

Are Retirement Funds Safe From Creditors?



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The good news is that qualified retirement plans that are subject to Employee Retirement Income Security Act (ERISA) of 1974 are generally protected from creditors. These protections are referred to as the anti-alienation rules. ERISA covers most employer-sponsored retirement plans which would include 401(k)/Profit Sharing plans, pension plans and some 403(b) plans.

ERISA does however, provide for four exceptions to its anti-alienation rules. They are as follows:

1. for payments to alternate payees pursuant to qualified domestic relations orders (QDROs) in cases of divorce or legal separation;
2. for payments of IRS tax levies;
3. for payments of federal court garnishments stemming from the imposition of criminal fines and orders of restitution; and
4. to satisfy liabilities of the participant to the plan due to criminal convictions, civil judgments, or administrative settlements involving the participant's misconduct with respect to the plan.

The bad news is that not all retirement plan products receive this protection. Nonqualified plans such as executive deferred compensation plans, non-ERISA 403(b) plans and IRA (Individual Retirement Accounts) are not protected. Protection for qualified plans can be lost if the qualified plan has not received a favorable Internal Revenue Service letter of determination on which the plan can rely.

Even though IRAs aren't protected by ERISA, they do have some protection under federal bankruptcy law. Rollover from an employer plan such as a 401(k) to an IRA would be protected from creditors up to \$1million in aggregate. This protection also applies to a SEP or Simple IRA. The federal protection for IRAs is available only in a federal bankruptcy action meaning you have to file for bankruptcy to protect the IRA. Inherited IRAs do not receive any protection.

Some states have established laws to further protect IRAs and other retirement plans, such as non-ERISA 403(b)s. In fact, a number of states provide protection of IRAs from creditors for the residents of their states. In those states' IRAs receive the same protection as ERISA plans. They are protected from creditors even without the owners having to file for bankruptcy. It is important to know what the laws are for the participants particular state.

There are strategies to consider when a state's protection is nonexistent or not very strong. Participants can maximize their contributions in their 401(k) and other qualified employer retirement plans that are protected under ERISA. For terminated participants, if the plan allows, leave the funds in the qualified retirement plan for as long as possible to protect the assets.

The rules around qualified and non-qualified retirement accounts can be complicated and confusing. It is always a good idea to contact an attorney or financial planner in your state for professional guidance.



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