



Romney Building, 10th Floor
Lansing, Michigan 48909
Phone: 517/373-6466

ROTH INDIVIDUAL RETIREMENT ACCOUNT PROTECTION

House Bill 5612 as introduced
Sponsor: Rep. Samuel Buzz Thomas

Senate Bill 856 as passed by the Senate
Sponsor: Sen. Kenneth DeBeaussiaert

First Analysis (3-12-98)
Committee: Commerce

THE APPARENT PROBLEM:

The federal Taxpayer Relief Act of 1997 created a new kind of individual retirement account (IRA), called the Roth IRA, which first became available to contributors on January 1, 1998.

A worker with earnings can start a Roth IRA by depositing \$2,000 a year (\$4,000 for a married couple). A taxpayer qualifies for the full contribution amount if single with an adjusted gross income up to \$95,000, or married with income up to \$150,000. A depositor does not get a tax deduction for the money put in, but the earnings that accumulate can be taken tax free, as long as the account is held for at least five years, and the depositor is at least 59½ years old, or disabled, or taking up to \$10,000 in earnings to buy a first home.

Generally, with a regular IRA, a depositor's money is tax-deferred but not tax-free; depositors pay taxes with they withdraw their money. Because of the tax advantages, people with regular IRAs have been encouraged to consider conversions to the new Roth IRAs. A depositor can qualify for a conversion if his or her adjusted gross income is \$100,000 or less, married or single.

According to financial planners, a roll-over to a Roth IRA is not tax free, since the money converted must be reported as taxable income. However, if a depositor switches to a Roth IRA in 1998, he or she can spread the income and the tax over four years. For a conversion after 1998, all the tax would be due at once.

One disadvantage to the Roth IRA (both for those who start anew, and for those who convert a regular IRA), is that many states have not changed their statutes to protect the Roth IRA from creditors when court judgments are executed. In contrast, a regular IRA is protected from creditors after a declaration of bankruptcy. Some argue that a regular IRA and the new Roth IRA should be similarly regarded in the event of bankruptcy.

THE CONTENT OF THE BILLS:

House Bill 5612 and Senate Bill 856 are identical. The bills would amend those provisions of the Revised Judicature Act that list the kinds of property that are protected from creditors in the execution of any judgment. Specifically, with regard to individual retirement accounts, the bills would expand the definition of IRA by referring to two sections of the Internal Revenue Code, rather than one. Under the bill, the protected accounts (that is to say, those exempt from levy and sale under any execution) would include "an individual retirement account or individual retirement annuity as defined in either section 408 or 408a of the Internal Revenue Code of 1986." Currently, the law makes reference only to "section 408 of the Internal Revenue Code." Under the bill, references to the Internal Revenue Code would be changed to read "the Internal Revenue Code of 1986." (Section 408a of the Internal Revenue Code was added as part of the Taxpayer Relief Act of 1997, and provides for a new type of individual retirement account, known as the "Roth IRA".)

MCL 600.6023

House Bill 5612 and Senate Bill 856 (3-12-98)

FISCAL IMPLICATIONS:

According to the Senate Fiscal Agency, the bill would have no fiscal impact on state or local government. (2-23-98)

ARGUMENTS:

For:

Under the Revised Judicature Act certain types of properties are protected against court-ordered judgments to collect assets, including qualified pension plans and IRAs. Since the federal Taxpayers Relief Act of 1997 now allows persons to deposit funds in a new type of IRA, the Roth IRA, simple fairness requires that the protection against judgments also be extended to the Roth IRA.

Against:

This legislation seems to reward personal bankruptcy. The number of personal bankruptcies reached a record high last year in the United States.

POSITIONS:

There are no positions on the bills.

Analyst: J. Hunault

■This analysis was prepared by nonpartisan House staff for use by House members in their deliberations, and does not constitute an official statement of legislative intent.