Total Term

ASSESSMENT GUIDE

Total Term (Tt) estimates the number of years a client could live on their current assets at their current lifestyle if neither changed.

Elements®
Financial Planning System

Total Term

Assessment Guide

What is it?

Total Term (Tt) estimates the number of years a client could live on their current assets at their current lifestyle if neither changed.

CALCULATION

Net Worth
÷ Annual Living Expenses

Total Term

17.9
Tt
Total Term

Example: If a client's net worth is $1,000,000 and they spend $100,000 annually, then their Total Term (Tt) is 10. They could live for about 10 years on their assets assuming no asset growth and no change in spending.

Why is it important?

Typically, at the core of most clients' goals are some personalized versions of "freedom" or "security". And to that end, clients often ask questions like “how am I doing?” or “do I have enough money?”

While these are certainly broad questions that require deeper discussions, Total Term is a great anchoring point to quickly address that question, framing the answer in a way that is easily digestible by the client (years versus dollars).You can also look at the change in Total Term over time to better understand the pace of a client’s progression towards financial independence.

Lastly, breaking apart Total Term by its underlying components - Liquid Term, Qualified Term, Real Estate Term, and Business Term - can help frame the health of the score. Ultimately, finding the “right” mix of assets can help you better understand if a client is prepared for retirement.

A traditional long-term retirement projection is useful in certain cases, but it’s “expensive” (i.e. time consuming) as the basis for an ongoing monitor of “where am I?” (and the implied precision can actually provide a false sense of certainty in some cases). Alternatively, Total Term is an efficient tool at broadly understanding and conveying current health and progress towards financial independence.

How do I use it?

Use this process to assess whether a client’s Total Term is appropriate or if they need to make improvements:

1. **Accuracy:** Ensure the accuracy of the Total Term inputs.
2. **Assessment:** Assess whether the given Total Term is appropriate.
3. **Improvement:** Identify areas of improvement.

STEP 1

Score Accuracy

1. Updating Net Worth: To calculate any of the Term Elements scores all you need is an up-to-date net worth statement and an accurate spending number (see the burn rate guide for details on how to obtain an accurate spending number).

Populating a client's net worth by adding accounts is only the first step. Maintaining the accuracy of those accounts over time is essential to tracking progress. The following table displays how frequently you should try to obtain updated values for different types of assets and liabilities to ensure a reliable set of Term scores.

Quarterly	• **Cash accounts** • **After- and pre-tax investments** • **Debt balances**
Annually	• **Real Estate** • **Businesses**

Elements' client prompts and the quarterly net worth progress reporting process will help clients keep these values up to date, in addition to any client education you can provide them on the purpose of helping you maintain an accurate net worth statement.

2. Accounting for Student Loans & Consumer Debt: Generally, Total Term is the sum of the other four term elements (Liquid Term, Qualified Term, Real Estate Term, and Business Term) which are net equity values (i.e. net of related debts). However, in cases that involve student loans or high consumer debt, the Total Term score will be less than the sum since these debts typically aren't netted against other assets (just against net worth as a whole).

Example: A client has a net worth of $1,000,000 and spends $100,000 annually. Included in net worth is a student loan balance of $200,000. While the following term scores add up to 16.3, Total Term is 10.0 since the student loan is only netted out of total net worth, not individual assets within each of the other Term scores:

- Lt = 1.7
- Qt = 0.4
- Rt = 2.6
- Bt = 11.6

STEP 2

Score Assessment

To assess this score:

1. **Determine whether the score is too high, too low, or just right.**
2. **Review the asset mix and underlying term scores.**

Score Ranges

Average Total Term scores and associated growth rates depend primarily on age as a barometer of net worth size. The following graph presents average Total Term scores based on age ranges.

Age Range	Tt Score Range	Tt Annual Growth
25–35	< 5	0.5–1
35–45	5–15	1
45–55	15–25	1–2
55+	25+	2–4

Generally, a client's Total Term will increase at a nonlinear rate:

- **When a client is young and net worth is likely lower, it grows at a smaller rate; a larger portion of their cash flow is allocated toward non-discretionary living expenses (versus saving) and the effects of compound growth have yet to really kick-in.**
- **When a client is older and net worth is likely higher, it grows at a higher rate; they have more disposable income to save and the effects of compound growth are greater.**

CORRELATING FACTORS

Understanding the correlation between these factors and your Total Term will help you determine if the given score is appropriate or not.

Lower Tt Scores

Higher Future Income

Higher Tt Scores

Higher Lifetime Income

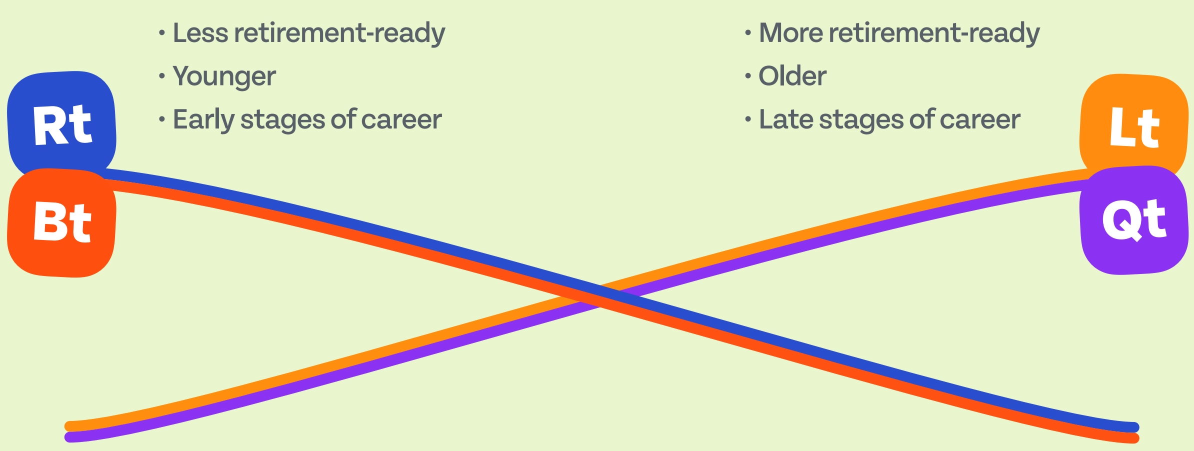
Older Clients

Sooner Retirement Date

Asset Mix

It’s also essential that you examine the underlying assets to determine if a client has an appropriate asset mix. The “right” mix of assets depends on a variety of factors that differ from client to client. However, the following graphic displays the general principle at play when assessing if a client’s asset mix is appropriate.

HOW IS YOUR CLIENT'S ASSET MIX?



Generally, a client with a heavier allocation toward Liquid Term and Qualified Term will have more flexibility in their retirement strategies. Whereas a client with a heavier allocation towards less liquid assets like Real Estate Term and Business Term will have less flexibility in their strategies.

Further, when considering a client’s “retirement readiness,” look at both the composition and overall size of their Real Estate Term. Personal-use real estate should generally not be considered as part of the retirement strategy. So for clients whose Real Estate Term is highly or completely composed of their primary residence, you might want to consider reducing their Total Term by that value.

Example: A client has a Total Term (Tt) of 28.0 and a Real Estate Term (Rt) of 12.0. Approximately half of their Rt score is composed of equity in their primary residence, while the remaining is composed of income-producing investment properties. Therefore, this client's Tt score is more reasonably closer to 22.

Alternatively, liquidating personal real estate in favor of renting could meaningfully change the composition of a client's Term scores (i.e. more liquid assets, higher spending).

STEP 3

Score Improvement

To start, you should consider the following overarching questions as you seek to make overall improvements to your clients' Total Term and financial health.

- **What is the underlying asset mix of other Elements (Lt vs Qt vs Rt vs Bt)?**
- **Is the client's Tt over-reliant on certain asset types?**
- **In which Term Elements can the client feasibly make some improvements to scores?**

As it relates to the underlying individual Elements, consider the following levers a client can pull to improve the absolute value of their Total Term score or the pace of its growth:

LEVERS FOR GROWING TOTAL TERM

Savings

- Is the client able to save more?
- Where should the client be saving at this stage in their life?
- Will future retirement income lessen the reliance on assets alone for income?

Spending

- Should the client reduce spending?
- Can the client afford to increase spending?

Debt Reduction

- Should the client accelerate their debt payoff?
- Should the client refinance to improve cash flow?

Asset/Income Growth

- Should the client reallocate their investments to pursue a different growth rate?
- Does the client need to find opportunities to increase their income?
- Should the client invest more in their business or other private ventures?

Case Study

Let's look at the following example and apply the principles presented above. This case study assumes you've already ensured that you have a good estimate.

Example: Given a Total Term of 12.9 and considering the following information, you begin your assessment of whether a client's Total Term is appropriate:

Lt = 1.7	Qt = 4.1	Rt = 1.1	Bt = 6.0	Tt = 12.9

Lifetime Income	**$2.7 million**
Age	**52**
Future Retirement Income	**40% income replacement**
Target Retirement	**About 10 years away**

Step 1 - Determine Score Appropriateness: By first considering this client's age, you determine their score of 12.9 is far below average.

Then, considering the additional information you find that given a shorter time horizon until retirement and a large income replacement, this client's Total Term score is too low for their needs.

Step 2 - Identify Improvements: Through data gathering, you find that the client can save additional money each month, and that they could stand higher risk in their investments. You target a healthy Total Term growth year over year, and use that as your guide.