Inherited IRAs: Are These Assets Considered Retirement Funds?

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In a unanimous decision, the U.S. Supreme Court ruled that inherited IRAs are not considered retirement funds and therefore are not protected in bankruptcy. The assets held in a traditional IRA account are considered to be safe in bankruptcy since the system is designed to ensure that these funds are available during retirement.

In the case *Clark v. Rameker*, the taxpayers filed for Chapter 7 bankruptcy with the intention of excluding approximately $300,000 of an inherited IRA because they felt that the money should be classified as retirement funds. The Supreme Court ruled otherwise saying that the funds in the inherited IRA do not receive the same treatment as traditional or Roth IRAs. Three characteristics of inherited IRAs were used to determine the decision. First, inherited IRA owners are not permitted to make additional contributions to the account. Second, owners of the inherited IRA are required to take distributions from the account regardless of their age. Third, owners are not subject to any age related penalties for early withdrawal of the funds from the inherited IRA. These characteristics are unlike the guidelines that must be followed for owners of traditional or Roth IRA accounts.

This decision by the U.S. Supreme Court allows debtors to protect their retirement assets and also allows creditors to collect on assets that are not considered to be retirement funds, such as inherited IRAs. Allowing debtors to treat their inherited IRAs as retirement funds would allow them to use those funds for current consumption after the bankruptcy proceedings have ended. This counteracts the purpose of the rule for excluding retirement funds from bankruptcy proceedings.