Physicians' Financial Questions Answered

October 2021 • Russell Van Sistine, CFP®

Q: When can I retire?

A: I must confess this is a question that I submitted. I think it's an important one that must be answered. Retirement is different for everyone, but the answer of when is the same for everyone*. "You can retire when you no longer need to work for money, but the money you have works for you."* Unfortunately, this very rarely happens by chance. It requires a goal (typically a time frame and income level), execution, and readjustment as circumstances change. Let's look at some numbers to explain:

1. Let's assume you are 50 years old and want to retire at age 65.
2. You want an equivalent income of $150,000 in today's dollars.
3. Let's assume that you have no desire to leave any inheritance.
4. Average rate of inflation is 3%.
5. Average rate of return, for conservative reasons, is 6%.
6. We are going to ignore taxes for this scenario.
7. You statistically plan to live until age 95.
8. Let's assume no pensions or Social Security income.

This is the simplest I can make the scenario for math reasons. If this is the case by the time you turn 65, you will want to have $4.76 million saved. Every change we make to the above scenario changes this number. If you have Social Security income, that number gets smaller. If you have real estate investments, that creates income and this number gets smaller. If inflation is higher, that number gets bigger. If you have higher rates of return, that number gets smaller.

These variables change every year and must be watched to increase the likelihood of retiring as soon as you want. Therefore, your financial professional wants to meet with you on a regular basis. We want to make sure we are staying on track; we want to make sure that your investments are getting <u>at least</u> the average rate of return to get you to where you want to be.

If you don't know your retirement number, it's time to make sure you have a plan that works. Markets fluctuate, income changes, unexpected expenses arise and for these reasons, you must create a financial plan with realistic expectations.

Q: Help us understand impact investing and socially conscious investing. What are the options to ensure our money is not being invested in companies doing harm to health and the planet? This goes beyond not investing in tobacco.

A: Environmental, Social, and Governance (ESG) Investing. This topic has become a great hit in the investment world lately. As in investor, it is important to make sure that you are investing with a purpose. Often the simple purpose of investing is to reach your financial goals faster than if you were to do it on your own. Now people are finding added purpose in investing that promotes the betterment of our world. Currently when people want to invest in such a way, they are looking for companies that are rated on some sort of Environmental, Social and Governance standard.

The difficult part is that there is no standard. The CFA Institute, which produces one of the most prestigious designations for financial analysts, is working on creating a platform for analyzing ESG Investments. Below is the CFA Institute's web address, as well as a link to its ESG Investing book for investment professionals. A must read if you want to get involved with ESG investing.

There are some important things to be aware of the current world of ESG Investing when using a fund manager to do the investing:

1. ESG Investing highly favors technology stocks, (the most often named as top ESG companies are Microsoft, Salesforce, NVIDIA, etc.) because technology companies tend to produce considerably less carbon than manufacturing companies. This creates a diversification problem.
2. A continuation of the above is that with a heavy weighting in technology, the returns of ESG funds are primarily coming from those technology stocks. If something happens to those heavily invested companies, you will feel it across all of your ESG funds.
3. No two ESG funds are going to measure ESG the same way, or necessarily the way that you yourself do. For this reason, it is important to read very carefully the Fund Prospectus.

Opinion: If you have a desire to invest in companies that are doing good for the world, my invitation would be to create the standard that works best for you. Seek out companies that you want to help because of the good they are doing. Then create a financial plan that calculates the risk you are taking on. As a financial professional, my job is to mitigate as much risk as I can to get an individual where they financially want to be with a greater degree of probability. With the current state of ESG Investing, there is a lot of added risk due to the reduced amount of diversification. It seems to me that at this time we can do more good helping the causes we want to support by getting involved and volunteering. This reinforces my desire to support community and the people I want to serve without sacrificing my ability to retire when I want to retire.

CFA Institute “Environmental, Social, and Governance issues in Investing”: https://www.cfainstitute.org/-/media/documents/article/position-paper/esg-issues-in-investing-a-guide-for-investment-professionals.ashx

CFA Institute main page for ESG investing: https://www.cfainstitute.org/en/advocacy/policy-positions/environmental-social-and-governance-issues-in-investing-a-guide-for-investment-professionals

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Q: Please talk about incentives for home improvements and purchases that are good for the planet—like going solar or buying an electric car, etc. What are the tax benefits? It’s hard to find these topics and know what the options are.

A: Incentives for personal consumption of “Green Technology.” This answer will have to come with a qualifying disclaimer: I am not a tax professional and cannot give tax advice, it is recommended that you take the information below to your CPA or tax professional to verify your eligibility for all tax incentives.

Now that I have the attorneys off my back, for electric vehicles please visit this website: https://fueleconomy.gov/feg/taxevb.shtml. The site has a list of all electric vehicles that are currently giving tax credits up to $7,500 and any stipulations attached to the credits. As this is a government website, I can’t guarantee how often it is updated.

Additionally, you can find more incentives for the state of California here: https://afdc.energy.gov/laws/state_summary?state=CA. Specifically, you may want to look at the California Clean Fuel Reward, which can offer a tax incentive of $1,500.

Similarly for solar, the governments website is: https://www.energy.gov/eere/solar/homeowners-guide-federal-tax-credit-solar-photovoltaics. The simple answer is that the Federal Government will give you a tax credit for 26% of the cost of installation minus any utility rebate on the cost of solar instillation—if completed before Dec. 31, 2022. The tax credit then drops to 22% for 2023. I found many websites that discussed a California tax credit; however, I couldn’t find a government website that said there was one. For this reason, I am not posting anything for the State of California. Please reach out to your tax professional and discuss with them.

Q: What about about investing in real estate in order to improve access to housing? How can we make it affordable for tenants, but still a reasonable investment strategy?

A: Investing in real estate to improve the community. This question is one that sits near and dear to my heart. Primarily because it involves so much of my favorite subject—Economics (my degree is in financial economics from Brigham Young University-Idaho).

The difficulty of this question is that a "reasonable" investment strategy is different for everyone. For some with incredibly low tolerance for risk, 3% is a reasonable strategy, while some with extreme levels of risk won't touch something unless they are likely to see double-digit returns. Let's look at some numbers and a scenario:

1. You purchase a home for $500,000 with no mortgage.
2. The only cost of the home is the original purchase, no upkeep, no property taxes, etc.
3. You charge $1,500 a month for rent and keep 100% of it.
4. You sell the home 15 years later for $783,715.86 (growth at 3% a year; obviously this isn't a California home.) No closing costs on the sale of your home.

With the above scenario, your average rate of return will be just under 5.94%. This is done using a cash flow calculation. Now apply this to reality, as the conditions for this do not exist. Every cost you incur over the next 15 years makes that return smaller. If you need a mortgage, you have the interest rate working against you. If there are a few months that go by without a renter, your rate of return goes down. If you must replace a roof, or wall, or washer, your rate of return goes down. These complications are why real estate investing is where it is in Sonoma County.

Opinion: There needs to be much more growth in properties to make it beneficial here in Sonoma County. If this means building on green space between Santa Rosa and Rohnert Park, that will be up to local voters. Purely from a supply and demand standpoint, building rapidly in any county with a shortage in housing will eventually lower the price of rent.
