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The Sweet Life: Charitable Gifts of Retirement Assets

Creamy milk chocolate, earthy dark chocolate, smooth white chocolate—in any form, this treat appeals to almost every sweet tooth on the planet. Chocolate comes from the fruit of native South American trees called *Theobroma cacao*, which is Greek for "food of the gods."[1] This nearly magical food is reported to protect the heart (with its phytonutrients) and create a positive mood (through the release of endorphins).[2]

Charitable giving is also good for the heart (although not in the same way as chocolate or exercise) and it produces positive feelings in the giver. Using retirement assets to make gifts not only feels good, but can provide unique benefits and opportunities.

In this issue of *The Good Advisor*, we look at qualified charitable distributions—gifts made directly from an IRA to charity. This is a noteworthy option for donors of retirement age who want to support a favorite charity.

Qualified Charitable Distributions

Chocolate has a long history. Researchers have found traces of chocolate as far back as 1500 B.C.[3] Mayans and Aztecs used chocolate as currency, for celebrations, and in everyday living.[4] Early chocolate was known for its bitter flavor and was often mixed with chili or honey. Chocolate arrived in the U.S. in 1641, and the first chocolate house opened in Boston in 1682. Chocolate eventually became the most popular sweet treat in the world thanks to the work of entrepreneurs like Daniel Peter (creator of milk chocolate), Henri Nestlé (co-founder of the Nestlé company), and Rudolf Lindt (inventor of the conche machine which aerates chocolate and evenly distributes the cocoa butter, making it smooth).[5]

Qualified charitable distributions (QCDs) have a much more recent history. QCDs became one of the more popular giving methods thanks to the Pension Protection Act (PPA) of 2006. The PPA gave IRA owners the option of making charitable contributions directly from the IRA to a qualified charity.[6] Both donors and charities found great value in this new giving option, making it almost as popular as chocolate! QCDs are sometimes referred to as IRA charitable rollovers—while not technically a rollover, an individual age 70½ or older can donate money (up to $100,000 per year) directly from an IRA to a charity. The amount distributed counts toward the individual's required minimum distribution (RMD) if one is due and is not considered income to the donor.

Legislative History

The PPA

The section of the PPA that authorized qualified charitable distributions was not permanent, and for years taxpayers waited nervously during each session to see if Congress would reauthorize it.

The PATH Act

Finally, in 2015, Congress passed the Protecting Americans from Tax Hikes Act of 2015 (the PATH Act) which made QCDs permanent.[7] Under the Internal Revenue Code at the time of the PATH Act, an IRA owner had to begin taking required minimum distributions at age 70½, without regard to financial circumstance or need.[8] Failure to take an RMD results in an IRS penalty of 50% of the amount that should have been taken but was not—a hefty fine![9]

For example, if Rainbow Bonka, the 74-year-old former VP of Candy Sprinkles for Bonka Candy Company, owned an IRA but refused to take his required minimum distribution of $9,000, Rainbow would be subject to a penalty of $4,500 for failing to take the RMD. If he took $5,000, he would still be penalized for failing to take the remaining $4,000—a penalty of $2,000.

The SECURE Act

In late 2019, Congress passed the Setting Up Every Community for Retirement Enhancement (SECURE) Act, which raised the age individuals must begin taking RMDs from 70½ to 72 beginning in 2020.[10] However, it is important to note that the SECURE Act did not change the age for making a qualified charitable distribution—that option is still available starting at age 70½.

Under the current Internal Revenue Code, the donor must direct the IRA administrator to make a distribution of up to $100,000 directly to a qualified charity.[11] If the IRA owner first receives the distribution, even if they immediately donate the funds, they have not made a QCD and will be taxed on the amount distributed (in other words, there is no "60-day rollover rule" for QCDs). The amount of this distribution is not includible in gross income, meaning the donation has no impact on the donor's charitable limitation.[12] Further, since a QCD has never provided a charitable deduction for donors, it continues to be a good option for those who no longer itemize deductions after the Tax Cuts and Jobs Act of 2016. Let's look at an example.

Billy Bonka never achieved the legendary status that his second cousin found with his chocolate factory, but nevertheless, Billy's job working with chocolate provided him with a comfortable life and a well-funded retirement. When Billy retired at the age of 72, he began to look for additional ways to support his favorite charities. After speaking with professional advisors, this maestro of confection realized he was neglecting a tremendous source of potential donations—his retirement assets!

Billy had an IRA from which he needed to begin taking an RMD of $10,000. However, since Billy's financial situation was solid, he did not need the RMD. Instead, Billy directed his IRA administrator to make a qualified charitable distribution of the full RMD amount to Billy's favorite qualified charity. The administrator facilitated a transfer directly from the IRA to the charity, and Billy obtained a contemporaneous written acknowledgement from the charity for the gift.

At tax time, Billy's tax preparer noted on Billy's return that the full amount of the RMD was a QCD. While Billy did not qualify for an itemized charitable deduction, he paid no tax on the donated RMD. In addition, the QCD had no impact on Billy's overall charitable giving limitation, meaning Billy can still claim a deduction for other charitable gifts.

NOTE: Charitable gift annuities are regulated by state law, so advisors should review the applicable state requirements carefully.

Rules

Of course, a donor must follow all the rules in order to properly make a QCD.

Qualified charities

In order to qualify for the preferential treatment, the distribution from the IRA must be made directly from the IRA to the qualified charity.[13] A qualified charity includes:

1. a charity described in section 170(c)(2);
2. certain veterans' organizations, fraternal societies, and cemetery companies; and
3. a Federal, State, or local governmental entity (but only if the contribution is made for exclusively public purposes).[14]

Neither a donor-advised fund nor a supporting organization is considered a qualified charity for the purposes of a QCD.

Additionally, the distribution will be treated as a qualified distribution only if a deduction for the entire distribution would be allowable under IRC §170. If the deduction is not includible in gross income, the IRC provides that the qualified charitable distribution will not be taken into account in determining the charitable deduction.[15]

Multiple IRAs

The limitation of $100,000 applies to all qualified charitable distributions during a year. A donor with multiple IRAs may not make QCDs of $100,000 each from multiple accounts—this would exceed the threshold. However, the donor could make QCDs of $50,000, $30,000, and $20,000 from three separate IRAs during the same year and fall within the limitation.

Keep in mind that both the donor and the donor's spouse may make qualified charitable distributions up to the $100,000 threshold.

Cautions

Although chocolate provides health benefits, it also adds calories, so overindulging can result in a number of health issues. As with most things in life, being careful and following good eating practices can help chocolate lovers avoid issues. Donors and charities must also exercise similar care in following good giving practices regarding QCDs.

Personal benefit

The Joint Committee on Taxation noted in its report: If a donor receives any personal benefit as a result of the QCD, the entire amount of the distribution will be disallowed unless the donor can demonstrate, among other things, that the fair market value (FMV) of the distribution exceeds the FMV of the benefit received from the charity.[16] This means that charities must be careful in soliciting potential donors with free meals or events. Likewise, a qualified charitable distribution cannot be made in exchange for a charitable gift annuity.

Substantiation

Donors must also be aware of and comply with the same substantiation requirements that apply to charitable deductions. The donor should make sure to obtain written confirmation from the charity for the QCD. This confirmation should contain the amount of the donation and a statement that:

- the charity received the donation directly from an IRA
- the charity is a qualified charity
- it was the donor's intent that the gift qualify as a QCD
- the donor did not receive any goods or services in exchange for the distribution

Non-deductible contributions

If a donor owns an IRA with non-deductible contributions, there is a special rule to determine the portion of the distribution that is includible in gross income and thus is eligible to be used as a QCD. Under the rule, the distribution is treated as consisting of income first, up to the aggregate amount that would be includible in gross income if all the owner's IRAs were distributed in a single year (except for the QCD). In determining the amount of subsequent IRA distributions includible in income, adjustments are made to reflect the amount treated as a QCD.[17]

Non-IRA gifts

Donors with savings in other retirement funds like 401(k)s, 403(b)s, SEPs, SIMPLEs, or pensions funds may want to make their own similar charitable distribution. However, like the kid outside the candy store, these individuals may only peer through the window and dream. Other retirement accounts are not eligible to make qualified charitable distributions.

Feeling Good While Doing Good

Often, chocolate is synonymous with celebrations and holidays—chocolate Easter bunnies and birthday cakes, chocolate fountains at weddings, heart-shaped boxes of chocolates on Valentine's Day. Dark chocolate in particular provides mood-boosting pleasure while delivering a healthy dose of flavanols, which support nitric oxide in the cell lining of blood vessels, helping the blood vessels relax to improve blood flow and lower blood pressure.18 For those who enjoy the taste, eating moderate amounts of dark chocolate is a way to feel good while doing good for the body.

A qualified charitable distribution from an IRA provides a similar double benefit—the satisfaction of helping a favorite qualified charity coupled with the mood-boosting feeling that comes from helping others with money that was not needed but was required to be withdrawn and taxed. The donor can feel good about their well-planned retirement while using their excellent planning to do good for others.

ENDNOTES

1 Jessie Szalay, "Chocolate Facts, Effects & History," Live Science, March 28, 2018.

2 Of course, as with everything, chocolate must be used in moderation. No one should be happy all the time.

3 "History of Chocolate," History.com, last updated August 21, 2018.

4 Id.

5 Jessie Szalay, "Chocolate Facts, Effects & History," Live Science, March 28, 2018.

6 Public Law 109–280, 120 Stat. 780, enacted August 17, 2006.

7 PATH Act of 2015, PL. 114-113.

8 IRC §401(C)(i).

9 IRC §4974(a).

10 Public Law 116-94.

11 IRC §408(d)(8).

12 IRC §408(d)(8)(A).

13 IRC §408(d)(8)(B).

14 See: IRC §170(c)(3)-(5) and §170(c)(1).

15 IRC §408(d)(8)(E).

16 Technical Explanation Of The Protecting Americans From Tax Hikes Act Of 2015, House Amendment #2 To The Senate Amendment To H.R. 2029 (Rules Committee Print 114-40).

17 IRS Publication 590-B.

18 "Dark Chocolate," The Nutrition Source, Harvard T.H. Chan School of Public Health website.

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An electronic copy of our companion booklet with more information about charitable organizations, including a discussion of supporting organizations, donor-advised funds, community foundations and private foundations is available in the Professional Advisor section of our webite at **www.catholicfoundation.com**.

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