Midyear Alert: Have You Taken Your RMD? Should You Make A QCD?

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If you haven't taken your required minimum distribution from your traditional IRA yet for 2023, have you considered your options now that half the year is gone?

What if you don't need that money to help pay your current expenses? A "QCD" could be a valuable option for you if you have a charity you would like to donate to.

A qualified charitable distribution is a way to benefit charity while using money that would otherwise be taxed when withdrawn. There are limits and rules, but nonetheless, a QCD is definitely worth considering — with the help of your tax adviser.

Taxing RMD Issues

Before getting into more detail on QCDs, let's review how RMDs are taxed.

"Annual required minimum distributions, or RMDs, are normally taxed as ordinary income and are includable in a taxpayer's adjusted gross income," according to Jo Anna Fellon, a partner and the National Leader of Private Client Services at Marcum LLP, a national accounting and advisory services firm.

"This is important to consider since the additional 3.8% tax on net investment income, taxes on Social Security benefits, Medicare premium expenses, as well as some tax credits are calculated based on a taxpayer's AGI," Fellon said. "The additional increase to a taxpayer's AGI in a year when a RMD is taken can drive up the annual tax bill in a meaningful way."

One option to mitigate taxes on RMDs is a QCD. As Fellon points out, "Often when the taxpayer, financial adviser, and tax professional are partnered in the annual planning, RMDs can actually create a benefit for a taxpayer who is charitably inclined when proper adherence to IRS guidelines are observed."

Get Tax Advice

At this point, let me remind you that you'll want to consult your tax adviser about how taking your RMD can affect your situation, as each person's tax situation is unique.

QCD Example

A QCD is an exclusion from your gross income, meaning that if you make a QCD for $50,000, that reduces your gross income dollar-for-dollar (for example, $120,000 gross income is reduced to $70,000). Of course, for that to happen, you have to be sure to do an *effective* QCD (there are rules to follow).

QCD Rules

If you are unfamiliar with QCDs, here are some key requirements you need to know:

- Age: The current starting age for RMDs is 73, but you can start your QCD earlier at age 70 ½. You must be at least 70 1/2 at the time you transfer QCD monies to the charity you are donating to.

- IRAs only: “Generally, QCDs are allowed from traditional IRAs and inherited IRAs (in some cases SEP or SIMPLE plans may qualify if they are inactive),” according to the Schwab Center for Financial Research.

- Spouses: Only the IRA owner can do a QCD for him- or herself, not for a spouse. However, note that both spouses can do their own QCDs, provided they meet all the other requirements.

- Limits: A QCD is limited to no more than $100,000 per year (note that under SECURE Act 2.0, the $100,000 will be indexed starting in 2024 — that means there will be a cost-of-living increase).

- Taxes: The QCD is a nontaxable IRA withdrawal.

- The charity: Only qualified charities can receive QCDs. Check the IRS Tax Exempt Organization Search Tool.

- Tax Deduction? No. There is no charitable deduction for a QCD.

- Timing: QCD monies must actually leave the IRA by Dec. 31. (Don’t wait until the end of the year when custodians are the busiest.)

- No intervention: If you withdraw IRA money that you want to count as a QCD, that won’t work. The QCD payment must go from the custodian of your IRA directly to the qualified charity.

- Note for your file: Get a written acknowledgement of the contribution from the charity for your file.

Who Accepts QCD Donations?

If you don't have a particular charity in mind, what about a local hospital or college that might have played a role in your life?

For example, if you decided to make a QCD to your college alma mater, you could contact the school's gift planning office to find out more information.

Again, check the IRS Tax Exempt Organization Search Tool to make sure the recipient of your donation is a qualified charity eligible to receive a QCD.

New For 2023

Starting in 2023, QCDs can offer you, the donor, a lifelong annuity payment.

SECURE Act 2.0, which was part of the Consolidated Appropriations Act that was passed in December of 2022, created a QCD "split-interest entity," allowing the charity to pay lifelong income to the QCD donor.

There are some important details about the split-interest entity:

- Limit: The maximum amount an individual can transfer via a QCD is $50,000.
- Once in a lifetime: You can only do one transfer in a lifetime. You cannot split it up over a few years.
- Spouse: Your spouse can do the same one-time $50,000 transfer from his or her IRA.
- Subtracting: The $50,000 (or whatever amount chosen) counts toward the annual QCD limit ($100,000 in 2023).
- Direct: Again, the QCD must be paid directly from the IRA custodian to the qualified charity.

- Annuity payments: The charity must start payments no later than one year after the date of funding.
- Taxation of annuity payments: The payments you receive from the split-interest entity are taxed as ordinary income at your regular tax rate.

A split-interest entity, according to SECURE Act 2.0, is:

- A charitable remainder annuity trust,
- A charitable remainder unitrust, or
- A charitable gift annuity

Payout Rate

For the split-interest entity, most charities offer payout rates that are provided by the American Council on Gift Annuities. On its website, the nonprofit organization describes the rates as "designed to balance an attractive payment stream for the annuitant with a good gift for the charity."

For example, the payout rate for a 74-year-old is 6.4%, which means that someone who makes a $50,000 QCD to, say, a school's charitable gift annuity life income plan could receive $3,200 per year for as long as the person lives. Once the person passes away, the university would keep the remainder of the donation.

Not Old Enough for RMDs?

If you are 70 ½ or older but have not reached your required beginning date for taking RMDs, should you consider a QCD? If you don't need your IRA to cover current expense, and you have a large IRA, your QCD will reduce your IRA's overall balance.

Do Your Due Diligence

Again, a reminder: Before you decide to make a QCD for your RMD, discuss it with your tax adviser to make sure it works for your overall tax situation.

Questions?

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