

Inherited IRAs and Bankruptcy

CLARK v. RAMEKER

http://www.supremecourt.gov/opinions/13pdf/13-299_6k4c.pdf

A unanimous Supreme Court decision dated June 12, 2014.

Inherited IRA accounts are not retirement accounts and thus aren't exempt under §522(b)(3)(C) or (d)(12).

Background:

Even if assets are part of the bankruptcy estate, they can be exempted from the estate.

Exemptions are generally under 522 of the bankruptcy code.

Under §522, debtors may elect to claim exemptions either under federal law, see §522(b)(2), or state law, see §522(b)(3)..

522(b)(3)(C), allows debtors who choose to use the state exemptions to also use federal exemptions for retirement plans.

In order to qualify for bankruptcy protection under §522(b)(3)(C), funds must be both "retirement funds" and in an account exempt from taxation under one of the enumerated Tax Code sections.

The question before the court, "are inherited IRAs retirement plans?"

A number of early cases said, no, inherited IRAs not retirement funds,

Starting in 2012 the tide turned and most courts found they were exempt, for the 9th circuit key case was Mullen v. Hamamlin 465 B.R. 863. The theory was that the fund's were retirement assets at one point, just not the debtor's retirement assets.

Inherited IRA differences from regular IRAs

1. Can't make future contributions to the plan.
2. Must make distributions in 5 years and or RMDs.
3. They can be withdrawn at any time, no 10% penalty.

Looking at the above factors, the Court determined inherited IRAs are not retirement funds.

What does it mean?

People who inherit IRAs can't file bankruptcy

Query: Spouses who rollover inherited IRAs, is that a fraudulent conveyance?
Does the 10 year look back for transfers to self settled trusts or other devices apply?

Protective measures for current inherited IRAs

1. Move the money into an individual retirement annuity in those states that exempt annuities.
2. The internet says Alaska, Arizona, Florida, Idaho, Missouri, North Carolina, Ohio, and Texas have specific state statutes exempting inherited IRAs.

Protective measures for prospective inherited IRAs

1. Use an ERISA qualified plan, its not an asset of the estate under 541. Solo ks are not ERISA qualified and would fail the retirement funds test under 522.
2. Use stand alone retirement trusts. . . 541 protection, however the recent Highway Bill wants to limit inherited IRAs to 5 years.
3. Use a Charitable Remainder Trust with sprinkling provisions. 541 protection.
4. Irrevocable Life Insurance Trust. 541 protection
5. Wildcard for small inherited IRAs