THE WALL STREET JOURNAL.

Popular IRS Charitable Tax Break Can Be Valuable—for Those Who Know How to Use It

Rules around IRA charitable transfers can be tricky. Here's what you need to know
If done properly, the transfer of money from an IRA to a qualified charity counts toward an IRA owner's required minimum distribution for the year.

By **TOM HERMAN**
Updated March 27, 2016 10:06 p.m. ET

A popular tax break that died at the end of 2014 has returned from the dead. That's welcome news for many older people thinking about making gifts to their favorite charities directly from their individual retirement accounts. It's joyous news for many charities, too. But, as with too many of our nation's tax laws, this seemingly simple break can be tricky, as readers have pointed out with several excellent questions.

At issue is a law that generally allows IRA owners who are 70½ or older to transfer as much as $100,000 a year to qualified charities directly from their IRAs, tax-free. That transfer is excluded from your income. If done properly, the transfer counts toward an IRA owner's required minimum distribution for the year.

Although this provision expired at the end of 2014, Congress resurrected it late last year, making it retroactive to the start of 2015—and making it permanent, says Greg Rosica, a tax partner at Ernst & Young LLP.

If you are thinking of taking advantage of this provision, make sure you understand the fine print. For example, you have to transfer assets directly from the IRA to qualified charities to qualify.

Among those keenly interested in this subject is my friend Steve Treadgold, a lawyer who lives in La Jolla, Calif. Steve raises an interesting question about the age limit.

Steve recently turned 70. He wants to make a donation now directly from his IRA to charity because it would qualify for a generous matching contribution from another organization. Steve will be 70½ in August. If he waits until then, the matching offer won't be available.

Steve asks: Can he make the transfer from his IRA now and qualify for this tax provision since this is the year in which he will turn 70½? Or does he have to wait to make the transfer at least until the day in August when he actually reaches the official milestone of 70½?

Answer: "You cannot take advantage of this special provision until you reach age 70½," says Martin Hall, a partner in the Boston office of Ropes & Gray LLP and head of the law firm's private client group. "Your reader will have to wait until August."

An IRS publication confirms this point. It says you must be least 70½ "when the distribution was made."

Here are answers to other questions about this provision, known in some tax circles as “qualified charitable distributions,” or QCDs.

Q: Can I make a transfer from my IRA to my donor-advised fund and qualify for this break?

A: No. Donor-advised funds, such as those offered by Fidelity Investments, Vanguard Group, Charles Schwab and other financial institutions, don’t count as qualified charities under this provision, says Mr. Rosica of Ernst & Young.

Q: What about other types of retirement plans? For example, can you make a qualified charitable transfer from a 401 (k) plan?

A: No, says Mr. Hall of Ropes & Gray. This provision doesn’t apply to “distributions from Keoghs, 403(b) plans, 401(k) plans, profit-sharing plans and the like,” he says.

Also, distributions from employer-sponsored retirement plans such as Simple IRAs and Simplified Employee Pension Plans “don't qualify,” Mr. Hall says.

Q: Is the maximum exclusion amount really $100,000 a year, or is it $100,000 over my lifetime?

A: That $100,000 amount is the maximum annual amount, says Mr. Rosica of Ernst & Young. It isn’t a once-in-a-lifetime offer.

Q: How does it work for married couples? Is the limit $100,000, or double that amount?

A: You and your spouse each can exclude up to $100,000. That amount is the maximum per person, not the maximum for married couples. “However, each spouse must have his or her own account, and each spouse cannot make a qualified charitable distribution for more than $100,000,” Mr. Hall says.

Q: If I take advantage of this provision, can I deduct my transfer as a charitable donation?

A: No. These charitable transfers are tax-free but not tax deductible.

Q: So if you can’t deduct these transfers as charitable gifts, why is this law so popular?

A: Many donors prize this provision because the transfer won’t inflate their income, thus helping them in several ways.

Many tax deductions, credits, phase-outs and other numbers are tied to “adjusted gross income” or certain other measures of income. Thus, by excluding qualified charitable transfers from income, this provision helps many people save money. For example, it may spare them from owing higher taxes on Social Security benefits and from having to pay higher Medicare premiums, as my colleague Laura Saunders pointed out in a column in The Wall Street Journal late last year.

If these direct IRA charitable transfers weren't excluded from income, taxpayers could get hit in other ways. Higher adjusted gross income "might make one more likely to be subject to the tax on net investment income," says Mark Luscombe, principal analyst at Wolters Kluwer Tax & Accounting. "It might increase the amount of the phaseout for many other deductions and credits. By keeping adjusted gross income lower by doing a direct IRA distribution to a charity, a taxpayer may increase the benefit of these other breaks."

Moreover, some donors can't deduct their charitable donations anyway because they take the standard deduction, instead of itemizing. About two-thirds of all returns each year claim the standard deduction.

***

Mr. Herman is a writer in New York City. He was formerly The Wall Street Journal's Tax Report columnist. Send your comments and tax questions to taxquestions@wsj.com*. Please include your full name, address and phone number in case we need to contact you to get more details about your question.*