

Bankruptcy in Retirement –Protecting Your 401(k), IRA, and Pension

By Arizona Bankruptcy Attorney John Skiba

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People needing to file bankruptcy after retirement happens more often than one might think. Often one of the causes leading to the bankruptcy is not only the retired person's financial situation but the financial difficulties of their grown children. It is natural that we want to help our family members out when they are going through difficult times, however when the person offering the help is on a fixed or limited budget it can have serious repercussions.

When there isn't sufficient income to help a family member and cover the basic living expenses people often resort to credit cards, which quickly pile up to the point where the minimum payment can no longer be made. The next step is often bankruptcy.

A second scenario I see is with those people who are not in retirement, and may not even be close, but who have saved and set aside money in an IRA account, 401(k), or other retirement account and then are drawing down those accounts to cover their credit card payments.

In both of the above situations it is important to understand what accounts are protected in bankruptcy and how that should impact your financial decision making prior to jumping into a bankruptcy case.

401(k) Accounts and IRAs are Exempt

401(k) retirement accounts and IRAs are exempt from execution by your creditors. This means that if you owe money on a credit card, the credit card sues you, obtains a judgment, and now wants to go after your assets, when it comes to your retirement accounts they can't. They are protected under both federal and Arizona law.

The same is true if you are in bankruptcy. Whether you are filing a chapter 7 bankruptcy or a chapter 13 bankruptcy your retirement accounts will be protected during the bankruptcy process.

Bankruptcy vs. Draining the Retirement Account

So, how should this impact your decision making when it comes to filing bankruptcy? If you are retired and dealing with overwhelming debt and need to file for bankruptcy you can go into the bankruptcy process assured that that you are not going to lose your only source of income to your creditors or to the bankruptcy court.

If you are not retired but also have high debt and are borrowing from your 401(k) or taking an early withdrawal on your IRA to make the credit card payments, you need to evaluate whether you will be able to (1) pay off the credit card debt, (2) whether the debt is so insurmountable that even taking

money out of your retirement accounts will only lessen, not eliminate the debt, (3) whether you have sufficient time prior to retirement to be able replenish your retirement accounts.

These questions are important because I see too often people that will drain their retirement accounts to pay what amounts to a small portion of their overall debt, only to find themselves having to file bankruptcy anyway only now they have no retirement funds.

The retirement funds are protected in bankruptcy. If you are in a situation where taking money out of retirement accounts to pay debt will not result in a complete pay off of your debt and/or you are close to retirement age and will not have sufficient time to replenish those accounts, you should meet with a bankruptcy attorney to consider your options.

Bankruptcy may be able to provide relief from your debts while still being able to protect your retirement accounts. I offer a free bankruptcy consultation where we can discuss your specific situation and I can give you recommendations on how to deal with your debt problems.

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