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The Secret Way Seniors Can Keep Deducting Gifts to Charity

Americans age 70½ or older can donate IRA assets, lowering their taxable income



ILLUSTRATION: PETER OUMANSKI

Millions of Americans will no longer get tax deductions for their charitable donations this year. But givers age 70½ or older often have a great way to get around this change.

It involves making donations directly from a traditional individual retirement account to one or more charities by using a smart move with a clunky name—qualified charitable distribution, or QCD.

“This transfer is usually the best way for IRA owners older than 70½ to do their giving,” says IRA specialist Ed Slott.

A growing number of IRA owners can use this maneuver. Roughly 3.2 million U.S. residents turned 70 in 2018, about 50% more than in 2010, according to estimates based on U.S. Census Bureau data.

The new focus on QCDs arises from the tax overhaul. It nearly doubled the standard deduction taxpayers get if they don’t itemize their write-offs for state taxes, mortgage interest, donations and the like on Schedule A.

This deduction is now \$12,000 for single filers and \$24,000 for most married couples— high enough so that nearly 29 million more filers will take it than in 2017. Those who do will no longer get write-offs they used to, including for donations.

Yet IRA owners who are 70½ and older have the best of both worlds: They can get a tax break for donations and take the higher standard deduction. In fact, the standard deduction rises to \$13,600 for singles and \$26,600 for couples age 65 and older.

Here’s how an IRA QCD provides benefits. Say that Mary and Jack, a married couple, are 71 and 72. Because they’re older than 70½, they must withdraw a certain amount every year from their traditional IRAs. This year it’s \$40,000.

This couple contributes about \$10,000 to various charities such as their church and colleges. They can choose to write checks to these groups, or give appreciated assets such as stock held in a taxable account, or donate from their IRAs.

But they won’t get a write-off if they send checks, as they’re taking the standard deduction of \$26,600. They also don’t want to give appreciated stocks, because that would deprive their heirs of a tax break, called the step-up, that eliminates capital-gains tax on some assets held at death.

Donating IRA assets gives Mary and Jack the best outcome. While they won’t get a charitable deduction, they won’t owe tax on the \$10,000 in donations and will reduce their taxable IRA payout to \$30,000.

What’s more, the \$10,000 donation disappears from their adjusted gross income, or AGI. That can lower Medicare Part B and D premiums, which are based on AGI plus tax-

free municipal-bond income.

Result: If the couple made \$10,000 of IRA donations in 2017 that cut their AGI to

\$165,000 from \$175,000, they'd save about \$130 per month on Part B and Part D premiums for 2019, based on data from the Kaiser Family Foundation. (Medicare premiums for higher-earning taxpayers are based on a two-year lookback.)

IRA donations can also reduce the 3.8% surtax on net investment income. The income threshold for this levy is \$200,000 for most singles and \$250,000 for most married couples.

Say that another couple, Jane and Bob, donate \$26,000 to charity per year and have AGI of \$275,000 that includes net interest, dividends and capital gains from a taxable account. Making the donations from their IRA as part of their required annual payout puts them below the \$250,000 threshold for the 3.8% surtax and also cuts their Medicare premiums substantially.

Less commonly, making donations from an IRA can help reduce taxes due on Social Security payments.

With QCDs, details matter. Attorney Natalie Choate, an IRA specialist, had one of her own IRA donations go astray in 2017, leaving her at risk of missing the mark on her required minimum distribution. The Internal Revenue Service forgave the mistake, as often happens. If it hadn't, she would have owed a 50% penalty. Here's more.

- Dollar limits. Each IRA owner can give up to \$100,000 a year directly to charities from his or her IRAs. One spouse can't use the other's allotment, but an IRA owner can donate more than his required annual payout.
- Eligibility. IRA owners must actually be 70½ to make charitable transfers.
 - ✓ First-dollars-out rule. The first dollars out of an IRA count as the required withdrawal for that year, and these dollars can't be put back in. For example, if someone is taking monthly payouts from his IRA and wants to make an IRA donation in November, it may be too late to have the entire gift count as part of the required payout.
 - ✓ Mr. Slott recommends making IRA donations early in the year to avoid mix-ups.
 - ✓ Direct payments. IRA donations must go directly from the account to the charity. Typically, the custodian submits them to the charity or else sends checks made out to the charity to the IRA owner, who sends them on.
 - ✓ Qualified nonprofits. IRA donations can't be made to many private foundations, according to the Council on Foundations. They also can't go to donor-advised funds, the popular giving accounts that allow individuals to bunch contributions and take an up-front deduction while designating recipients later on. In general, gifts of IRA assets should go to public charities, such as colleges, churches, and the like.
- No benefits. No benefit is allowed from the charity to the IRA donor, not even a dinner, says Ms. Choate. These rules are different from those that apply for cash donations to charities.

- IRS reporting. The donor must have proper proof in hand from the charity before filing his tax return.

However, IRA custodians aren't required to detail donations on the account owner's 1099-R form. Tax preparers say that as a result, too many givers forget their IRA donations and pay tax on them.



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