

IRAs Have Greater Protection.

By Laif Meidell – American Retirement Planners

www.FinancialHealth.com

Published August of 2005, in the Nevada Business Journal. <http://www.nbj.com/issue/0805/9/943>

Richard and Betty Jo Rousey of Berryville, Arkansas probably share a lot in common with many couples who have relocated to Nevada over the past years. Both worked for a large company in another state before relocating to their current home. When Richard and Betty Jo left Los Angeles and the large defense contractor to whom they were employed, they were required to take a lump sum distribution of their \$55,000 company sponsored 401(k) plans and roll it over into two IRAs.

A few years later in 2001, Richard and Betty Jo filed for Chapter 7 bankruptcy protection. At this time a court-appointed trustee, Jill R. Jacoway, was assigned to supervise the sale of any assets not exempt under the bankruptcy statute and distribute the proceeds to creditors. According to U.S.C. § 522(d)(10)(E), a debtor may exclude from the bankruptcy estate (1) the right to receive payment from a stock bonus, pension, profit-sharing, annuity, or similar plan or contract if (2) the right to receive the payment is on account of illness, disability, death, age, or length of service.

The Rouseys wished to keep their IRA assets from the bankruptcy estate and believed they met the requirements for § 522(d)(10)(E). The bankruptcy court ruled against them along with two courts of appeal, on the basis that IRAs cannot be considered a “similar plan” because unlike others, the holder has unlimited access to the IRA funds. So they took their case to the Supreme Court who disagreed with the lower courts and overturned their ruling. The Supreme Court stated that there are many similarities and just as many differences between the types of accounts listed. However, the only relevant similarity shared by a stock bonus, a pension, a profit-sharing plan, and an annuity is that they constitute “income that substitutes for wages” and if an IRA shares the same similarity, then it must constitute a “similar plan” under § 522(d)(10)(E). Supreme Court Justice Thomas also concluded that IRAs are (1) meant to be used after a specific age, (2) meant to substitute for wages, and (3) impose real, deterring penalties.

Shortly after the Supreme Court ruling in *Rousey v. Jacoway* on April 4th, President Bush signed into law the Bankruptcy Abuse Protection Act of 2005. The main goal of this law was to stop abuses in the bankruptcy system, but it provided other benefits that were not as well publicized, namely the protection to more types of retirement accounts. In addition to providing protection to IRAs and Roth IRAs, the Act includes retirement assets held in a fund or account that is exempt from taxation under section 401, 403, 408, 414, 457, or 501(a) of the internal revenue code of 1986. It should be noted that IRAs and Roth IRAs are only exempt from creditors up to \$1 million (adjusted for inflation), but this \$1 million does not include rollovers to IRAs from other retirement plans. One hundred percent of rollovers to IRAs from retirement plans plus their earnings are protected.

The new bankruptcy law also provides protection to the business owner. Previously, the business owner could not exclude his retirement plan from bankruptcy if the plan did not include someone other than the employer’s spouse, a partner or a partner’s spouse. Under the Act, the plan simply has to be exempt from taxation.

Now IRAs and Roth IRAs share the same protection from bankruptcy under Federal law that was once only available to qualified retirement plans. This should result in the average American placing a higher priority on making their annual IRA contributions each year. The U.S. personal savings rate hit the lowest level in history last month with the exception of a single negative reading following 9/11. Hopefully, as Americans, we can take some comfort in knowing that our IRA and Roth IRA dollars will be protected for retirement, and turn our current savings rate trend upwards.

Sources: Investment News, AssetProtectionCorp.com, Taxes – The Tax Magazine, Hussman.com

Additional disclaimer: This article was written to provide general information about the Bankruptcy Abuse Protection Act of 2005. This article, however, should not be construed as legal advice. We recommend that you consult a lawyer if you want professional advice regarding this law, your interpretation of it, and whether it is appropriate to your particular situation.