



June 3, 2016

***TAX SAVINGS ALERT – DIRECT CHARITABLE GIFTS FROM IRAS***

Dear Clients and Friends:

Owners of traditional Individual Retirement Accounts (IRAs) may use a special rule to achieve substantial income tax savings while benefitting charities of their choice. They may transfer up to \$100,000 from their IRAs to charitable organizations without incurring income tax on the IRA withdrawal.

Federal law mandates that an IRA owner who reaches age 70 ½ must withdraw a minimum distribution each year. Withdrawal of the required minimum distribution (RMD) for the year in which the owner reaches age 70 ½ may be deferred until April 1 of the following year. The IRA owner must withdraw the RMD for each subsequent year by December 31 or be subject to a possible 50% penalty.

An IRA owner could withdraw the RMD and then contribute it to the charity. This owner would report the RMD as taxable income and claim an income tax charitable deduction for the contribution to the charity or charities.

Federal law limits the charitable deduction an individual may claim. Total charitable deductions cannot exceed 50% of an individual's income, as adjusted. To illustrate the benefit of this rule, this letter assumes that the IRA owner may deduct only 50% of the contribution. The taxpayer would then pay tax on 50% of the RMD despite all the amounts withdrawn passing to charity.

IRA owners who take advantage of a special rule would distribute up to \$100,000 per year directly to a charity rather than to the owner. The IRA owner would not report that distribution as taxable income nor receive a charitable deduction for that distribution. This direct distribution to the charity complies with the RMD rules, even though the owner does not receive any of it. This direct distribution allows the IRA owner to accomplish his or her charitable goals, avoid any taxable income on the withdrawal, and escape a penalty for not distributing the RMD.

The following chart provides an example of the effects of this charitable distribution based on an individual with an RMD of \$100,000.

	Direct Distribution Of RMD to Charity	Withdrawal of RMD Then Gift to Charity
Gross Income	\$ 0	\$ 100,000
Charitable Deduction	<u>0</u>	<u>50,000</u>
Taxable Income	\$ 0	\$ 50,000

In both situations, the individual satisfies the RMD and avoids the 50% penalty. Nevertheless, the individual owes no tax and reports no income when directing the distribution to the charity. The individual who withdraws the RMD and then contributes it to the charity may be subject to tax on half of the withdrawal. That additional income may affect other tax benefits, depending on the IRA owner's personal tax situation.

This special rule applies not just to an IRA owner. A beneficiary of an inherited IRA may also take advantage of this charitable planning. An individual claiming the benefit of this rule should obtain a receipt from the charity to confirm the contribution.

This special rule is limited to IRAs. It does not apply to 401(k), 403(b) or similar qualified retirement plans. The charitable recipient cannot be a donor advised fund, support organization, or certain private foundations. Charitable remainder trusts, charitable lead trusts, and pooled income funds are also ineligible beneficiaries for this treatment.

If you wish to take advantage of this planning approach, we would be pleased to discuss it with you.

Kind regards.

Very truly yours,

HARTOG, BAER & HAND  
A Professional Corporation



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