CHAKA™
STRATEGY

Essentials of Time Value of Money©

A Key Financial Concept for Lawyers

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Background – Chaka Patterson

- Partner at Alston & Bird (and former Partner at Jenner & Block and Jones Day)
- Professor at University of Chicago Law School
- Former General Counsel of a Fortune 1000 Global Education Company
- Former Treasurer & VP for Investor Relations of a Fortune 100 Energy Company
- JD from Harvard Law School
- MBA from University of Chicago Booth School of Business

HARVARD LAW SCHOOL

CHICAGO BOOTH
The University of Chicago Booth School of Business

THE UNIVERSITY OF CHICAGO
THE LAW SCHOOL

Introduction: Key Takeaways

- The Time Value of Money (TVM) is a foundational financial principle
- Lawyers frequently encounter situations where understanding TVM is crucial–whether negotiating settlements, calculating damages, or advising clients on financial decisions

What is the Time Value of Money?

The Time Value of Money means that money available today is worth more than the same amount in the future due to its potential earning capacity

This principle underpins concepts like Present Value (PV), Future Value (FV), and Discounting

Core Concepts of TVM

1. **Present Value (PV):** The value of future money in today's terms
2. **Future Value (FV):** The amount your money will grow in the future
3. **Interest Rates:** These determine the rate of growth or discount
4. **Compounding:** Earning interest on principal and previously earned interest
5. **Discounting:** Calculating today's value of future cash flows

Why TVM Matters for Lawyers

- Evaluating settlement offers.
- Calculating damages for future lost income.
- Dividing financial assets in divorce cases.
- Negotiating structured payments in contracts.
- Advising on estate planning and tax strategies.

Real-World Applications

- Litigation
- Corporate Law
- Family Law
- Tax Law
- Estate Planning

Tools for TVM Calculations

- Financial calculators or apps.
- Spreadsheet software like Excel (using PV and FV functions).
- Consultation with financial experts.

TVM Example 1

Business Contract Negotiations

Scenario:

A client enters into a contract where payments for goods or services are structured over multiple years. The client wants to evaluate whether the proposed payment terms are fair compared to receiving a single upfront payment.

Application of TVM:

- The lawyer helps their client assess the present value of the structured payments.
- They negotiate adjustments if the structured payments undervalue the deal in today's terms.

TVM Example 2

Settlement Negotiations

Scenario:

In a breach of contract case, the defendant offers a settlement of $10,000,000 in five equal annual payments. Alternatively, they offer $9,000,000 as a lump sum today.

Application of TVM:

- The lawyer calculates the present value of the $10,000,000 structured payments.
- They determine if the lump sum payment today is more advantageous, factoring in potential investment opportunities for the client.

TVM Example 3

Real Estate Transactions

Scenario:

A developer offers to pay for land in installments over five years rather than a single payment. The lawyer represents the seller and must assess whether the installment terms are fair.

Application of TVM:

- The lawyer calculates the present value of the installment payments using an appropriate discount rate (e.g., the rate of return the seller might earn if they had the full amount upfront).
- They use this calculation to decide whether to renegotiate terms or accept the deal.

TVM Example 4

Structured Settlements

Scenario:

A client wins a lawsuit and is offered structured payments of $50,000 annually for 20 years or a $750,000 lump sum today.

Application of TVM:

- The lawyer compares the present value of the structured payments to the lump sum.
- They advise the client on which option is more financially advantageous, considering interest rates and potential investment returns.

TVM Example 5

Class Action Settlements

Scenario:

In a class action lawsuit, the settlement offers include payouts over a decade. The lawyer represents the class and must ensure the settlement is fair in today's terms.

Application of TVM:

- The lawyer calculates the present value of the settlement payouts.
- They use this analysis to argue for a fairer lump sum payment or negotiate adjustments to the payout schedule.

Key Takeaways

TVM is crucial for financial accuracy in legal scenarios.

It ensures fair and informed decision-making for clients.

Understanding TVM enhances your value as a lawyer.

Mastering TVM helps you negotiate smarter outcomes.

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