

Bankruptcy Laws and IRAs

Although bankruptcy laws have tightened (October, 2005), as a result of a Supreme Court ruling earlier this year, retirement plan and IRA assets are exempt from most creditor claims. Secondly, the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 has given investors increased protection for several types of retirement plans not previously protected from bankruptcy proceedings.

IRA-holders benefit the most from the change. Since the “average worker” changes jobs five to seven times during a career, retirement plan assets usually end up being consolidated into one IRA. Investors in this category will be protected.

To be specific, the Supreme Court has ruled that IRAs used “for the benefit of the debtor and any dependent” can be protected from creditor claims. In other words, IRA funds needed to provide for the financial support of an investor in bankruptcy proceedings may now be protected.

The Bankruptcy Act, already signed by the President, extends bankruptcy protection of ERISA employment-sponsored retirement plans to other plans. The Act protects creditors for all retirement assets rolled over to IRAs for up to one million dollars (\$1,000,000.). The \$1,000,000 limit includes contributory and Roth IRA assets, even if the assets are not needed for financial support.

Educational Savings Accounts (ESAs) and 529 College Savings Plans are also protected under the Bankruptcy Act, provided that the participant made contributions at least one year prior to bankruptcy. The account beneficiary must be someone other than the person filing for bankruptcy, and contributions made between 365 and 720 days before filing are capped at \$5,000.