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Doing Better By Doing Good:
IRA Distributions to Public Charities

By Jonathan Davis

Protecting Americans From Tax Hikes Act of 2015 (PATH Act)

The Federal "Protecting Americans From Tax Hikes Act of 2015" ("PATH Act") made permanent a provision of the Internal Revenue Code that allows taxpayers, aged 70 and ½ or older, to direct as much as $100,000 of IRA distributions, each year, to most kinds of "public" charitable organizations – and to have the distribution count towards fulfilling the required minimum distribution requirement for IRAs. (PATH Act sec. 112(a)DivQ, amending US Internal Revenue Code sec. 408(d)(8) – effective for IRA distributions occurring after 2014 and after the IRA owner has attained age 70 and ½). It's obviously not for everyone. But, for the few IRA owners who might be interested in exploring this approach, it offers a few additional benefits.

"Regular" IRAs (not Roth IRAs) must be distributed beginning not later than April 1 of the year after the year in which the owner attains age 70 and ½. Distributions from an IRA must be not less than certain minimum amounts (called "required minimum distributions"). These are based on IRS tables and depend upon the age of the IRA owner (or the ages of the IRA owner and the designated post-death beneficiary). (Treasury Reg. sec. 1.401(a)(9)-9).

If the IRA owner has more than one IRA, the owner can take more than the amount of the required minimum distribution from one IRA and have the excess count against the required minimum distributions for the other IRAs. (Reg. sec. 1.408-8 Q&A9).

> For example – the IRA owner may take a distribution from just one IRA that equals or exceeds the minimum distributions required from all of the owner's IRAs, and, in that way, satisfy the required minimum distributions for all IRAs for that year.

IRA Distributions to Public Charities

Under the PATH Act, in each year after an IRA owner who has attained age 70 and ½, the owner may have an IRA make distributions of as much as $100,000 to a "public charity"; and what would otherwise have been an ordinary income distribution to the owner will, instead, offset the owner's required minimum required distribution amounts for the year.

> For example – suppose that in 2016 the owner has five IRAs and the required minimum distributions from all IRAs is required to total $50,000. The owner could have one of the IRAs distribute all $50,000 to a "public charity" and none of the other IRAs would have

to make required minimum distributions to the owner for that year. The owner could do something similar in subsequent years.

Additional Tax Benefits

There may be other benefits.

The distribution to the "public charity" is excluded from the owner's gross income for the year of distribution. That's important because amounts excluded from gross income are also excluded from the owner's "adjusted gross income" ("AGI") for Federal income tax purposes, and several tax costs may occur if AGI is too large.

For example – itemized deductions – including charitable deductions - may be reduced if AGI is too high. But, an IRA owner may reduce his or her AGI by using an IRA to pay the required minimum distribution directly to a "public charity" and, in addition, not have to worry about losing some of the tax benefit of the charitable contribution if the owner's itemized deductions, in general, have to be reduced.

Another example – "miscellaneous itemized deductions" are allowed only to the extent they exceed 2% of AGI. If AGI is lowered (by excluding from gross income IRA distributions to "public charities") more of the miscellaneous itemized deductions may be allowed.

Another example – in 2016, for taxpayers age 65 or older, medical expense deductions are allowed only to the extent they exceed 7 and ½% of AGI. (In later years allowable medical expense deductions must exceed 10% of AGI).

Another example – personal exemptions begin to phase out as the taxpayer's AGI exceeds certain levels.

Being able to exclude from Federal AGI distributions by IRAs to public charities may moderate or avoid some of these disadvantages.

Also, in calculating the Massachusetts personal income tax, these kinds of charitable distributions are, in effect, deductible.

Not a PATH for All Taxpayers

Despite the benefits, making IRA distributions directly to "public charities" is obviously not for everyone.

- The IRA owner must be wealthy enough so that he or she does not personally need the required minimum distribution.

- The IRA owner must be motivated to make a charitable contribution to a "public charity". Public charities are, essentially, publicly supported charities like non-profit colleges, hospitals, American Cancer Society, the Red Cross; also religious institutions; – but not "private foundations" and, in this case, also not "donor advised funds". [Although, when you think about it, using an IRA in this way is a bit like having a "donor advised fund".]

- And the IRA owner must have attained age 70 and ½ before the IRA makes the distribution (not after the distribution, even if it is in the same calendar year).

But, in the right circumstances, this might be an approach worth considering - for example, if the IRA owner intends to fulfill a large lump sum charitable pledge (for example, to a building fund at the local hospital), or to make regular charitable contributions each year to a favorite public charity (for example, an annual donation to a college).

Advanced Planning Needed to Implement Distributions to Public Charities

An interested IRA owner should, well in advance, consult with the IRA trustee as to what the IRA trustee will require in order to make the distribution. For example, the IRA trustee may not be willing to make distributions to more than one public charity during the year – the administrative burden of making multiple distributions being too great. Or, the IRA trustee may not be willing to divide distributions in the year between a public charity and the IRA owner – again, because of administrative difficulties. Also, the IRA trustee may require particular paper work, including a request from the public charity. If the IRA owner is thinking of doing this over several years, the IRA trustee may require a new set of paperwork each year.

Depending upon what the IRA trustee wants, it may make sense for the IRA owner to first reduce the size of the IRA by making a direct "trustee to trustee" transfer into a new IRA or into an already existing IRA, so that IRA owner ends up with an IRA that is the right size for what the owner intends and what the IRA trustee is prepared to allow. Or, the IRA owner may decide to first make a "trustee to trustee" transfer into a new IRA with a different IRA trustee that is more cooperative than the previous trustee.

Surviving Spouses

Suppose an IRA owner dies and the owner's spouse is the IRA beneficiary. Can the surviving spouse do the same thing with the IRA? The Internal Revenue Code requires that the IRA must be "maintained" "for the benefit of" the individual who has attained age 70 and ½ (Code sec. 408). It seems that if the spouse has either elected to treat the IRA as his or her own, or the spouse has made a direct "trustee to trustee transfer" from the IRA to the spouse's own IRA, or has made a "rollover" to the spouse's own IRA, then the spouse can use the same technique subsequently (provided that the spouse has attained age 70 and ½ before the charitable distribution is made). (See, Treasury Reg. sec. 1.408-8 Q&A 5, Q&A 7, and Q&A 8).

An Attractive Tax Planning and Charitable Giving Technique for Some

It's clear that the technique has some attractions for the right individual but, also, some complexities. If an IRA owner is interested in the technique the owner should begin to explore the matter with the owner's professional advisors and with the IRA trustee.

About the Author

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