

STATE TREASURER

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Summary: Personal Money Management Discussion

Part one: This is your money. You want to be prudent, match expenditures with your income and provide for your future recognizing effects of inflation through the years. This part is not going to address legalities-just what might be some reasonable approaches to realize your objectives.

1. You set up a checking account, state general fund, savings account for out of the normal expenditures, spending reserve account, and 401(k), corpus of PMTF, to generate investment income to supplement your checking account, for future retirement or for the kids. A specified amount of your income is placed in the 401(k) each year and not in your checking account.

2. You put your salary into the checking account to pay monthly expenditures. You supplement the checking account by depositing 401(k) investment earnings into the account and also deposit earnings from the savings account into the checking account.

3. FY08. Security and bond markets go wild and double the investment income is earned and placed into the checking account. In addition, the value of your investments in the 401(k) have gone up 30%. At this stage you might contemplate doing one of several things:

- a. You could take some of the money out of the checking account and transfer it to the savings account or to the 401(k) but also take a look at what your current financial circumstances are. Do you need to pay for a home repair, replace a car or help the kids with their college expenses? In making these choices you will look at what your financial needs are under the current conditions and make an overt fiscal choice. In the case of state funds the legislature would look at demands for appropriations and decide how much of the increased earnings to allocate for current expenditures and how much to save or set aside;
- b. You could conclude that you don't trust yourself nor your kids to make that decision every year and limit how much investment earnings from the 401(k) would remain in the checking decision. In the case of state funds the legislature has said leave a stated amount of 401(k) earnings in the checking account and place the rest in the savings account. Then the legislature has said that if the savings account exceeds a certain amount, the excess would be placed into the 401(k) account. The legislature could say these sums are to inflation proof the corpus and offset future capital losses.

4. FY09. Security and bond markets crash. 401(k) fixed income markets still produced reasonably reliable earnings which could be placed into the checking account. There has been a sizable capital loss and the value of the 401(k) has dropped substantially. At this stage you might contemplate doing one of several things:

- a. You could cut expenditures from the checking account to match the decrease in fixed income earnings and let the actual capital losses and decreases in value in the 401(k) gradually be recouped over a period of years. Your broker said that on average, the value and capital gains of your 401(k) should increase 7% each year based on your investments. You do not want to take money out of your checking or savings account to replace the capital losses which occurred in your 401(k). To further address any concerns about the effects of inflation, in the future keep all capital gains in the 401(k) and allow those inputs to accumulate, offset prior capital losses and on average provide additional monies to meet the effects of inflation whatever they may turn out to be each year;
- b. You could conclude that income from the 401(k) should include both interest and capital gains and losses such that the amount deposited to your checking account will be about 5% of what it was the year before. Thus, you might decide to put only the net investment income into the checking account and transfer money from the savings account to the checking account to make up the additional shortfall which would also result in the capital losses in the 401(k) being made up this year. In this case most of your savings account will be depleted. If additional short fall years occur, and this decision is made, each year may require an increasing amount of your income, or in the case of the legislature, additional appropriations to continue replacing capital losses.