

HOUSE OF REPRESENTATIVES STAFF ANALYSIS

BILL #: HB 253 Transfers in Divorce
SPONSOR(S): Geller and others
TIED BILLS: **IDEN./SIM. BILLS:** SB 702

REFERENCE	ACTION	ANALYST	STAFF DIRECTOR or BUDGET/POLICY CHIEF
1) Civil Justice & Property Rights Subcommittee		Mathews	Jones
2) Insurance & Banking Subcommittee			
3) Judiciary Committee			

SUMMARY ANALYSIS

An Individual Retirement Account (IRA) is a retirement savings account that provides the account owner with certain tax benefits which are not available for a traditional savings account. An IRA may be a traditional IRA or a Roth IRA.

An IRA is intended to be the property of its owner and may only be transferred to another person upon the owner's death or in a dissolution of marriage. When an IRA account owner dies, the account may be transferred to a named beneficiary, and if the beneficiary is not the account owner's spouse, the IRA is considered an inherited IRA. If an IRA is transferred to a spouse or ex-spouse incident to a divorce, the spouse receiving the IRA becomes the new owner of the interest in the assets in the other spouse's IRA on the effective date of the transfer. The assets in an IRA may be transferred in a divorce by:

- Name change, where transfer is executed by changing the name of the IRA owner from that of one spouse or former spouse to that of the other; or
- Direct transfer, where the assets in one spouse's IRA are directly transferred or rolled over to a new or existing IRA of the other spouse.

Under the Internal Revenue Code (IRC), a state may specify assets which are exempt from creditor claims in a bankruptcy proceeding and may choose to provide greater protection against such claims than the IRC. Florida generally adopts the federal exemptions for an IRA and certain pension, profit sharing, and retirement benefits like 401(k) accounts. While Florida adopts the general IRC exemption for an IRA, which includes the transfer incident to a divorce, Florida includes a specified additional exemption for an inherited IRA which the IRC does not. Although there is no current controversy in Florida regarding the exemption for an IRA account awarded incident to a divorce, recent bankruptcy court decisions from other jurisdictions may indicate the need to clarify Florida's exemption.

Section 222.21(2)(d), F.S., clearly exempts interests in a retirement plan subject to the Employee Retirement Income Security Act (ERISA), such as a 401(k) plan received by an ex-spouse incident to divorce through a Qualified Domestic Relations Order (QDRO). The exemption language is less precise, however, as to whether an ex-spouse's interest in an IRA received in a transfer incident to divorce is exempt from the claims of the non-participant spouse.

HB 253 clarifies that any interest in an IRA received during a transfer incident to divorce remains exempt from creditor claims after the transfer is complete. The bill applies retroactively to all transfers made incident to divorce.

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

The bill provides an effective date of upon becoming law.

FULL ANALYSIS

I. SUBSTANTIVE ANALYSIS

A. EFFECT OF PROPOSED CHANGES:

Background

The Employee Retirement Income Security Act (ERISA)

ERISA is a federal law that sets minimum standards for most voluntarily established retirement plans in the private industry to provide protection for individuals in those plans.¹ ERISA identifies requirements for plans for the protection of plan participants.

401(k) Plan

A 401(k) plan is a feature of a qualified profit-sharing plan that allows employees to contribute a portion of their wages to individual accounts.² An employee's elective contributions are excluded from the employee's taxable income; however, distributions, including earnings, are considered taxable income at retirement.

Individual Retirement Accounts

An Individual Retirement Account (IRA) is "...a trust created or organized in the United States for the exclusive benefit of an individual or his beneficiaries."³ An IRA is created by a written document which shows that the account meets the following criteria:⁴

- The account's trustee or custodian must be a bank, federally insured credit union, savings and loan association, or other entity approved by the Internal Revenue Service (IRS) to act as such.
- The trustee or custodian generally may not accept contributions in an amount more than the account's deductible amount for the year, but rollover contributions and employer contributions to a simplified employee pension (SEP)⁵ can be more than this amount.
- Contributions, except for rollover contributions, must be in cash.
- The account owner must have a non-forfeitable right to the amount in the account 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 account owner must begin receiving distributions from the account in April of the year after he or she reaches age 70 1/2.

An IRA may be a traditional IRA or a Roth IRA. While a traditional IRA allows an account owner to make tax deductible contributions into the account and defer being taxed on the income until making withdrawals after retirement,⁶ a Roth IRA allows an account owner to make non-tax-deductible contributions into the account and make tax-free withdrawals after retirement.⁷

An IRA is intended to be the property of its owner and may only be transferred to another person upon the owner's death or in a dissolution of marriage proceeding. When an IRA account owner dies, the account may be transferred to a named beneficiary.

¹ U.S. Department of Labor, Employee Retirement Income Security Act (ERISA), <https://www.dol.gov/general/topic/retirement/erisa> (last visited Mar. 27, 2021).

² Internal Revenue Service, 401(k) Plans, (Sep. 23, 2020), <https://www.irs.gov/retirement-plans/401k-plans> (last visited Mar. 27, 2021).

³ 26 U.S.C. § 408(a).

⁴ IRS Publication 590-A, *Contributions to Individual Retirement Arrangements (IRAs)*, (Feb. 24, 2020), <https://www.irs.gov/publications/p590a> (last visited Mar. 27, 2021).

⁵ An SEP is a written arrangement that allows your employer to make deductible contributions to a traditional IRA (an SEP IRA) set up for the account owner to receive such contributions. Generally, distributions from SEP IRAs are subject to the withdrawal and tax rules that apply to traditional IRAs *Id.*

⁶ *Id.*

⁷ *Id.*

If the beneficiary is not the account owner's spouse, the IRA is considered an inherited IRA.⁸ The beneficiary of an inherited IRA:

- May not make contributions to the account;
- Must make withdrawals regardless of his or her age; and
- Is not subject to a penalty for early withdrawals from the account.

If the beneficiary is the account owner's spouse, the beneficiary may do one of the following:⁹

- Treat the IRA as his or her own IRA by designating himself or herself as the account owner;
- Treat the IRA as his or her own by rolling it over into his or her own IRA, or to the extent it is taxable, into a:
 - Qualified employer plan;
 - Qualified employee annuity plan (section 403(a) plan);
 - Tax-sheltered annuity plan (section 403(b) plan); or
 - State or local government deferred compensation plan (section 457 plan).
- Treat himself or herself as the beneficiary of the IRA.

When an IRA is transferred to a spouse or ex-spouse incident to a divorce, the spouse receiving the IRA becomes the new owner of the assets in the other spouse's IRA on the effective date of the transfer. There is no legal authority for an IRA to be split or transferred until the divorce is finalized, and a court order is entered directing how the account must be split. The parties must give the IRA custodian a copy of the court's order, and the custodian may then split the account or transfer the account accordingly, in a tax-free transfer. The assets in an IRA may be transferred by:

- Changing the name of the IRA owner from that of one spouse or former spouse to that of the other; or
- Making a direct transfer of the IRA assets or a portion of the assets from one spouse's IRA directly into the other spouse's new or existing IRA.

IRA Asset Protection

Although established under the federal tax code, a state's laws may affect an IRA in a case involving a trust, real estate, or a bankruptcy exemption that protects the IRA from the claims of creditors. A person may file for bankruptcy to assist in discharging debt or making a plan to repay debts. All bankruptcy cases are handled in federal courts under rules outlined in the U.S. Bankruptcy Code (Code).¹⁰ In general, filing for bankruptcy serves two purposes: to convert the estate of the debtor into cash and distribute it among creditors; and to give the debtor a fresh start by providing certain exemptions and rights to assets that bankruptcy does not reach.¹¹ A person may file one of two primary forms of bankruptcy.¹² In a proceeding under Chapter 7 of the Code, a debtor must surrender his or her assets to a trustee who then liquidates the assets and distributes all proceeds to the debtor's creditors.¹³ A Chapter 13 bankruptcy petition allows a debtor to stay creditor actions and propose a plan to pay all creditors, thus rehabilitating the debtor financially.¹⁴

In either a Chapter 7 or Chapter 13 bankruptcy, a debtor may claim certain property as exempt from creditors in the bankruptcy proceedings.¹⁵ The Code provides many exemptions to protect certain assets from creditors' claims, but under the Code, a state may choose to opt out of these exemptions.¹⁶ If a state chooses to opt out, the federal Code exemptions are not available to debtors within that state, unless the state specifically opts in to a Code exemption within state law. A state may also provide greater asset protections than the Code.

⁸ 26 U.S.C. §401(a)(9).

⁹ IRS, *supra* note 2, at 20.

¹⁰ 11 U.S.C. § 101, et seq.

¹¹ 9 Am. Jur. 2d Bankruptcy s. 5.

¹² An individual may also file a petition under Chapter 11, but such petitions are rare.

¹³ 11 U.S.C. §§ 704 & 726.

¹⁴ 9 Am Jur 2d Bankruptcy s. 72.

¹⁵ 11.U.S.C. § 522.

¹⁶ 11.U.S.C. §§ 522(b)(3)(A) & (d).

Florida is an opt-out state, meaning that when a Florida resident files for bankruptcy or is otherwise subject to a creditor's judgment, Florida law, rather than the federal Code, provides the exemptions available to the debtor.¹⁷ Florida law provides a number of exemptions for various retirement-related assets, such as IRAs and other pension, profit-sharing, and retirement benefits.¹⁸ Florida also exempts all inherited IRA accounts from creditors' claims, while the Code does not.¹⁹

Transfers Incident to Divorce

Florida provides a bankruptcy exemption for IRA accounts that are exempt from taxation under s. 408 of the Internal Revenue Code (IRC),²⁰ and the IRC tax exemption for an IRA account awarded incident to a divorce provides tax-exempt status for a former spouse's interest in such an account at the time the transfer is made, and thereafter.²¹

Although there is no current controversy in Florida regarding the exemption for an IRA account awarded incident to a divorce, recent bankruptcy court decisions from other jurisdictions may indicate the need to clarify Florida's exemption. In a 2018 opinion, the U.S. Bankruptcy Appellate Court for the Eighth Circuit held that a debtor's funds must satisfy two requirements to be considered exempt retirement funds under the bankruptcy exemption in 11 U.S.C. § 522(d)(12):

- The amount must be retirement funds; and
- The retirement funds must be in an account that is exempt from taxation under one of the provisions of the IRC.²²

The Court found that the funds in an IRA account awarded to a transferee spouse incident to his divorce years before he filed for chapter 7 bankruptcy, but which he never transferred from his former wife's IRA account or designated himself as the owner of, were not retirement funds for purposes of a bankruptcy exemption.²³ As such, these funds were subject to creditors' claims.

Effect of Proposed Changes

HB 253 clarifies that any interest in an IRA awarded or received in a transfer incident to divorce is exempt from creditors upon being awarded or received and remains exempt from creditors' claims after the transfer is complete. The bill applies retroactively to all transfers made incident to divorce.

The bill provides an effective date of upon becoming law.

B. SECTION DIRECTORY:

Section 1: Amends s. 222.21, F.S., relating to exemption of pension money and certain tax-exempt funds or accounts from legal processes.

Section 2: Provides an effective date of upon becoming a law.

II. FISCAL ANALYSIS & ECONOMIC IMPACT STATEMENT

A. FISCAL IMPACT ON STATE GOVERNMENT:

1. Revenues:

None.

¹⁷ S. 222.20, F.S.

¹⁸ S. 222.21(2), F.S.

¹⁹ S. 222.21(c), F.S.

²⁰ S. 222.21(2), F.S.

²¹ 28 U.S.C. § 408(d)(6).

²² *In re Lerbakken*, 590 B.R. 895 (2018). See also *Clark v. Rameker*, 573 U.S. 122 (2014).

²³ *Lerbakken* at 897, 898.

2. Expenditures:

None.

B. FISCAL IMPACT ON LOCAL GOVERNMENTS:

1. Revenues:

None.

2. Expenditures:

None.

C. DIRECT ECONOMIC IMPACT ON PRIVATE SECTOR:

The bill may make it more difficult for creditors to access certain interests in IRAs transferred pursuant to dissolution of marriage actions.

D. FISCAL COMMENTS:

None.

III. COMMENTS

A. CONSTITUTIONAL ISSUES:

1. Applicability of Municipality/County Mandates Provision:

Not applicable. The bill does not appear to affect county or municipal governments.

2. Other:

None.

B. RULE-MAKING AUTHORITY:

Not applicable.

C. DRAFTING ISSUES OR OTHER COMMENTS:

None.

IV. AMENDMENTS/ COMMITTEE SUBSTITUTE CHANGES