RAYMOND JAMES

Tax Planning with Qualified Charitable Distributions

Understand how to benefit from this tax-saving tool

GIVING WITH GREATER BENEFITS

Are you 70½ or older and have an IRA? Do you have charitable intentions for your current or future required distributions? Consider the use of a qualified charitable distribution (QCD).

Although QCD has been around for nearly a decade, it was not made permanent until 2015 when Congress passed the Protecting Americans from Tax Hikes (PATH) Act. This means an IRA owner subject to RMD can donate up to $100,000 directly from an IRA to a charity without getting taxed on the distribution.

Donating IRA funds directly to qualified charities allows the IRA holder or beneficiary to avoid taking possession of the funds and the tax bill that comes with it. Another benefit of the RMD payment applied to the QCD is that the amount is excluded from tax formulas that could impact multiple categories such as Social Security taxation, Medicare Part B and D premium increases, and the Medicare tax on investment income.

IMPORTANT FACTORS

- *A QCD can be used to meet your required minimum distribution.*
- *Your $100,000 contribution limit can include amounts in excess of the RMD payment; however, the total annual amount cannot exceed $100,000 per person.*
- *A QCD is available to an inherited IRA owner if the owner is at least age 70½. While age 70½ is still the trigger age for making QCDs, the SECURE Act reduces the individual's permitted exclusion by the amount of post-age-70½ deductible IRA contributions.*
- *If an RMD payment has already been made for the year, it's considered an irrevocable taxable distribution that can't be reclassified or reapplied as a QCD.*
- *With QCDs, the variety of eligible charitable entities is limited to primarily public charities.*
- *A QCD is not available to active SEP or SIMPLE IRAs – accounts still receiving ongoing employer contributions.*
- *While a QCD can be done from a Roth IRA, this generally isn't advisable given that most distributions at age 70 ½ or older will not be taxed anyway.*
- *The QCD avoids the pro-rata rule. With a QCD, your taxable distributions are distributed first. Normally, if you have made after-tax contributions to one or more IRAs, the pro-rata rule applies (meaning part of the distribution is taxable and part nontaxable).*

HOW IT WORKS

The QCD must be paid directly to the charity which must be a qualified 501(c)(3) institution eligible to receive tax-deductible contributions, like many public charities. A QCD cannot be made to a private foundation, donor-advised fund or supporting organization (as described in IRC 509(a)(3)), nor to a charitable gift annuity or a charitable remainder trust (CRT).

A qualified charitable distribution doesn't offer a split-interest opportunity, such as with charitable remainder trusts where donors receive part deduction and part income from the asset. In that regard, the QCD distribution must have been eligible for a full deduction, not partial. This rule assures that the IRA owner doesn't get a kick-back or other "quid pro quo" benefit for the donation – preventing any "split-interest charitable trust," such as a CRT, from being an eligible QCD beneficiary.

The charitable entity, as the recipient of the QCD, must receive the donation by December 31 in order to ensure credit to the proper year.

QCD AND THE SECURE ACT

The SECURE Act passed in late 2019 made a slight change in the QCD rules to avoid potential game-playing due to the elimination of the age cap on IRA contributions. With removal of the age cap on IRA contributions, an individual could (without the following SECURE-imposed change) make a tax-deductible IRA contribution and an income excludable QCD with the same dollars. The SECURE Act prevents this "double dipping" by modifying the income exclusion for QCDs.

While age 70½ is still the trigger age for making QCDs, the SECURE Act reduces the individual's permitted exclusion by the amount of post-age-70½ deductible IRA contributions.

Example:

In 2020, Jane, who is single, turns age 70½ and has compensation income of $60,000. She makes a tax-deductible contribution of $7,000 to her traditional IRA for 2020. In the same year, after her age 70½ "birthday," she transfers $30,000 from one of her traditional IRAs to her favorite charity. Her 2020 income-excludable QCD amount is only $23,000: Total QCD ($30,000) reduced by tax-deductible IRA contribution ($7,000). $7,000 of her QCD will be included in her 2020 gross income.

Contributions to a Simplified Employee Pension (SEP) IRA will NOT have this effect of reducing the QCD income exclusion cap.

COMPARING THE BENEFITS OF QCD AND NON-QCD STRATEGIES

For some individuals, it may make sense to use a mix of a gifting strategy that incorporates traditional (non-QCD) gifting in addition to the QCD.

STRATEGY 1: QUALIFIED CHARITABLE DISTRIBUTIONS (QCD)

With the amount paid excluded from income taxes, the QCD transfers directly from the IRA to the designated charity and the QCD amount avoids being added as taxable income on your tax return. For those in a high tax bracket, the QCD is a useful way of removing an otherwise taxable RMD payment from being added as income on your tax return.

Tax Year 2019 Standard Deduction

Filing Status	Standard Deduction
Single	$12,200
Head of Household	$18,350
Married Filing Separately	$12,200
Married Filing Jointly	$24,400

Unlike other forms of charitable giving that require you to itemize the gift in order to deduct the contribution on your tax return, the QCD does not have to be itemized. Consequently, you can claim both the standard deduction, or itemize, and still exclude up to $100,000 from the income associated with an IRA distribution. With the passage of the SECURE Act, however, IRA account owners must now reduce their intended QCDs by any contribution amounts made into their IRAs after age 70½. In other words, IRA contributions made after age 70½ cannot be turned around to be used as QCDs. This new anti-abuse provision is designed to prevent individuals from skirting the limitations associated with “regular” charitable giving.

STRATEGY 2: TRADITIONAL (NON-QCD) CHARITABLE CONTRIBUTIONS

When using a typical charitable contribution, in order to claim the charitable deduction, you must elect to itemize donations on Schedule A of your tax return. You should consider itemizing if the total amount of your itemized deductions is more than your standard deduction amount.

When you donate cash to a public charity, you can generally deduct up to 60% of your adjusted gross income. Provided you’ve held them for more than a year, appreciated assets including long-term appreciated stocks and property are generally deductible at fair market value, up to 30% of your adjusted gross income.

Given that the RMD payment is taxable and increases your adjusted gross income, it can potentially impact taxation of Social Security benefits (for low income earners) and potentially increase premiums associated with Medicare Part B and D premiums (for high income earners).

2019 Medicare Part B and Part D monthly premiums based on income

(as reported on your tax return two years ago)

Your Annual Income		Part B	Part D
Individual Tax Return	**Joint Tax Return**	**You Pay**	**You Pay**
$85,000 or less	$170,000 or less	$135.50	$0
$85,001 up to $107,000	$170,001 up to $214,000	$189.60	$12.40
$107,001 up to $133,500	$214,001 up to $267,000	$270.90	$31.90
$133,501 up to $160,000	$267,001 up to $320,000	$352.20	$51.40
$160,001 up to $500,000	$320,001 up to $750,000	$433.40	$70.90

The 3.8% Medicare tax on investment income can also be avoided using QCD. This tax is assessed on couples with Modified AGI over $250,000 and singles over $200,000, and the QCD technique can help keep a taxpayer below these thresholds.

How to file taxes with a QCD

Your 1099-R form will show the distributed amount for the calendar year when your withdrawal is made with no code indicating a QCD. Therefore, when filing:

- List the QCD amount on the 1040 tax form on the line designated for IRA distributions.
- On the line for the taxable amount, enter zero if the full amount was a qualified charitable distribution.
- Enter “QCD” next to this line. See the Form 1040 instructions for additional information.

WHEN A QCD MAY NOT BE THE BEST OPTION

- Gifting highly appreciated stock in a non-retirement account has a dual benefit that the QCD does not have. It removes the gain from taxation and also provides the ability to claim a tax deduction against your income. The QCD just removes the RMD amount from taxation.

- In situations where the contribution will be made by cash or check, the QCD will come out with equal benefit. The QCD may be an effective means of reducing the tax impact of RMD payments; however, using appreciated securities is still the best option from a tax perspective.
- Also, if you are not in the best of health, and your intent is to pass the stock to a family member, it would be wise to simply allow your beneficiary to inherit the highly appreciated asset at death in order to take advantage of the step-up to the date of death value.

WHEN A QCD MAY BE MORE BENEFICIAL THAN DONATING APPRECIATED STOCK

- In instances where the amount of your charitable contributions is at such a high level – relative to your income – the charitable deduction cannot be claimed, even with the utilization of the five-year carry-forwards. Also, if it is unlikely that the carry-forward amount will be used during the five-year period, it will expire.
- If your itemized deductions don't reach the level where they exceed your standard deduction, then the benefits of itemizing charitable deductions are of little use. You can either claim the standard deduction or go with itemizing – but you can't do both. Keep in mind that QCD is available regardless of whether you itemize or choose the standard deduction. If your donation of appreciated securities doesn't rise to the level where it exceeds the standard deduction threshold, then the value of this method of giving is limited. For instance, with the standard deduction for a married couple in 2019 set at $24,400, if you donate $28,000 of appreciated securities, the charitable deduction of $28,000 exceeds the standard deduction by only $3,600 (with itemization). The reality is that this itemizing strategy only produces a charitable deduction that is $3,600 larger than just claiming the standard deduction. If you are considering donating appreciated securities, it's best used when you have enough deductions (such as interest on mortgage) to itemize before including the highly appreciated stock as a charitable contribution.
- If your highly appreciated stock is held within an IRA, then any withdrawal will be taxed as ordinary income anyway, with no opportunity for capital gain treatment.

NEXT STEPS

Since each individual's situation is unique, it's important to seek guidance to explore if this tax-planning tool is right for you to maximize your tax savings. Begin the process by meeting with your financial advisor to take a comprehensive look at your situation in the context of your overall financial plan. If you have considered donating all or part of your IRA required minimum distribution payment to charity, then take action before year-end.

WORK WITH YOUR FINANCIAL ADVISOR

Your financial advisor has the tools, resources and expertise to help you understand if this tax planning tool may be right for you.

- Assess the potential impact of QCDs on your overall financial plan.
- Evaluate key decision factors and understand how they may benefit you.
- Implement your specific plan to maximize your benefits from giving.

LIFE WELL PLANNED.

RAYMOND JAMES®

INTERNATIONAL HEADQUARTERS: THE RAYMOND JAMES FINANCIAL CENTER
880 CARILLON PARKWAY // ST. PETERSBURG, FL 33716 // 800.248.8863
LIFEWELLPLANNED.COM