

## HOUSE OF REPRESENTATIVES STAFF ANALYSIS

**BILL #:** HB 469 Individual Retirement Accounts

**SPONSOR(S):** Stargel and others

**TIED BILLS:** None **IDEN./SIM. BILLS:** SB 978

REFERENCE	ACTION	ANALYST	STAFF DIRECTOR or BUDGET/POLICY CHIEF
1) Civil Justice Subcommittee	15 Y, 0 N	Woodburn	Bond
2) Insurance & Banking Subcommittee	13 Y, 0 N	Philpot	Cooper
3) Judiciary Committee	16 Y, 0 N	Woodburn	Havlicak

### SUMMARY ANALYSIS

An Individual Retirement Account (IRA) is a form of retirement savings account that provides tax benefits to the owner of the account. The account is primarily used as a means of saving for retirement. When the owner of an IRA account dies the account may be transferred to a named beneficiary. When transferred to a beneficiary it is known as an Inherited IRA.

Florida law provides for protection of various assets from creditors, which protection also extends to bankruptcy proceedings. Under current Florida law, a regular IRA is exempt from creditor claims whereas an Inherited IRA is not.

The bill provides that an Inherited IRA retains the same protection from creditors that the original IRA enjoyed.

The bill takes effect upon becoming law and applies retroactively.

The bill does not appear to have a fiscal impact on state or local government.

## FULL ANALYSIS

### I. SUBSTANTIVE ANALYSIS

#### A. EFFECT OF PROPOSED CHANGES:

##### Introduction

In *Robertson v. Deeb*, the Florida 2nd District Court of Appeal held that s. 222.21(2)(a), F.S., does not exempt Inherited Individual Retirement Accounts (IRA) from creditor judgments.<sup>1</sup> The court reasoned that the statute only protects the original IRA and when the IRA is transferred to the beneficiary, the account loses its tax status and thus is no longer exempt under the statutory scheme. The decision was further applied in *In Re: Ard* by the Federal Bankruptcy Court for the Middle District of Florida allowing a trustee to include the debtors' inherited IRA in the bankruptcy estate.<sup>2</sup> The two decisions allow a creditor to garnish an Inherited IRA to satisfy a judgment and also prevent the Inherited IRA from being exempted during bankruptcy proceedings. The bill provides that the exemption from creditors that applies in s. 222.21(2)(a), F.S., for the original owner of an IRA will continue to apply after the IRA has been passed to the beneficiary.

##### Individual Retirement Account

An Individual Retirement Arrangement is a tax deferred or tax advantage retirement savings plan.<sup>3</sup> The IRA is a form of retirement savings account that is established in accordance with I.R.C. §408 or §408A.<sup>4</sup> An IRA is defined as, "...a trust created or organized in the United States for the exclusive benefit of an individual or his beneficiaries,"<sup>5</sup> and must also meet the following criteria:

- The trustee or custodian must be a bank, a federally insured credit union, a savings and loan association, or an entity approved by the IRS to act as trustee or custodian.
- The trustee or custodian generally cannot accept contributions of more than the deductible amount for the year. However, rollover contributions and employer contributions to a simplified employee pension can be more than this amount.
- Contributions, except rollover contributions, must be in cash.
- The owner must have a non-forfeitable right to the amount at all times.
- Money in the account cannot be used to buy a life insurance policy.
- Assets in the account cannot be combined with other property, except in a common trust fund or common investment fund.
- The owner must start receiving distributions at the age of 70 1/2 years.<sup>6</sup>

There are different types of IRA's, including the traditional IRA and the Roth IRA. The traditional IRA allows the owner of the account to make tax deductible contributions to the account and defer paying taxes on the income until withdrawals are made from the IRA after retirement.<sup>7</sup> The Roth IRA<sup>8</sup> allows an owner of the account to make non-tax deductible contributions into the account and make tax free withdrawals from the account upon retirement.<sup>9</sup>

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<sup>1</sup> *Robertson v. Deeb*, 16 So.3d 936 (Fla. 2d DCA 2009).

<sup>2</sup> *In re: Ard*, 435 B.R. 719 (Bkrcty. M.D. Fla. 2010).

<sup>3</sup> See Internal Revenue Publication, *Publication 590, Individual Retirement Arrangements (IRA)* at 3 (2010).

<sup>4</sup> Lynch and Griffin, "The *Robertson* Case: A Beneficiary by Any Other Name is Still a Beneficiary," *The Florida Bar Journal*, April 2010, Vol. 84, No.4.

<sup>5</sup> 26 U.S.C. §408(a).

<sup>6</sup> *IRS Publication 590* at 9.

<sup>7</sup> *Id.* at 7.

<sup>8</sup> A Roth IRA also differs from a traditional IRA in that the owner can open one at any age and does not have to take deductions at age 70 1/2.

<sup>9</sup> *IRS Publication 590* at 57.

IRAs have become increasingly important since their creation in 1974.<sup>10</sup> At the end of 2009, IRAs held \$4.3 trillion, or more than one quarter of the \$16.1 trillion in estimated total U.S. retirement assets and make up almost ten percent of U.S. households' total assets.<sup>11</sup> It is estimated that 41.4 percent of U.S. households owned one or more types of IRAs.<sup>12</sup>

When the owner of an IRA dies, the IRA may be left to a named beneficiary.<sup>13</sup> If the beneficiary is someone other than the owner's spouse,<sup>14</sup> the IRA is considered an Inherited IRA.<sup>15</sup> The beneficiary has two options when inheriting an IRA:

1. The beneficiary must withdraw all of the funds from the original IRA within five years of the original owner's death, or
2. The beneficiary must transfer the funds to an inherited IRA and take annual distributions over the remaining lifespan of the beneficiary.<sup>16</sup>

The beneficiary of an inherited IRA may not make contributions to the account, must make withdrawals regardless of his or her age and, unlike the original IRA, there is no penalty for early withdrawals from the account.

### IRA Asset Protection

A creditor can collect money owed to it by filing an action for a judgment in state court. A judgment is an order of the court creating an obligation, such as a debt. The creditor may then use that judgment to collect assets from the debtors by way of garnishment to satisfy the debt. Florida law protects various assets from creditor garnishments including retirement accounts. Individual Retirement Accounts are afforded such protection in s. 222.21(2)(a)1. and 2., F.S., which provides that:

Except as provided in paragraph (d), any money or other assets payable to an owner, a participant, or a beneficiary from, or any interest of any owner, participant, or beneficiary in, a fund or account is exempt from all claims of creditors of the owner, beneficiary, or participant if the fund or account is:

1. Maintained in accordance with a master plan, volume submitter plan, prototype plan, or any other plan or governing instrument that has been preapproved by the Internal Revenue Service as exempt from taxation under s. 401(a), s. 403(a), s. 403(b), s. 408, s. 408A, s. 409, s. 414, s. 457(b), or s. 501(a) of the Internal Revenue Code of 1986, as amended, unless it has been subsequently determined that the plan or governing instrument is not exempt from taxation in a proceeding that has become final and nonappealable;
2. Maintained in accordance with a plan or governing instrument that has been determined by the Internal Revenue Service to be exempt from taxation under s. 401(a), s. 403(a), s. 403(b), s. 408, s. 408A, s. 409, s. 414, s. 457(b), or s. 501(a) of the Internal Revenue Code of 1986, as amended, unless it has been subsequently determined that the plan or governing instrument is not exempt from taxation in a proceeding that has become final and nonappealable;

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<sup>10</sup> The IRA was created by the passage of the Employee Retirement and Security Act (ERISA) in 1974.

<sup>11</sup> *The IRA Investor Profile: Traditional IRA Investors' Rollover Activity, 2007 and 2008*. ICI Investment Company Institute [www.ici.org](http://www.ici.org). Last visited February 17, 2011.

<sup>12</sup> *Id.* at 3.

<sup>13</sup> 26 U.S.C. §408(d)(3)(C)(ii).

<sup>14</sup> An IRA inherited by a spouse is not considered an inherited IRA and is treated the same as the original account.

<sup>15</sup> 26 U.S.C. §408(d)(3)(C)(ii).

<sup>16</sup> 26 U.S.C. §401(a)(9).

The application of s. 222.21(2)(a), F.S., protects an owner's IRA from a creditor so long as the IRA follows IRS guidelines and retains its tax exempt status. Section 222.21(2)(a), F.S., applies to creditors in state court and in federal bankruptcy court.<sup>17</sup>

The 2nd DCA recently declined to extend the protection in s. 222.21(2)(a), F.S., to inherited IRAs in *Robertson v. Deeb*.<sup>18</sup>

### Robertson v. Deeb & In Re: Ard

In *Robertson*, a creditor had obtained a judgment against Robertson and served a writ of garnishment on the trustee of Robertson's Inherited IRA. Robertson had been named beneficiary of his late father's IRA and upon his father's death, was given the option of keeping the IRA in his father's name and withdrawing all the proceeds from the IRA over the next five years or transferring the IRA into an Inherited IRA and take annual withdrawals from the account for the remainder of his life expectancy. Robertson chose the latter. Robertson claimed that his beneficial interest in the IRA was exempt from garnishment pursuant to s. 222.21(2)(a), F.S., "because he is a 'beneficiary' of the 'fund or account' that qualified as an IRA when his father was alive."<sup>19</sup> The court ruled that section 222.21(2)(a), F.S., does not apply to Inherited IRAs,

...because the plain language of that section references only the original 'fund or account' and the tax consequences of inherited IRAs render them completely separate funds or accounts.<sup>20</sup>

The Court reasoned that since the Inherited IRA was not the original IRA<sup>21</sup> and the tax status was different,<sup>22</sup> the exception in s. 222.21(2)(a), F.S., did not apply since the exception was conditioned on the tax status of the original account.

The decision in *Robertson* has been further applied in federal bankruptcy court in *In Re: Ard*.<sup>23</sup> In *In Re: Ard*, the debtor had an Inherited IRA similar to that in *Robertson*. The court noted the outcomes involving inherited IRAs "turned on the particular language of each state's law applicable to the exemption of IRAs."<sup>24</sup> The bankruptcy court, pursuant to the decision in *Robertson*, ruled that s. 222.21(2)(a), F.S., did not apply to an inherited IRA and thus not exempt in federal bankruptcy proceedings.<sup>25</sup> The debtor was therefore required to turn the IRA over to the bankruptcy trustee.

### Effect of Proposed Changes

The bill contains "whereas" clauses to express the Legislature's intent that Inherited IRAs, as defined in s. 402(c) of the Internal Revenue Code, were intended to be exempt from the claims of creditors and that the decisions in *Robertson* and *In re: Ard* are contrary to the Legislature's intent.

The bill amends s. 222.21(2)(c), F.S., to provide that an IRA exempt from creditors under s. 222.21(2)(a), F.S., would continue to be exempt if the original IRA is transferred to an Inherited IRA. Under the proposed changes, when an owner of an IRA passes away, his or her named beneficiary would continue to enjoy the protection from creditors that the original owner enjoyed under s. 222.21(2)(a), F.S. This protection would most likely extend to protection in bankruptcy proceedings, as well.

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<sup>17</sup> 11 U.S.C. s. 522(b) (Federal Bankruptcy law allows a debtor to exempt certain property from bankruptcy proceedings according to state law).

<sup>18</sup> *Robertson*, at 937.

<sup>19</sup> *Id.* at 938.

<sup>20</sup> *Id.*

<sup>21</sup> The court reasoned that the IRA ceased to be the original IRA when it was passed to a beneficiary.

<sup>22</sup> The court noted that Inherited IRAs do not have a penalty for early withdrawals, distributions must be made, and Inherited IRAs are not entitled to contributions or rollovers into existing IRAs to point out the inconsistencies with the original IRA.

<sup>23</sup> *In re: Ard*, at 719.

<sup>24</sup> *Id.* at 722.

<sup>25</sup> *Id.*

The bill contains language indicating that its provisions are clarifying and apply retroactively.

The bill takes effect upon becoming a law.

**B. SECTION DIRECTORY:**

Section 1 amends s. 222.21(2)(c), F.S., relating to exemption of an IRA from claims of creditors.

Section 2 provides that the bill becomes effective upon becoming a law.

**II. FISCAL ANALYSIS & ECONOMIC IMPACT STATEMENT**

**A. FISCAL IMPACT ON STATE GOVERNMENT:**

**1. Revenues:**

None.

**2. Expenditures:**

None.

**B. FISCAL IMPACT ON LOCAL GOVERNMENTS:**

**1. Revenues:**

None.

**2. Expenditures:**

None.

**C. DIRECT ECONOMIC IMPACT ON PRIVATE SECTOR:**

None.

**D. FISCAL COMMENTS:**

None.

**III. COMMENTS**

**A. CONSTITUTIONAL ISSUES:**

**1. Applicability of Municipality/County Mandates Provision:**

This bill does not appear to require counties or municipalities to take an action requiring the expenditure of funds, reduce the authority that counties or municipalities have to raise revenue in the aggregate, nor reduce the percentage of state tax shared with counties or municipalities.

**2. Other:**

This bill provides that it is intended to be clarifying and remedial and shall apply retroactively. Retroactive application of legislation can implicate the due process provisions of the Constitution.<sup>26</sup> As a general matter, statutes which do not alter vested rights but relate only to remedies or procedure can be applied retroactively.<sup>27</sup>

<sup>26</sup> See *State Department of Transportation v. Knowles*, 402 So.2d 1155 (Fla. 1981).

<sup>27</sup> See *Metropolitan Dade County v. Chase Federal Housing Corporation*, 737 So.2d. 494 (Fla. 1999).

The Florida Supreme Court has ruled that statutes enacted soon after a controversy over the meaning of legislation may be considered a legislative interpretation of the original law and not substantive change:

When, as occurred here, an amendment to a statute is enacted soon after controversies as to the interpretation of the original act arise, a court may consider that amendment as a legislative interpretation of the original law and not as a substantive change thereof. This Court has recognized the propriety of considering subsequent legislation in arriving at the proper interpretation of the prior statute.<sup>28</sup>

**B. RULE-MAKING AUTHORITY:**

None.

**C. DRAFTING ISSUES OR OTHER COMMENTS:**

None.

**IV. AMENDMENTS/ COMMITTEE SUBSTITUTE CHANGES**

None.

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<sup>28</sup> *Lowry v. Parole and Probation Commission*, 473 So.2d 1248, 1250 (Fla. 1985)(internal citations omitted).