

The Basics

Game plans from the NFL's instant millionaires

Even if you'll never catch a touchdown pass, the advice given to some superstar rookies can help you score a solid retirement plan.

By [Kiplinger's Personal Finance Magazine](#)

At the age of 25, Steve Smith has the same financial goals as most family men: build a college fund for his children, move to a bigger house, save for a secure retirement and give something back to the community. But there's one big difference between Smith and most other 25-year-olds: \$27.5 million.

That's the size of the six-year contract extension signed last spring by Smith, a wide receiver with the Carolina Panthers. (You might remember him scoring a touchdown in a recent Super Bowl.)

You'd think a windfall that large would put Smith on easy street, and his goals within easy reach. Ditto for other players in the NFL, where first- and second-round draft picks customarily get million-dollar signing bonuses. A third-round draft pick in 2001, Smith got about \$500,000, plus a first-year salary of \$209,000. This year, most NFL rookies make \$230,000.

The three-year career

But unlike those of us who have to plan for 20 to 30 years in retirement, NFL players have to plan for more than half a century. On average, an NFL player's career lasts about three years. Although most players end up with other jobs, they rarely match their earnings from football.

And those earnings are in jeopardy even before they're paid out. Agents and financial "advisers" often try to lure players with loans for the full amount of an anticipated signing bonus. When and if players actually get the money, it can be reduced by more than half, factoring in taxes, the agent's cut and NFL Players Association dues. All that puts some players in debt before they take the field.

And then there's the irresistible pressure to dole out money to family and friends and to buy a mansion and a fancy car.

"Coming out of college, I helped some family members, paid off debts and spent money on things I shouldn't have," says Smith, who went to the University of Utah. But he didn't get into the debt trap.

Now, with a multimillion-dollar contract, Smith is more determined than ever to make the most of his good fortune. He's working with Jon Peterson of Next Level Financial Group, in Sausalito, Calif., whose clients -- including 18 NFL players and about 20 college players who are expected to sign with the pros -- pay up to 1.5% of assets under management for his services. All have been carefully selected for their potential staying power in the NFL and for their willingness to buy into Peterson's philosophy: "If you're going to drink it, drive it or wrap it around your neck, that's not money management."

Instead, Peterson's clients learn about patience and pacing -- lessons familiar to those of us who don't earn big bucks catching passes. "You have to pay yourself and save as much as possible," says Smith, the frugal millionaire. On the other hand, the rest of us can learn from Peterson's strategies to minimize Smith's tax bill, protect his assets, prepare for retirement and stretch his money as far as possible.

The monthly allotment

Despite the eye-popping numbers, only a fraction of the money from Smith's contract is guaranteed. He can count on an up-front bonus of several million dollars; the rest is spread out over a half-dozen years.

For NFL rookies, it's especially critical to preserve a lump-sum signing bonus because long-term income is far from a sure thing. Jorge Cordova, one of Peterson's clients and this year's third-round draft pick with the Jacksonville Jaguars, blew out his knee in late August before the season even started. Now on injured reserve, his first-year salary will be cut from \$230,000 to \$130,000.

Peterson generally takes his clients' income and parcels out the money to several pots. He sets aside enough cash in a money-market account to cover six months' worth of regular expenses. He also gives his clients a regular monthly allotment to smooth out their income over 12 months. (Players receive the bulk of their salary during the official season, which ends in January.)

Only when those bases are covered do the players begin to invest. Even then, Peterson starts by having them max out contributions to their 401(k) plan, to which the NFL kicks in a generous \$2 match for every dollar the players sock away. They also invest in taxable accounts, primarily in mutual funds that hold blue-chip stocks. After they have accumulated at least \$200,000 in taxable investments, Peterson switches them from mutual funds to managed accounts in which they own individual securities and can control when to take gains and losses for the best tax outcome.

Even when players receive big signing bonuses, Peterson leaves riskier investments -- such as restaurants and real estate other than players' homes -- for the future. "If you have \$50 million and lose \$50,000 in Mexican real estate, you just lick your wounds," says Peterson. "But if you're worth only \$100,000, a loss that size is a problem."

Peterson urges his players to pay off their credit-card bills every month. And he discourages them from buying a house during their rookie year because -- as Jorge Cordova discovered -- an athlete's life can change quickly and unexpectedly.

When players are ready to buy a house, Peterson prefers that they take out a mortgage, even if they can afford to pay cash. That way they avoid having too much of their money tied up in a house and get a tax break on their interest payments. Players can buy tax-free bonds that generate enough income to cover the mortgage payments.

Because NFL players may spend just a few years in any one city, Peterson recommends that they get a three- to five-year adjustable-rate loan or an interest-only mortgage, which holds down their monthly payments. Lest they be saddled with a huge mortgage after their career ends, he likes them to pay ahead or set aside enough money to pay off the loan if necessary.

Tax-saving strategies

Signing bonuses are paid in a lump sum, just like any windfall, so they typically bump players into the top tax bracket (the 35% bracket starts at \$319,000 this year, whether you're single or married). To minimize the extra taxes, players often take advantage of their vagabond careers to take up residence in a state that doesn't have an income tax, such as Texas or Florida.

Contributing the maximum amount to a 401(k) plan helps a bit, as do charitable contributions. Smith had been donating money to children's causes in the Charlotte, N.C. area but wasn't doing a good job of tracking how much he actually gave. As a result, he was losing thousands of dollars in tax breaks because he couldn't always put his hands on receipts and canceled checks.

With one bonus, Smith set up the Posey Foundation, named after college teammate Demetrius Posey, who died in an auto accident in 2003. During the off-season, Smith and his wife, Angie, spend a lot of time working with the foundation, which helps local children who are underprivileged or abused. "The money was a gift to me, so I feel like I should be making a gift to others," says Smith.

Setting up a foundation can be both expensive and complicated, so Peterson generally recommends that players with less than \$2 million to donate start with a [donor-advised fund](#). These arrangements, which are offered by many mutual fund companies and brokerage firms, let donors make a gift and get an immediate income-tax deduction. They can then invest the money and take their time deciding which charities to support. You can usually start such a fund with as little as \$10,000.

Another key tax strategy is for players to defer taxes on investment income until their NFL career is over and their tax bracket is probably lower. For pro football players, that could be 10 years or less.

This is one of those rare situations in which a deferred annuity can make sense. Deferred annuities generally aren't a good idea because fees are high and distributions are taxed as ordinary income rather than as capital gains. But for former football players who want to have a guaranteed income for the rest of their lives, these annuities can be just the ticket.

Peterson generally recommends a GE Retirement Answer annuity from Genworth Financial (formerly GE Financial). The money must be invested for at least 10 years before you can start to access the funds, which could be age 35 given the length of an NFL career. At that point, you convert to a variable immediate annuity and start to receive regular payouts that can last for the rest of your life or for a set number of years.

The company guarantees a minimum income floor based on lifetime investment performance of at least 5% per year, and your payouts can increase if the investments perform better than the guarantee over time.

As long as you elect to receive regular payouts for life, you can begin distributions before age 59-1/2 with no early-withdrawal penalty, and a portion of each payment isn't taxed because it's considered a return of principal.

Smith invested a piece of his recent bonus in a deferred annuity and will continue to add money throughout the year. As a result, he'll be able to guarantee his family an income in the low six figures after he quits the game. "Retirement will be all wrapped up by next year," says Smith.

College: a big head start

Smith has set aside \$120,000 from his signing bonus in 529 college savings plans for his children, Peyton, 7, and Baylee, 3; he and Angie are expecting a third child in April. Peterson likes 529 plans for his players because the accounts allow generous contributions and are among the few ways to earn investment income for college that's tax-free, regardless of your income level.

Assuming the plan earns an average annual return of 8%, Smith's investment should grow to nearly \$302,000 in 12 years -- which could be enough to cover the entire bill. Nevertheless, Smith continues to add money to his children's college savings by patronizing stores that participate in the Upromise program, which rebates a percentage of purchases to a college account. "We go out of our way to drive to stores that participate," says Smith. So far, purchases have put about \$5,000 in Upromise accounts for each of his children.

Playing it safe

Life insurance, liability insurance, disability insurance -- football players usually load up on as much coverage as they can get to protect themselves and others who depend on their income. Peterson generally recommends buying term insurance rather than a cash-value policy. Not only is term insurance a lot less expensive, but it also lets players manage their investments independently.

Liability coverage is a must for NFL players, whose presumed deep pockets are a magnet for lawsuits. On top of the maximum liability insurance available through their homeowners and

auto insurance, players typically add a few million dollars more in coverage with an umbrella policy.

Disability insurance is also critical, especially for top-notch college players who want to protect their future value. But it's expensive -- an annual premium of \$12,000 per \$1 million of coverage -- and not every player qualifies. A good employment contract can also provide some protection. It made a difference for Smith -- he broke his leg in the Panthers' first game, but his income hasn't been affected so far because he is expected to return by the end of the season.

One of Smith's biggest concerns is estate planning for his children. He'll be working with a lawyer to create a will that makes it clear how the children's guardian would be allowed to spend their inheritance. Says Smith, "You have to spell it out line by line."