

How to Use Your Retirement Savings for Charitable Giving

By Kathryn Garrison and Kelli Anderson

We have good news for those who want to use their Individual Retirement Account (IRA) to donate to charities. Congress last year made permanent a provision that allows individuals to make a distribution directly from their IRA to a charity without having to recognize it as income. It also counts toward their required minimum distribution, which is the amount they're required to take out of their IRA each year after age 70½.

For the past several years, Congress has extended this charitable IRA contribution in the 11th hour, making planning difficult. So the permanent extension is a welcome change. However, while these qualified charitable distributions can be useful for tax-efficient charitable giving, they aren't appropriate for everyone in all circumstances. When they're not, there are other ways to use IRA accounts for charitable giving.

Qualified Charitable Distributions

To make a qualified charitable distribution, one must be over age 70½, and the gift is limited to \$100,000 per year. The payment has to go directly from the IRA account to the charity. It can't go from an IRA to an individual's bank account, and then to the charity. Additionally, the charity must be a public charity that provides a contribution acknowledgement. As such, qualified charitable distributions can be an efficient way to make charitable gifts, especially for taxpayers with income over \$259,400 (for single filers) and \$311,300 (for married couples filing jointly) - those who are subject to taking limited itemized deductions because their income is above a certain threshold.

Let's look at an example. John, age 72, has an annual income of \$250,000, which includes Social Security, pension, annuity payments, and investments. He is required to take an annual minimum distribution from his IRA of \$75,000. This withdrawal will increase his adjusted gross income to \$325,000, which will likely result in a limit to his annual charitable deductions, as well as various other deductions and exemptions.

John is very involved in his alma mater and makes cash gifts to the school each year. If he distributes his required minimum distribution to his bank account and then sends \$75,000 to the school, he may qualify for a charitable deduction. But it will be somewhat reduced because his income is over \$269,400, making him subject to a limitation on deductions. If he instead has the custodian of his IRA send the \$75,000 directly to the school as a qualified charitable distribution, he is considered to have taken his required minimum distribution—but he doesn't have to recognize the distribution as income. He won't be able to claim a charitable deduction on his income tax return, but in his situation, this is preferable to recognizing the income and taking the offsetting deduction.

Not only individuals subject to limits on their deductions can benefit from qualified charitable distributions. If recognizing the income from required minimum distributions results in one's Social Security income being taxed or higher Medicare premiums, a qualified charitable distribution could be beneficial. On the other hand, making a gift of significantly appreciated assets—or any number of other potential giving vehicles—might be more efficient in any given year. Individuals should consult a financial advisor to determine their most efficient giving option.

Charitable Bequests

In addition to making qualified charitable distributions during their lifetime, individuals may also donate IRA assets at death by designating a charity as the primary beneficiary of all or a portion of an IRA account. When an heir receives an IRA (or a portion of one), he or she must start taking distributions based on his or her age, and those distributions are taxed as income. The alternative is to deplete the IRA account within five years of inheriting it. Unfortunately, this is what most heirs do. Additionally, while the IRA passes outside of probate based on the beneficiary designation, it's still included in the estate for estate tax purposes. That combined hit of estate taxes and income taxes can result in more of the account going to Uncle Sam than to heirs.

A better option may be to leave all or a portion of the IRA directly to a public charity through a beneficiary designation form. The charity can liquidate the account and either spend it or contribute it to an endowment (based on the donor's instructions) without paying any taxes. That way the entire value of the IRA would go to the charity. The estate may also receive a dollar-for-dollar charitable estate tax deduction for the value of the donated amount. Additionally, while a qualified charitable distribution may not be made to a private foundation, supporting organization, or donor-advised fund, it can be left as a charitable bequest to any of these—and still qualify for the charitable estate tax deduction.

Look at the Whole Picture

It's important to work with an accountant and financial advisor to determine the most effective means of making charitable gifts. With a bit of advanced planning, donors can make sure their gift not only fulfills their charitable goals, but also protects the value of their estate.

[Kathryn Garrison, Senior Financial Advisor, Moss Adams Wealth Advisors LLC, advises executives and high-net worth individuals in the creation of highly personalized financial plans and comprehensive wealth strategies. Reach her at kathryn.garrison@mossadams.com or 206-302-6752. Kelli Anderson, Senior Manager, Moss Adams LLP, serves estates, gifts, trusts, and high-net worth individuals, helping them navigate estate, gift, and generation-skipping transfer taxes. Reach her at kelli.anderson@mossadams.com or 206-302-6763 or.]