



**House
Legislative
Analysis
Section**

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BANKRUPTCY: RETIREMENT PLANS

House Bill 4010 as enrolled
Second Analysis (6-30-89)

Sponsor: Rep. Michael J. Griffin
House Committee: Judiciary
Senate Committee: Judiciary

THE APPARENT PROBLEM:

The Revised Judicature Act exempts various sorts of property from levy and sale to enforce a judgement such as a child support order or a judgement rendered in bankruptcy proceedings. While individual retirement accounts (IRAs) are protected from bankruptcy proceedings, other forms of retirement plans are not. This means that a person who declares bankruptcy can lose what has been put aside for old age, and his or her family can also suffer the loss of that retirement income. The problem appears especially acute for professionals vulnerable to large malpractice awards that can force them into bankruptcy. The Michigan State Medical Society and others urge that Michigan law be amended to protect retirement plans from bankruptcy proceedings.

THE CONTENT OF THE BILL:

The bill would amend the Revised Judicature Act to protect certain retirement plans from bankruptcy proceedings. The exemption would apply to the operation of the federal bankruptcy code and would cover a person's interest in a pension, profit-sharing, annuity, or other retirement plan protected by the federal Employee Retirement Income Security Act (ERISA). The exemption would not apply to contributions made within 120 days before the debtor filed for bankruptcy, nor would it apply in the execution of court orders for divorce or child support.

The same restrictions would apply to the existing exemption for individual retirement accounts. In addition, the bill would protect amounts deposited in an IRA which were "rollovers" from the other retirement plans protected by the bill. (Ordinarily, IRA contributions in a given year in excess of the amount for which one can claim an income tax deduction are not protected from levy and sale to enforce a judgement.)

MCL 600.6203

FISCAL IMPLICATIONS:

The House Fiscal Agency reports that the bill has no fiscal implications. (2-22-89)

ARGUMENTS:

For:

The bill is a humane measure that would allow hard-earned retirement assets to be preserved when a debtor goes through bankruptcy. Undue hardship for the debtor and his or her family would thus be avoided. Such protection is especially important for medical professionals whose vulnerability to exorbitant malpractice judgements leaves them exposed to the loss of their retirement funds. Some may fear that the bill would allow a malpracticing

professional to shelter and have access to huge sums of money, but that is not the case: by limiting its application to certain federally-qualified retirement plans, the bill ensures that federal limits on contributions and benefit payments also apply.

Against:

The bill threatens to leave injured parties without means to collect well-deserved malpractice awards. Even with federal limitations, it is possible for contributions to certain retirement plans to total tens of thousands of dollars per year and still qualify. Moreover, as Michigan law protects jointly-held real property, whatever money that is not placed into the protection of a retirement plan could be invested in real estate, leaving virtually no assets to satisfy a judgement. In essence, the bill offers shrewd professionals the opportunity to forego malpractice insurance by shielding their money in retirement accounts.

Against:

It appears that the bill could actually decrease protection of IRA contributions. Since the IRA exemption in state law was enacted prior to the 1986 federal tax reforms, contributions up to the deductible amount allowed under the Internal Revenue Code in 1984 (when the IRA exemption was enacted in Michigan law) are exempt from an execution. If the IRA exemption provision of the Revised Judicature Act were amended, however, the exemption would apply only up to the amount that the contributor could deduct at the time of amendment. (Generally, under the 1986 federal tax reforms, IRA contributions are deductible only for those contributors who are not covered by another qualified retirement plan.) In addition, the bill would exempt from execution rollovers to IRAs from other protected plans, but would not address rollovers from other IRAs. Reportedly, courts are treating IRA-to-IRA rollovers as exempt now, but would not necessarily continue to do so if the bill were enacted.

Further, the bill need not specify that its proposed exemptions for retirement plan assets would apply to the Federal Bankruptcy Code. Simply listing the retirement plan assets would make those assets exempt "from levy and sale under any execution." Referring to the bankruptcy code only in the IRA and retirement assets exemptions could lead courts to believe that the judicature act's other exemptions did not apply to bankruptcy proceedings.