

Inherited IRAs Are Not Retirement Funds, Supreme Court Rules

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Funds held in inherited IRAs are not retirement funds and must be included in a bankruptcy estate, the U.S. Supreme Court ruled June 12. The Court's 9-0 ruling in [Clark v. Rameker](#) ^[1], No. 13-299 (U.S. 6/12/14), *aff'd* 714 F.3d 559 (7th Cir. 2013)) was definitive in drawing a distinction between inherited IRAs and retirement funds, and between inherited IRAs and other funds to which the Bankruptcy Code's exemptions apply. The Court's ruling ended years of ping-pong litigation in which successive courts reversed decisions by lower courts.

The facts of the case: In 2000, Ruth Heffron established an IRA, which her daughter Heidi Heffron-Clark inherited when Ruth died in 2001. In 2010 Heffron-Clark and her husband filed a bankruptcy petition. In it they claimed that the inherited IRA was exempt from inclusion in the bankruptcy estate. The bankruptcy trustee and unsecured creditors of the estate disagreed on the grounds that the funds in the inherited IRA were not retirement funds.

The Bankruptcy Court agreed with the bankruptcy trustee and the creditors in its 2011 ruling. In 2012 the U.S. District Court for the Western District of Wisconsin reversed the Bankruptcy Court's decision, ruling that the exemption covers any account containing funds originally accumulated for retirement. In 2013, the 7th U.S. Circuit Court of Appeals reversed the District Court's ruling, holding that there is a difference between IRAs that are inherited and those that are not. Now the U.S. Supreme Court has upheld the 7th Circuit's ruling, settling the matter.

Justice Sonia Sotomayor, who wrote the opinion, said that the Bankruptcy Code makes it clear that inherited IRAs are not retirement funds to which the bankruptcy exemption applies. She pointed to three legal characteristics of inherited IRAs that led the Court to conclude that funds in them are not set aside for retirement:

1. the holder of an inherited IRA may never invest additional money in the account;
2. holders of inherited IRAs must withdraw money from them, regardless of how many years they are from retirement; and
3. the holder of an inherited IRA may withdraw the entire balance at any time, for any purpose, with no penalty — but that is not the case for traditional or Roth IRAs.

Sotomayor went on to say that to treat inherited IRAs the same as those intended for retirement would allow the holder of an inherited IRA to withdraw any or all of the funds for any purchase he or she wishes, while the Bankruptcy Code is intended to preserve debtors' ability to meet their basic needs and make a "fresh start." Sotomayor added that the possibility that an account holder could leave an inherited IRA intact until retirement and take only required minimum distributions does not mean that the inherited IRA therefore has the legal characteristics of a retirement fund.

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[1] Clark v. Rameker: http://www.supremecourt.gov/opinions/13pdf/13-299_6k4c.pdf