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MEMO

To: Account Review Committee

From: Ray Thompson

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Subject: Rules and Requirements for Charitable Distributions from IRA's

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For nearly a decade, the rules allowing for a tax-free Qualified Charitable Distribution ("QCD") directly from an IRA to a charity have been an on-again, off-again affair, with Congress allowing the QCD option to lapse, only to be reinstated again in subsequent years. With the PATH Act of 2015, QCD's were finally made permanent.

The core requirements for making QCD's from an IRA to a charity are contained in IRC Section 408(d)(8), and include the following main provisions:

1) The <u>IRA owner must be at least 70½</u> (not merely turning 70½ sometime that year) at the time the distribution is made.

2) <u>Only distributions from an individual IRA (including rollover IRAs and inherited IRAs) are eligible</u>, not distributions from a SEP or SIMPLE IRA (if they are still "active" and receiving ongoing employer contributions), nor from any type of employer plan. A QCD is also permitted from a Roth IRA as well, although most distributions from a Roth IRA are already tax-free if you are over 59½ years of age, so the QCD rules wouldn't be applicable.

3) To qualify for QCD treatment, the rules also stipulate that <u>the distribution must go to a public charity</u> [as described in IRC Section 170(b)(1)(A)], and thus cannot go to a private foundation or a charitable supporting organization (charitable organizations that carry out their exempt purposes by supporting other charitable organizations) or a donor-advised fund.

4) <u>The QCD must be one that otherwise would have been eligible for a full charitable deduction</u> under IRC Section 170. This "must have been eligible for a full deduction rule" ensures that the IRA donor does not receive any "quid pro quo" benefits for the donation (which would limit the donor's deduction to only the net amount contributed) and, thus, fail the "full deduction" QCD requirement. This requirement also prevents any "split-interest charitable trust" (e.g., charitable remainder trust or a charitable lead trust) from being an eligible QCD beneficiary.

5) The maximum dollar amount of a QCD for any individual from his/her IRA is limited to $100,000 per year. For QCDs, this annual limitation is done on a "per-taxpayer" basis (across any/all of the individual's IRAs, regardless of how many accounts are used to generate the charitable distribution); a married couple can each do up to $100,000 (as long as each taxpayer's QCD comes from his/her respective IRAs).

6) Required Minimum Distributions ("RMD's") can be used as the QCD funding mechanism.

7) The QCD is subject to IRS "ordering rules". While a QCD is normally treated as a direct pre-tax contribution from an IRA to a charity, additional "ordering rules" are necessary to determine the tax consequences of a QCD when the available pre-tax IRAs include after-tax (non-deductible) contributions.

8) The benefit of doing a QCD from an IRA is that the distribution comes out of the IRA without any of the tax consequences that would otherwise apply to a withdrawal (i.e., it is excluded from income altogether). Notably, there is no charitable tax deduction for making the QCD contribution to the charity, but only because by definition it was already entirely pre-tax (having come directly from a pre-tax IRA).

   In addition, to the extent that the IRA owner had a Required Minimum Distribution (RMD) obligation for the year, the QCD is deemed to satisfy the RMD, even though the QCD is not taxable as an RMD otherwise would have been. And since an IRA owner must be age 70½ in order to do the QCD, by definition he/she will also have at least some RMD due for that tax year.

9) In order to receive favorable treatment for a QCD in the current tax year – including having the RMD satisfied for the current tax year, and falling under the current year's maximum QCD contribution limit – the charity should ideally cash the QCD check by December 31st. In practice, this means beginning the process to complete the QCD by mid-December, as most IRA custodians will insist that the check be payable to the charity but still mail it to the IRA owner first (who must then forward it on to the charity); to get the check payable to and sent directly to the charity will in most cases require a bank Medallion guarantee (a similar but more stringent process than getting a signature notarized), which usually has to be mailed in once completed (possibly creating further delays).

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