QUALIFIED CHARITABLE DISTRIBUTIONS

QUALIFIED CHARITABLE DISTRIBUTIONS: Qualified charitable distributions (QCDs) are when distributions from traditional Individual Retirement Accounts (IRAs)[1] are directed to qualifying charities. These are deemed "qualified charitable distributions" and not recognized as income to the IRA owner for federal income tax purposes (state rules vary). In years past, taxpayers had to wait until December to see if Congress would approve QCDs for the year, but the Consolidated Appropriations Act of 2016 has made QCDs permanent and they can now be part of a cohesive charitable plan.

IRA DISTRIBUTIONS TREATED AS INCOME: Distributions from IRA accounts are generally treated as ordinary income to the IRA owner and may directly impact the taxpayer's marginal bracket. Once the IRA owner reaches age 72, annual distributions are mandatory.

CHARITABLE DEDUCTIONS: Generally, taxpayers can offset income through deductions, including charitable deductions. However, charitable deductions are not unlimited. The available tax deduction is limited to 60% of adjusted gross income for individuals contributing cash, 30% of adjusted gross income if contributing appreciated property, and 20% of adjusted gross income when contributing to non-public charities. Excess contributions can be carried forward to the next five tax years. Any unused deduction after five years will be lost. Accordingly, it is imperative to speak with a tax preparer to understand available deductions.

BENEFITS OF QUALIFIED CHARITABLE DISTRIBUTIONS: A QCD is not limited by adjusted gross income. It allows a traditional IRA owner to exclude up to $100,000 of distributions, which may include required minimum distributions (RMDs), annually from income if made directly to a qualifying charity. In other words, an IRA owner can continue (or begin) an annual charitable gifting plan by using distributions from an IRA account without increasing his or her taxable income level. This structure heavily benefits traditional IRA owners who are in the mandatory withdrawal stage and are concerned about an increase in their tax bracket. As an example, if we assume an individual is in the 25% tax bracket with a $50,000 QCD -this would translate into a tax savings of $12,500 (which is 25% of $50,000).

QUALIFIED CHARITABLE DISTRIBUTIONS VS. GIFTING APPRECIATED SECURITIES: Although QCDs have clear benefits, they are not the only way to make tax-advantaged charitable contributions. Taxpayers who own highly appreciated assets and have the requisite adjusted gross income level may derive a greater benefit from treating the IRA distribution as income and donating highly appreciated stocks to a charity or donor advised fund (see reverse page.[2] Therefore, while a QCD allows the taxpayer to exclude an IRA distribution from income, donating appreciated securities will allow the owner to offset the income AND avoid future capital gains tax.

1. A QCD **cannot** be made from an inherited IRA

2. A QCD **cannot** be made to a donor advised fund.

Returning to the above example, assume that the individual also has $50,000 in appreciated securities in a taxable account with a $10,000 cost basis (meaning a $40,000 long term unrealized gain). If the taxpayer takes the required IRA distribution as income (and does not make a QCD), and instead donates the appreciated securities, the owner will receive a $50,000 charitable deduction which offsets the IRA income. The taxpayer will also permanently avoid what would have been a $40,000 long-term capital gains tax liability from the appreciated securities. This equates to tax savings of $12,500 ($50,000 x 25% tax rate), plus $6,000 ($40,000 gain x 15% long term capital gains tax rate).

This scenario is highly dependent upon many factors, including adjusted gross income level. In addition, these strategies may impact Medicare Part B premiums. Therefore, it is imperative to consult with a tax preparer to determine the benefits of these strategies.

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