your school friends who entered careers such as banking, law or accounting are most likely to have cleared their debts by the age of 40 and are now firmly along the path of creating wealth for themselves and their families. As a medic, your studies and training were longer (not to mention harder!) and more expensive, and your early career earnings lower than your peers. In effect, you are starting the wealth creation process firmly on the back foot.

2

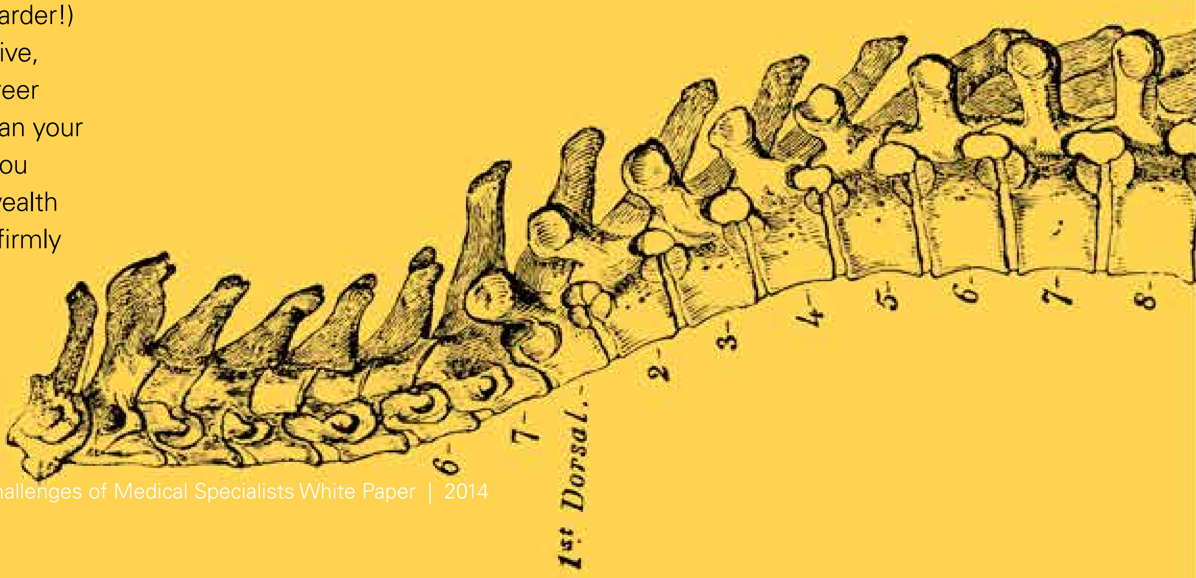
However once into your 30s, your job stability is greater than your peers and your earnings potential is higher. Though you will graduate with a larger HECS debt, this inherent job stability (not quite the extent as in the past but still far more so than your peers) provides you with some unique wealth creation opportunities.

3

The bulk of your wealth is tied up in the net present value (NPV) of your future earnings stream. For a 45 year old medical practice owner earning $750,000 p.a., this equates to an asset value of $10 million. This needs protecting!

4

You are going to become (or are already) a significant payer of income tax. Australia's marginal income tax rates are some of the highest in the world. Once your earnings exceed $180,000, you will be parting company with nearly 50 cents of every dollar earned. It is wise to plan ahead to mitigate this.



A medical practitioner's career is commonly associated with high earnings and an enviable lifestyle. But scratch the surface and you'll uncover complex layers of commercial obligations, personal commitments and business intricacies that are highly vulnerable – all operating in a delicate balance that hinges entirely on one individual. Medical specialists face the same personal and financial stresses as any other profession. But these eight characteristics are unique to the profession.

5

Australia is a highly litigious culture and once in private practice, you will need to ensure your assets and business are protected from the insatiable appetites of lawyers and patients expecting a perfect service. There are a number of critical steps you must take to ensure you are fully protected.

6

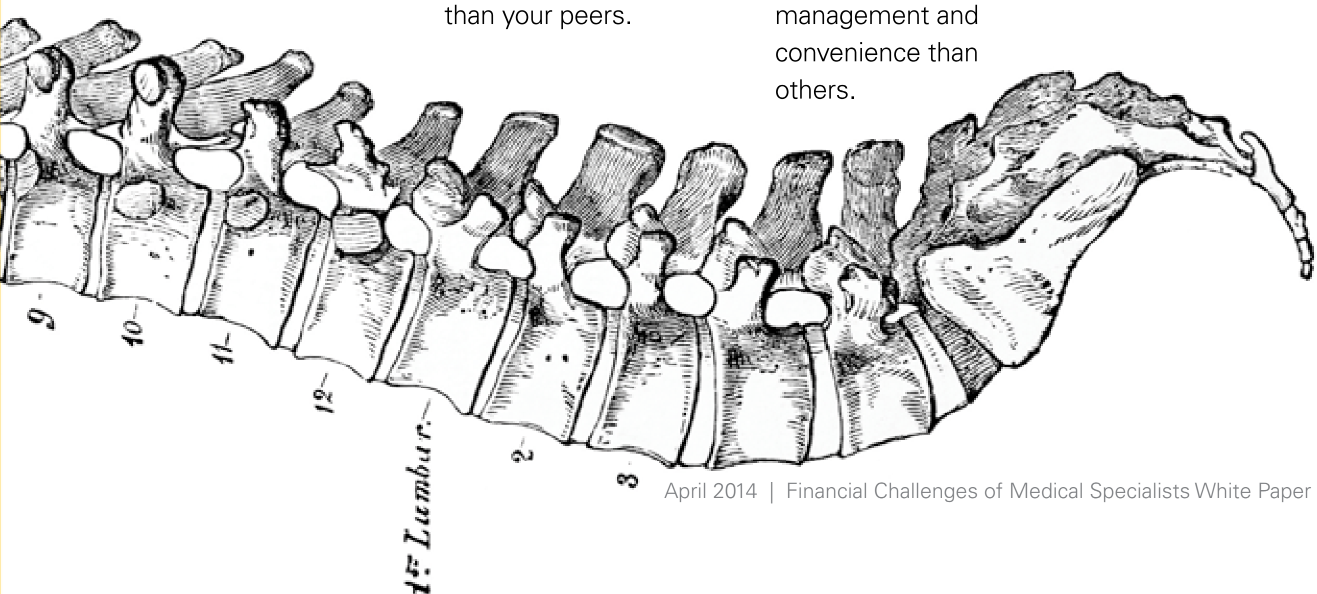
Unlike most small business owners in Australia, you are building up little, if any, goodwill in your practice that can be realised on retirement. In addition, your practice is likely to be based predominantly on referrals, the success or failure of which are inextricably linked to your ability to perform professionally. As a result, your retirement planning must be more proactive and start earlier than your peers.

7

You are likely to be working ridiculous hours. Not to mention combining your job with the demands of a family and a personal life! You have almost no time to breathe let alone shop around for the best financial adviser, the best accountant, the best solicitor, mortgage broker, business coach etc. As a result of these acute time pressures, you are likely to place a much higher premium on efficient time management and convenience than others.

8

You are likely to continue working longer (well into your late 60s) than almost any other profession. Is this because you want to, or you have to? With foresight and thorough planning, the choice can be yours.



Solutions

So tell me something I don't know, you may well be thinking. Well, these are the unique issues facing medical practitioners. The solutions are as follows:

1

Leverage your stable job and reduce your tax bill

Wealth is created by the development of a passive income stream that grows with time to ultimately replace your earned income. From this point onwards, retirement is possible. Leverage (purchasing assets with debt as well as cash) is a common way for individuals to turbo charge the wealth creation process. The Australian Tax Office (ATO) also kindly permits individuals to claim a tax deduction for interest associated with debt taken on for the purpose of generating income. This includes investment property loans and debt assumed to purchase shares. However leverage is not without risk and is not suitable for everyone. It is perfectly suited, though, for those in more secure, well remunerated jobs. Whilst job security is no longer guaranteed for those in the medical profession, it is at least more certain than most other professions.

2

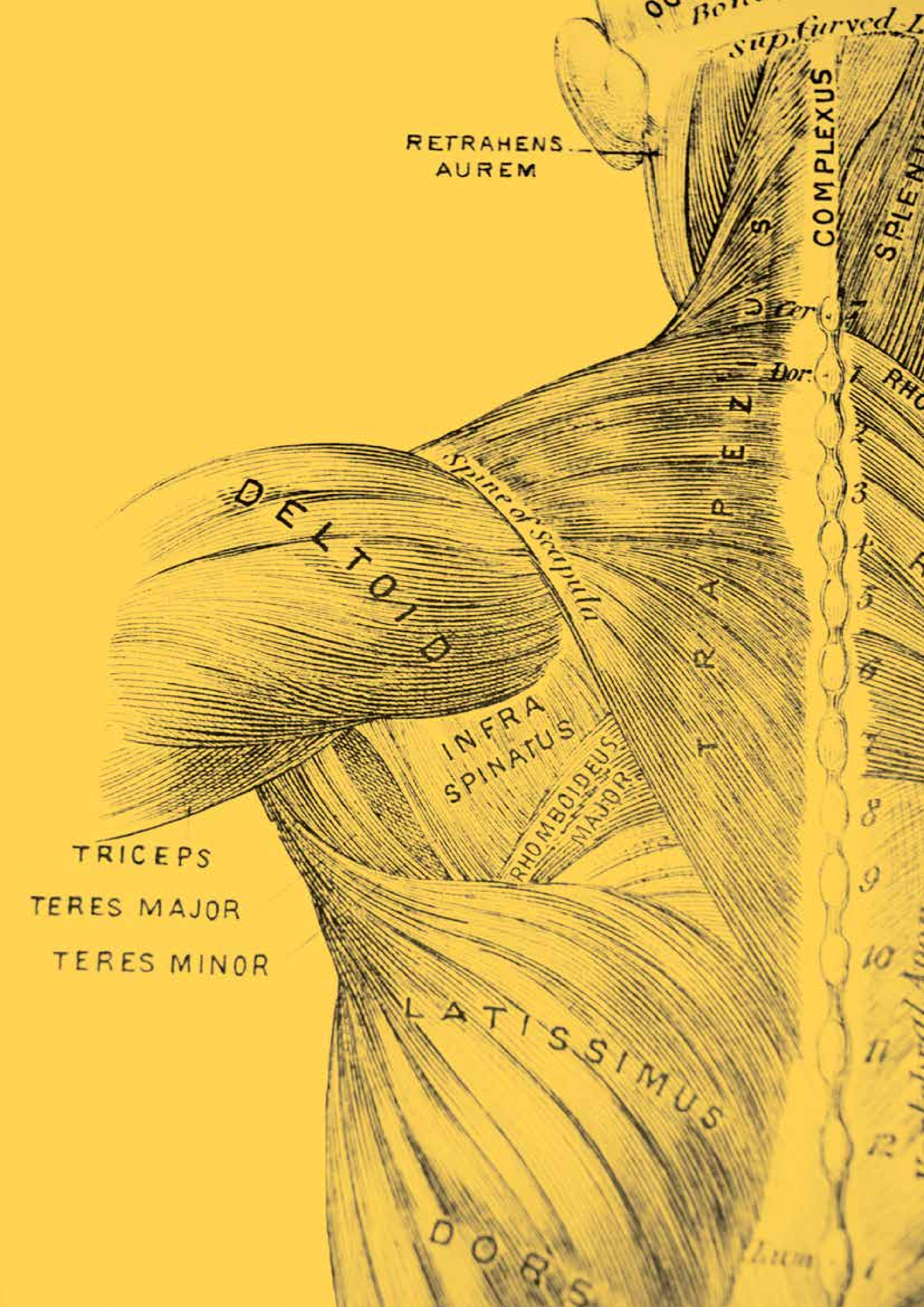
Protect your future earnings stream

Once into your mid-30s, you may be finally starting to earn some real money. As you look ahead, you can (hopefully) see a stable and rising earnings trajectory. However this is likely to be all you have in the world as you have probably only recently repaid your debts. Any event that would prevent you from working would be disastrous. As a doctor there are unique threats from the critical use of your hands to the threat of needleprick injury that other professionals simply don't face. As a result, it is absolutely critical that you insure this earnings stream to the maximum permitted amounts. But income protection insurance policies are not like bottles of milk or litres of fuel – i.e. they are not indistinguishable commodities. It is vital that the insurance policy is appropriate for your situation, that it covers you for all the risks to which you are uniquely exposed and that it is fully up to date. You simply can't and mustn't buy one of these online at a knock down price! There are so many variables to consider that it is essential to seek professional advice for all your personal and business insurance.

3

Structure your business and personal assets correctly

There is an old saying that the key to asset protection is to own nothing and control everything. This is why Trusts – and especially Discretionary Trusts – are so popular for high income, high risk occupations such as running a consulting practice. The most appropriate business and asset structuring is vital to help assist against any future legal action. Professional advice must be sought as this topic is not straightforward and the implications of getting it wrong are immense.



Sup. Curved
COMPLEXUS
RETRAHENS AUREM
DELTOID
Spine of Scapula
TRAPEZIUS
INFRA SPINATUS
RHOMBOIDEUS MAJOR
TRICEPS
TERES MAJOR
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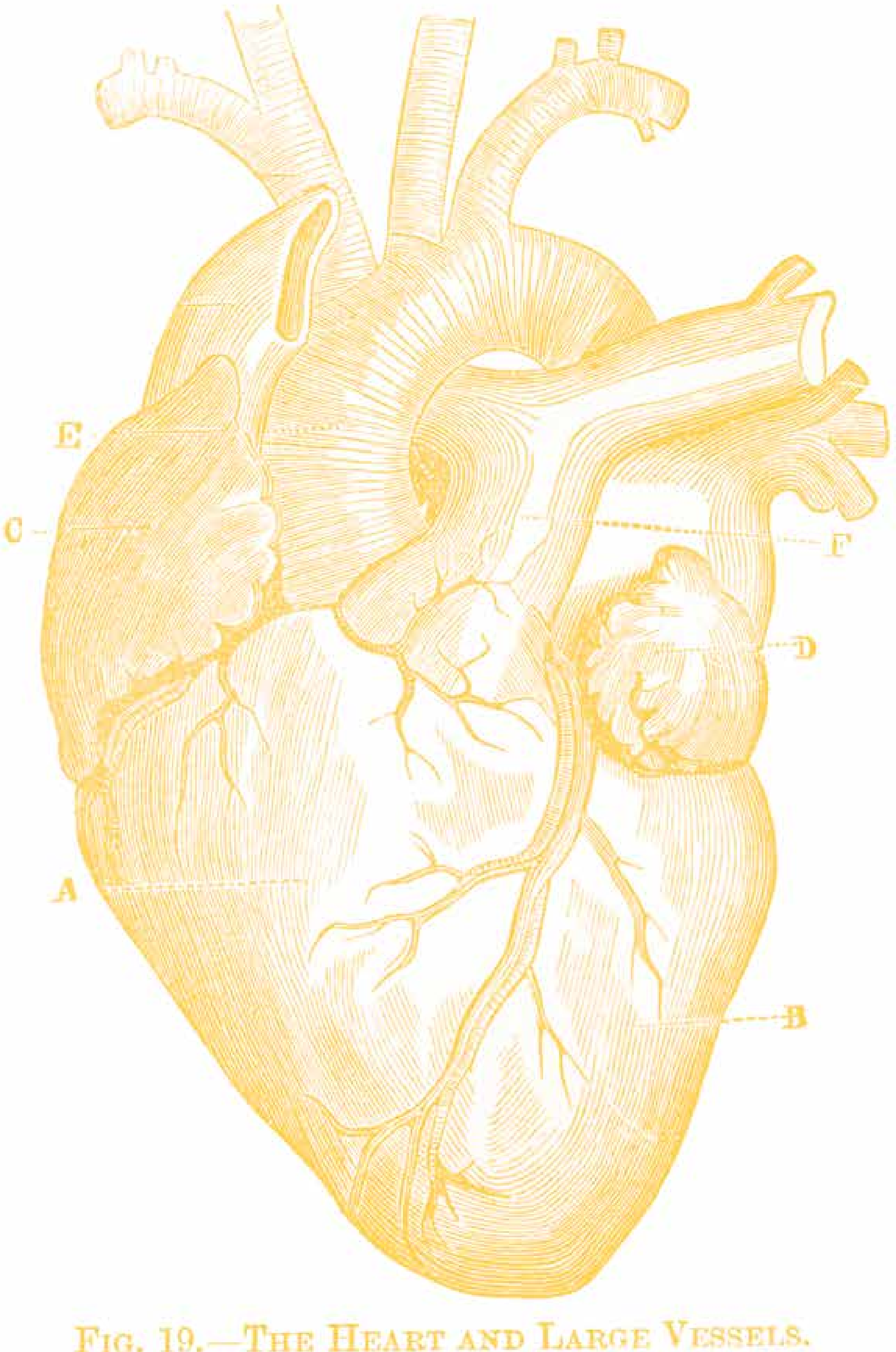


FIG. 19.—THE HEART AND LARGE VESSELS.

A, Right Ventricle.
B, Left "
C, Right Auricle.
D, Left Auricle.
E, Aorta.
F, Pulmonary Artery

4

Establish a flexible, tax-effective, tailored wealth creation vehicle

Self Managed Super Funds (SMSFs) have become wildly popular within the medical profession for three excellent reasons. Firstly, the income and capital gains tax rules are extremely generous. You are liable for just 15% income tax in the accumulation phase reducing to zero once a pension is commenced, and just 10% capital gains tax in the accumulation phase (provided the asset is held for more than one year). Second, the range of assets that can now be purchased in a SMSF is extensive. You are no longer restricted to just shares and term deposits, as you are now able to buy both commercial property (including your medical rooms) and residential property. Finally, the protection offered by a SMSF from creditors is even superior to that of a discretionary trust. Due to their growing popularity, the cost of establishment and annual maintenance of a SMSF has fallen significantly over the past five years.

5

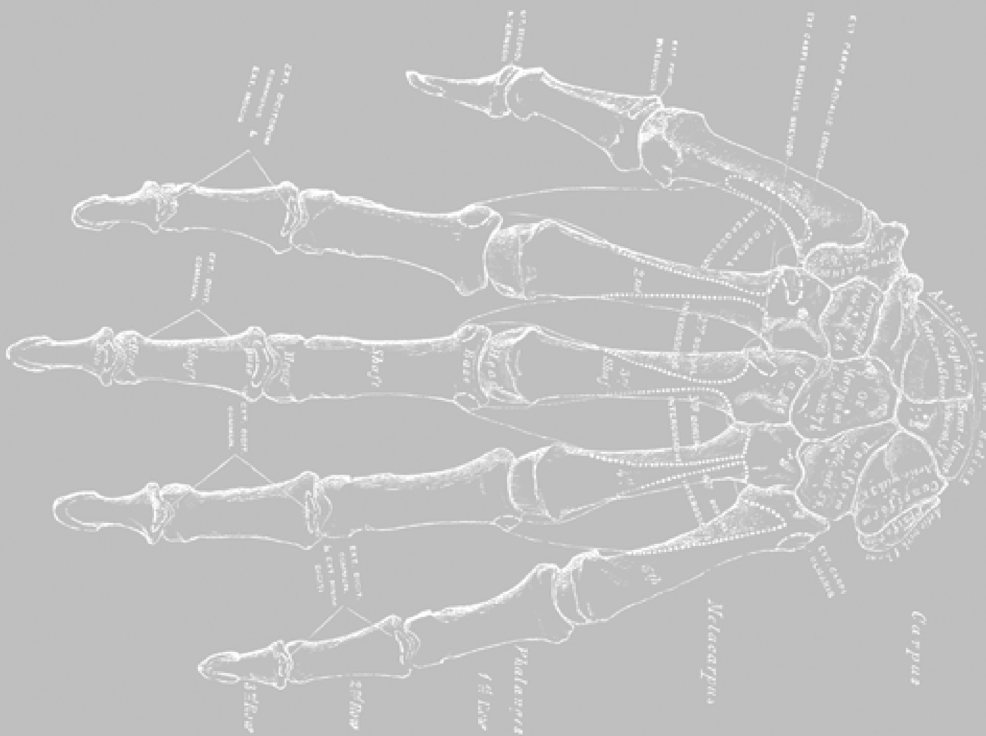
Establish your own Annual General Meeting

Each year Stanford Brown coordinates the activities and reports of your key professional advisers (Tax & Accounting, Insurance, Lending, Banking and Financial Planning) around the boardroom table. Like your medical team, your personal AGM needs to be cohesive and competent with leadership and direction.

6

Get started now!

You are starting the wealth creation process later than your peers, and are unlikely to have the luxury of a tax-free goodwill business sale on retirement. Hence it is critical that you get started early. Due to the miracle of compound interest, savings made in your 20s and 30s are far more valuable than the traditional savings period of the 50s.



Why choose Stanford Brown as your financial partner?

Teaming up with an expert financial advisory company is essential, but which one? Whilst we are fully aware that time is at a huge premium for you, we strongly recommend that you research a selection of financial and accounting advisory firms in order to choose the most competent and expert partner that is most suitable for your particular situation. This is a huge decision and one that shouldn't be taken lightly. If chosen wisely, you may well remain with this firm for 20 years or more.

Based in North Sydney, Stanford Brown is an award-winning boutique financial advice firm, specialising in the medical profession. Some of the benefits of choosing us as your financial partners are as follows:

- **Partner with a firm that has 25+ years of experience advising medical practitioners**
  We provide holistic advice for our clients in the areas of wealth creation, superannuation, personal insurance and mortgage lending. In addition, we work seamlessly with our partner firms in tax & accounting and estate planning. Over the course of our 25+ years of experience we have managed more than 300 insurance claims for our clients.
- **Partner with a firm that has a deep pool of talent and experience**
  Stanford Brown has assets under management in excess of $500 million and looks after the financial affairs of more than 1,000 clients, employing more than 30 staff. As an independently owned boutique firm (our three Partners all work full time in the business), we are small enough to geniunely value you and your business, and significant enough to provide the comfort and security that goes with a large firm.
- **Partner with a firm that will commit to act in your best interests**
  Our role as your adviser is to fully understand your financial goals and how these relate to your life goals, to develop a plan to enable you to realise these goals, to challenge your plans and assumptions, to lead you with courage through your journey, and to always act in your best interests.

When it comes to health, we place our trust in dedicated medical specialists, professionals who have benefited from years of experience and highly specialised training. And so too should financial health be entrusted to experts – experienced professionals who are not only highly proficient in the complex landscape of wealth creation and preservation, but who also understand the unique needs of a medical specialist and can tailor solutions accordingly.

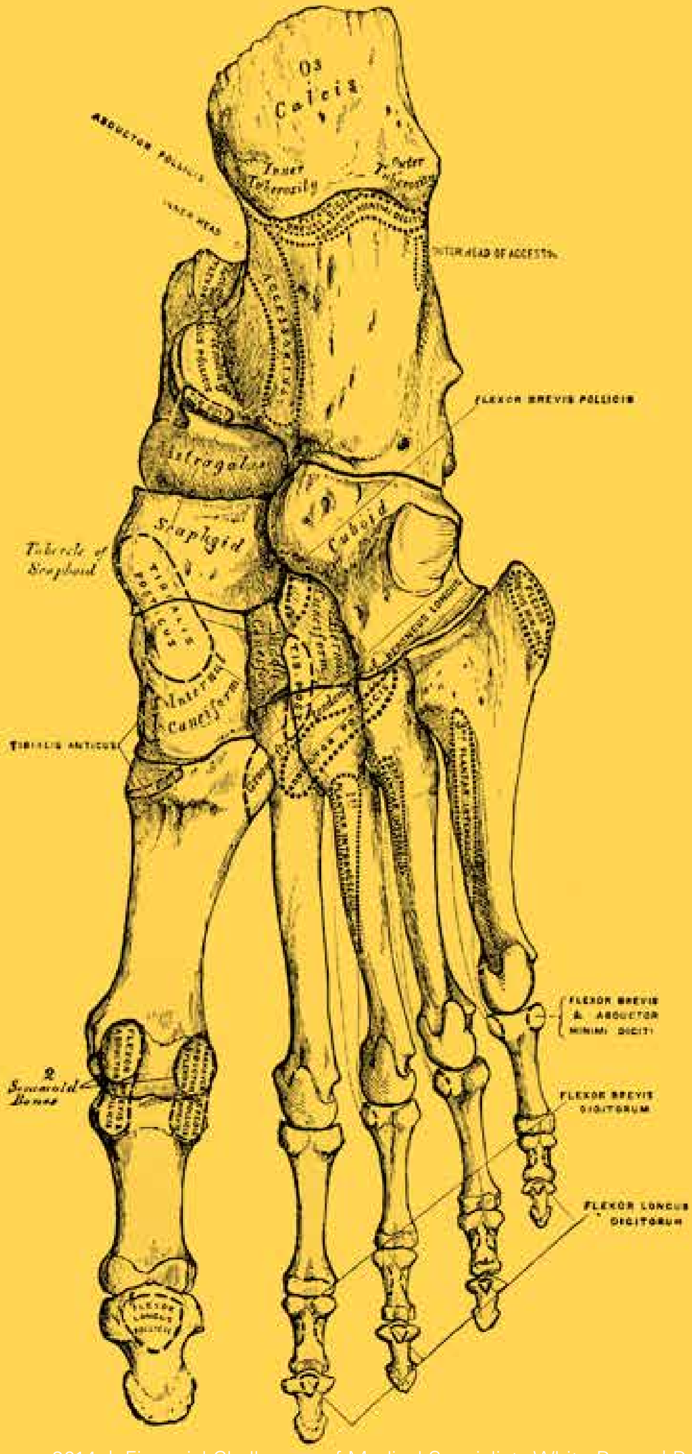
Who do we work best with?

Our ideal client is a medical practitioner who has achieved or wants to achieve a level of success in their professional life. They are able to make decisions, delegate and take advice.

Why do we specialise in doctors?

Over the years we have found that we work best with, and add the most value to, individuals from the medical profession. All our financial advisers are University educated with numerate degrees; all have many clients working in various roles within medicine and hence are familiar with the challenges and unique characteristics you face. Finally, we find that medics, more than any other profession, get the most value from our fee-based advisory services.

If you would like to find out more about Stanford Brown and our advice process, then pick up the phone and call us on 02 9904 1555 or send an email to help@stanfordbrown.com.au.



Appendix

Case Study 1

Transferring your Medical Rooms to your SMSF

Adam is a cardiac consultant and owns his own medical rooms valued at $500,000. Adam and his wife Eve are also members and trustees of the Garden of Eden Self Managed Super Fund (SMSF). This fund has a balance of $750,000 held in liquid assets such as shares and cash. The medical rooms are currently shared with two other consultants each of whom pays annual rental income to Adam of $15,000.

Should Adam transfer his medical rooms to his SMSF?

Before we examine the pros and cons, let's first understand how the transfer process works and the funding options available to the SMSF.

What's the process?

Adam would sell his medical rooms to his SMSF at a commercial rate (verified by an independent valuer) and then enter a lease agreement with his SMSF to rent the practice at a market rate. The sale of the medical rooms to the SMSF would constitute a disposal of the asset and is, hence, liable for Capital Gains Tax. It is also subject to Stamp Duty, but this may be reduced to a nominal $50 if Section 62A of the NSW Duties Act applies. For this to occur, the rooms must be owned solely by Adam and once transferred into his SMSF, must be for his sole benefit. This is a complex area and requires accounting advice.

It is vital that the Trust Deed of Adam's SMSF permits this transfer, as well as falling into line with the SMSF Investment Strategy. Again, this is complex and advice is required. SMSF Investment Strategies deal with issues such as asset allocation, liquidity and diversification. It is essential that the fund contains a healthy cash buffer to service any obligations of the building, especially if there is any possibility of it being untenanted.

How does the SMSF fund the purchase?

Purchasing a commercial property is unlikely to be a trivial matter. Fortunately, there are a number of financing options available to Adam.

i) Purchase the medical rooms using cash held in the SMSF. Nice idea, but few SMSFs have this kind of spare cash lying around. So …
ii) Purchase the medical rooms using a combination of cash and a contribution to super. Individuals are allowed to contribute up to $475,000 in one hit into their SMSFs. This comprises three year's worth of non-concessional contributions ($450,000) taking extra special care you don't breach the 3 year bring-forward laws (again, must take advice here) in addition to a $25,000 concessional contribution.
iii) Borrow the money from a bank using a limited recourse loan and a Bare Trust (mind numbingly complex – accountant essential!)

In our example, option two may offer Adam the optimal solution. He can bring forward 3 years super contributions, maximise his concessional contribution limit of $25,000 and hence will only need to find cash of $25,000 to fund the purchase.

So, why go to all this trouble (and expense…)

Here are the benefits of transferring medical rooms into a SMSF:

i) You pay a lot less tax. The rental income of $45,000 is taxed at just 15% whilst Adam is in 'accumulation phase' and becomes entirely tax-free once he starts a pension (possible from age 55). However, that's not all. If Adam subsequently decides to sell the medical rooms once he retires, then it is possible to exempt the sale from all Capital Gains Tax.
ii) You receive much greater protection from creditors in the event you are sued. We live in an increasingly litigious world and doctors are

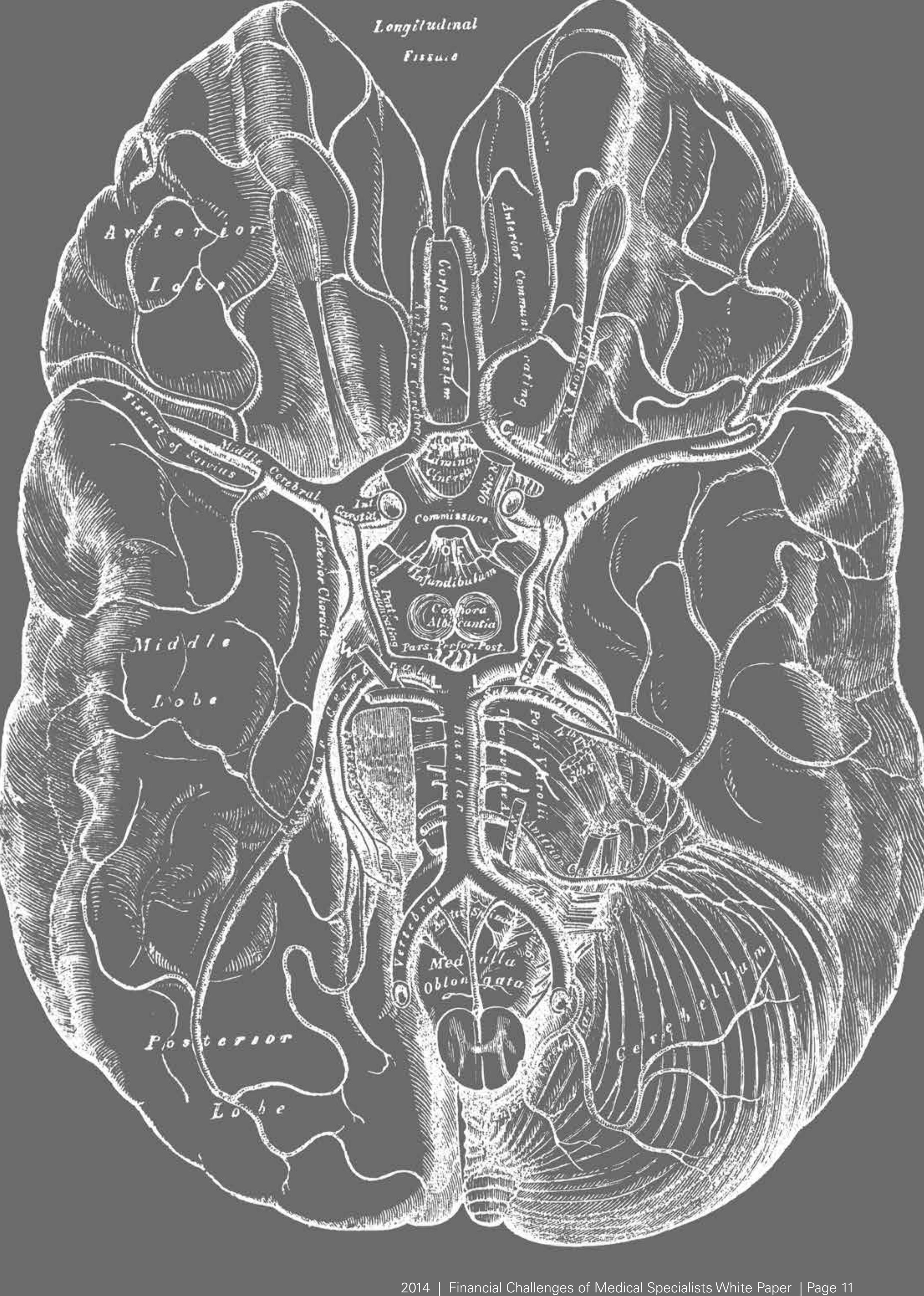
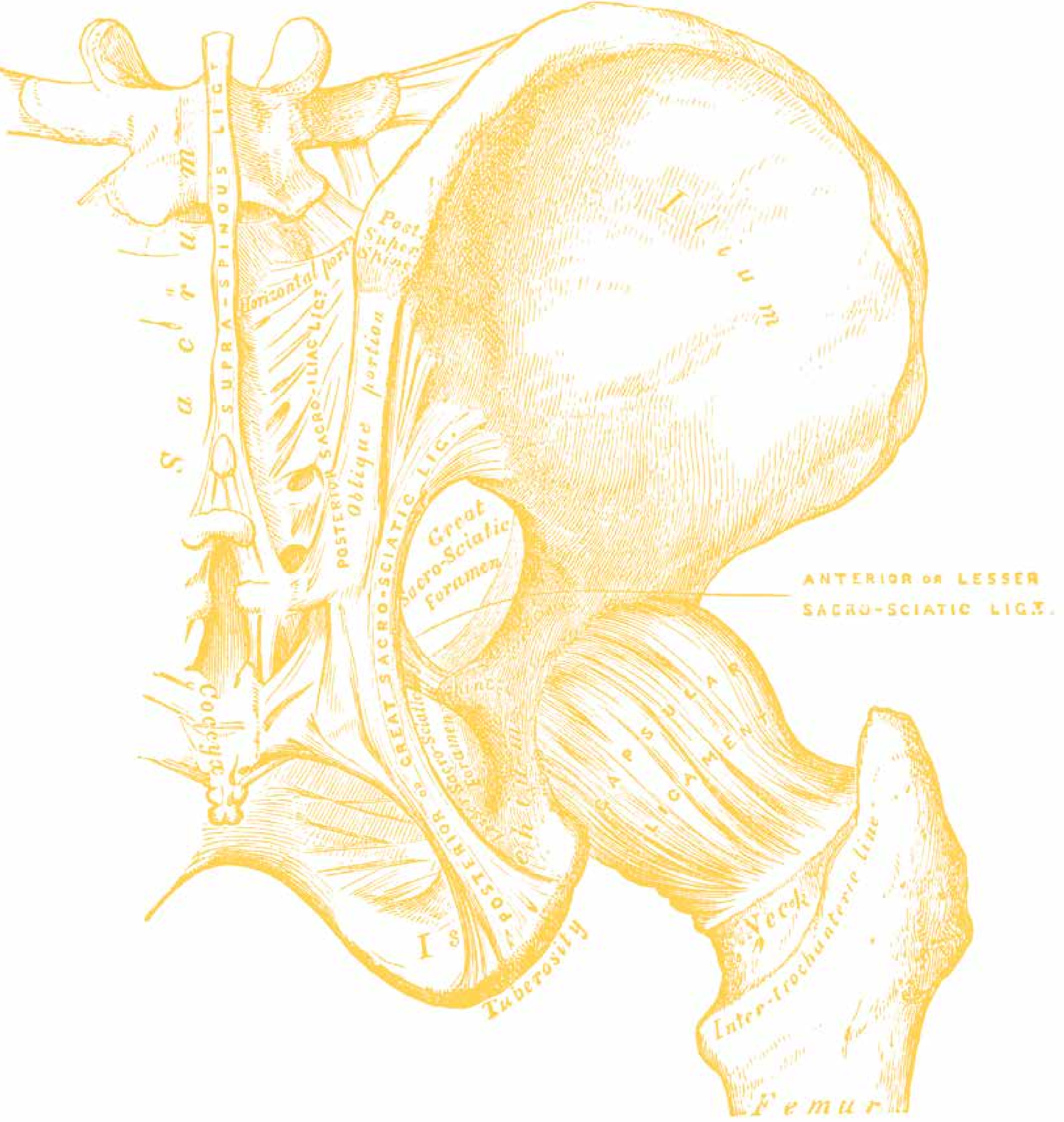

Longitudinal
Fissure
Anterior
Lobe
Corpus Callosum
Anterior Communicating
Fissure of Sylvius
Middle Cerebral
Commissure
Infundibulum
Corpora
Albicantia
Pars. Perfor. Post.
Anterior Choroid
Middle
Lobe
Basilar
Pons Varolii
Vertebral
Medulla
Oblongata
Posterior
Lobe
Cerebellum

Fig. 195.—Articulations of Pelvis and Hip. Posterior View.



expected by their patients to be perfect. The Bankruptcy Act provides far greater protection to assets owned inside Superannuation than outside.

Are there any disadvantages or pitfalls of this strategy?

Yes! Whilst the benefits are substantial, there are areas to be careful of. Namely:

i) Commercial properties such as medical rooms are highly illiquid assets. This means that they are difficult to sell in the event you have to (death, illness or buying that Learjet). Your SMSF has obligations to meet and needs a minimum amount of liquidity to do so.

ii) You may incur Capital Gains Tax and Stamp Duty on the transfer. These can both be very painful and should be avoided at all costs.

iii) A whole army of advisers will want a piece of the action. If your team of professionals (legal, accounting, and financial advice) have not dealt with these transactions before, you may end up subsidising their training as well as your personal request.

iv) Your SMSF is much more likely to get audited by ASIC if it purchases a commercial property. Hence your whole fund must be in perfect compliant order before a strategy like this takes place.

v) Both the transfer and the rental income must be set at commercial arms-length rates. You no longer have scope to offer 'mates rates'.

vi) If you need to borrow the money, the banks are likely to charge you a higher loan rate than that offered on your residential home. This is because the SMSF loan has to be non-recourse in nature. This means that if the SMSF defaults to the bank, they can only take the commercial property – they can't touch the rest of your Super Fund assets.

In Summary

Transferring commercial property into self managed super funds often leads to very substantial tax savings. In addition the asset ends up in a more creditor-secure location. But the process is complex and the potential to make mistakes is large. Advice is critical!

Case Study 2
The Importance of the right Insurance policy

John (48) is a specialist surgeon with a successful practice grossing over $1m per annum. At the recommendation of a colleague, John took out an income protection policy, as well as Life / Total & Permanent Disability insurance in 2003 and hadn't reviewed the policies since.

John considered himself fairly healthy, participating in regular exercise and following a balanced diet. However in January 2013, he began to be plagued with fatigue, blurred vision and headaches and decided to visit his own doctor.

Much to the shock of John and his family, he was diagnosed with brain cancer. This devastating blow threatened to interrupt his capacity to work for a significant amount of time – potentially years.

John's neurosurgeon mapped out a treatment plan, advising that if John failed to respond, surgery (ies) would be imminent.

Within days it became apparent that this would seriously jeopardise the practice's immediate cash flow. His ability to retain the practice support staff was suddenly uncertain.

Apart from his health concerns, John was deeply anxious about his financial future. He had a cash buffer and knew he had some insurance in place, but it had been 10 years since the policies had been arranged. John decided to ask some hard questions that he wished he asked 10 years ago.

Could he work intermittently when he was able, and still receive the full benefit?

Unfortunately for John, his policy was an older style contract, and will require him to be totally disabled, that is, perform no work (including administrative work) in order to receive the full monthly benefit from his Income Protection policy.

There are now specific Income Protection policies that have been tailored for medical professionals that allow the life insured to perform up to 10 hours per week of personal exertion employment and still be defined as totally disabled and therefore receive the full monthly benefit. This 10 "hour rule" would also allow John to work 10 hours per week during the waiting period whereas an older contract would add any days worked to the waiting period.

These 10 hours are often critical to allow a doctor to maintain minimum function of their practice.

Would insurance cover each of his business overheads in full?

John's insurance was only taken out to cover his income. The overheads of his business would remain in place and will rapidly deplete any cash buffer.

What if after the operation he couldn't perform specialist surgeon duties but could complete a medical administrative role. Would his insurance refuse to pay?

Income Protection – after the waiting period, Income Protection pays a monthly benefit (the sum insured amount) for as long as John is unable to perform his duties as a result of accident or sickness. If John is able to return to work in a reduced capacity, Income Protection will pay a partial payment. If John is unable to ever return to work due to accident or illness, then the monthly benefit is paid (indexed annually) until the agreed benefit payment period, which will usually be age 65. Income Protection policies tailored for medical professionals are now offering age 70 benefit payment periods.

Would an Income Protection Claim be paid?

YES. As John is unable to engage in his usual occupation, then after the waiting period has expired, the monthly benefit would be paid each month. If John elected to return to work in an administrative capacity on a significantly reduced income, then the Income Protection policy would pay the difference between the sum insured amount and the income derived from performing the administrative function.

Total & Permanent Disablement ("TPD") insurance – pays a lump sum when two medical professionals (selected by the insurer) determine that in their opinion, it is unlikely the life insured will ever engage in any occupation for which they are reasonably suited through training, education or experience.

For certain occupation categories (Medical Professionals included) the any occupation definition can be upgraded to an own occupation definition which requires that in the opinion of the two medical professionals selected by the insurer, the life insured is unlikely to ever again engage in their own occupation.

Would a TPD Claim be paid?

As John was 38 when he took out insurances cash flow was tight, so he elected to go with the cheaper option of 'any' occupation. Had John selected an 'own' occupation definition and it was determined that due to the deterioration of John's fine motor skills it unlikely he would ever be able to perform surgery again, then the sum insured would be paid. Unfortunately John's policy was an 'any' occupation definition, so if it is determined that although John could no longer be a surgeon he could be a GP, medical consultant or even a lecturer of medicine at university, then no payment will be paid.

In Summary

Insurance is a specialised field and it is wise to seek the counsel of advisers who have an intimate knowledge of both the type of insurance products that are best suited to medical professionals and the intricacies of the claims process.

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