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Year-End Giving from IRAs: Traps to Avoid

ESTATE PLANNING, TAX, WEALTH MANAGEMENT
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The holiday season is a time of giving and reflection. Charitable contributions are a time-honored way of achieving one's philanthropic goals while enjoying certain tax benefits along the way. For IRA owners over age 70½, one of the most efficient ways to give is known as the qualified charitable contribution ("QCD"). But look out. IRA owners who have control over the checkbook need to be aware that the QCD rules come with a trap for the unwary.

Here's how a QCD works. Taxpayers over age 70½ are obligated to take required minimum distributions ("RMDs") from their IRA accounts each year. Normally, these amounts are included in the owner's income, and the owner is entitled to a charitable deduction if he or she donates the RMD to charity. But since an owner's charitable contribution deduction is limited by certain provisions in the tax code, the deduction does not fully offset the reported income.

By contrast, with a QCD, the custodian of an IRA transfers money directly to a charity chosen by the owner. The amount transferred, up to $100,000 per year, is not included in the IRA owner's income, and counts toward his or her RMD for the year. This is a win-win result for the owner and the charity.

Taxpayers with control of their IRA checkbooks need to be careful when writing checks to charities this time of year. This is because the rules are written such that only the IRA *custodian*, and not the IRA *owner*, can make a QCD. This is contrary to the rules for other types of charitable gifts and can lead to unintended tax consequences.

For example, assume that an IRA owner mails a check to a charity on December 23 with the intention that the donation qualify as a QCD and count toward the RMD for the year. The charity deposits the check in its bank account on January 2, and the IRA custodian transfers the funds from the IRA account to the charity's bank account on January 3. Under ordinary charitable deduction rules, the gift would be deemed complete when the owner mailed the check on December 23. But under the QCD rules, since no action was taken by the custodian until January 3, the QCD will not be treated as made until the second year. The owner thus failed to take the required RMD for the first year and will be subject to penalties for failure to do so.

So what can an IRA owner with control of the checkbook do to avoid this result? First, since charities receive a high volume of donations during the holiday season, it is wise to avoid last-minute gifting to allow for sufficient processing time. It may also be a good idea to call the charity to obtain its assurances that the check was received and will be deposited before year-end. In addition, IRA owners with control of the checkbook may nonetheless wish to consider having the custodian mail the check directly to the charity. Doing so would cause the QCD to be complete as of the date of the mailing. Taking these precautions can ensure that year-end gifting is accomplished without any unwelcome holiday surprises.

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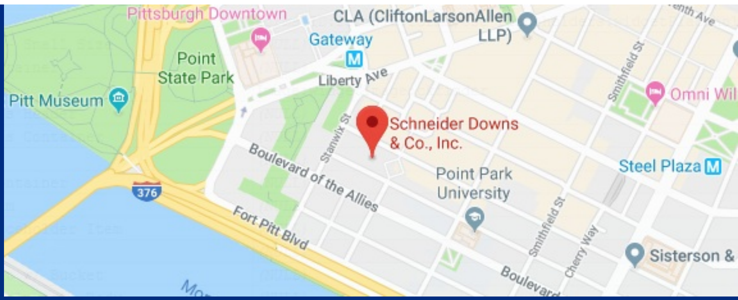

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