Individual Retirement Accounts
Qualified Charitable Distribution (QCD)

DONNA BANKS INCOME TAX SERVICE
Monica Banks Figueroa
LTC #71221-C

Rob Figueroa
LTP #26342-P

Email: MONICA@BANKSTAX.COM

Qualified Charitable Distribution (QCD)

In general, distributions from a traditional IRA are taxable in the year received. However, a qualified charitable distribution (QCD) is generally a nontaxable distribution made directly by the trustee of your traditional IRA (other than a SEP or SIMPLE IRA) to an eligible charitable organization. If all of the qualifications are met, a QCD is nontaxable and you cannot claim a charitable contribution deduction for it. Taking a QCD can help lower taxable income.

Qualifications and Rules

Certain qualifications must be met:

- You must be at least age 70½ when the distribution is made.
- The maximum annual exclusion for QCDs is $100,000 per taxpayer. Any QCD in excess of the $100,000 exclusion limit is included in income as any other distribution. If you file a joint return, your spouse can also have a QCD and exclude up to $100,000.
- Beginning 2023, a one-time QCD up to $50,000 may be made to a split-interest entity (charitable gift annuity, charitable remainder trust, and charitable remainder annuity trust).
- The amount of the QCD is reduced by the aggregate IRA contribution deductions taken by you after you turned 70½.
- A QCD may be used to satisfy all or part of your required minimum distribution (RMD) but is not limited to the RMD amount.
- You must have the same type of acknowledgment of your contribution that you would need to claim a deduction for a charitable contribution.
- A charitable contribution deduction on Schedule A (Form 1040), *Itemized Deductions,* cannot be claimed for any QCD excluded from income.
- The QCD amount is limited to the amount of the IRA distribution that would otherwise be included in income. If your IRA includes nondeductible contributions, the distribution is first considered to be paid out of otherwise taxable income.
- The QCD cannot be distributed to you first and then donated, it must be transferred directly to the charity. Any check issued must be made payable to the charity. If you have check-writing privileges for an IRA, you may be able to write out a check to the charity. Check with your IRA trustee for the proper QCD procedure.

QCD versus direct contribution to a charity. You can make a charitable contribution to a qualified charity through a QCD or by withdrawing funds from an IRA and then donating the funds directly to the charity. In either case, the distribution from the IRA counts toward meeting the RMD. By withdrawing funds from the IRA and making the contribution direct to the charity, you may increase your AGI and your taxable income. See *Increase in AGI,* later.

Example: *Janet is single, age 73, and wants to contribute $5,000 to a qualified charity using funds from her IRA. She considers the following two options:*

Qualified charitable distribution. Janet could make the $5,000 contribution through a QCD by instructing the IRA custodian to send the charity $5,000 directly from her IRA. The QCD does not increase her AGI (or count as income when determining the taxability of her Social Security benefits), but she is not able to claim a charitable contribution deduction for it.

Withdraw-then-donate. Alternatively, she can withdraw $5,000 from her IRA, deposit the funds into her bank account, and then directly make the contribution to the charity. The $5,000 distribution

Individual Retirement Accounts

Qualified Charitable Distribution (QCD)

increases her adjusted gross income and, if she itemizes, increases her total itemized deductions by the $5,000 charitable contribution.

Suppose Janet has $11,000 in other itemized deductions. If not for the $5,000 charitable contribution, Janet would use the standard deduction of $15,700 (2023) for a single taxpayer over age 65. With this contribution, she itemizes and deducts $16,000 ($11,000 + $5,000), $300 more than the $15,700 standard deduction amount. In this case, she only benefits from $300 of the $5,000 contribution. All else being equal, Janet's taxable income would be $4,700 higher with the withdraw-then-donate option than with utilizing a QCD. Janet would need to have $15,700 in other deductions, an amount equivalent to her standard deduction, to make this option match the tax effectiveness of a QCD.

Increase in AGI. Under the withdraw-then-donate option, a taxpayer's AGI will be higher than with the QCD option. A higher AGI could increase taxable income, total tax, and affect various limitations.

- **Social Security.** A higher AGI increases provisional income by the same amount. Provisional income is used to calculate the taxable portion of Social Security benefits. For most Single taxpayers, provisional income between $25,000 and $34,000 causes up to 50% of Social Security benefits to be taxed. Above $34,000 causes up to 85% of Social Security benefits to be taxed, which is the maximum amount that can be taxed. The threshold levels for Married Filing Jointly are $32,000 and $44,000, but the same principle applies.
- **Capital gains.** An increase in taxable income could push a taxpayer into a higher maximum capital gains tax rate. For 2023, capital gains are taxed at 0% for Single taxpayers with taxable income less than $44,625.
- **Medicare Parts B and D premiums.** The amount of Medicare Part B and Part D premiums are tied to the taxpayer's modified AGI from two years ago. MAGI for 2023 will affect the amount of 2025 premiums.
- **Medical and dental expense deduction limitation.** Medical and dental itemized deductions are limited to the amount that exceeds 7.5% of AGI. The QCD option could produce a lower total tax bill by setting a lower threshold for deducting medical expenses.
- **Charitable gift deduction limitation.** Gifts donated through a QCD are not reported as itemized deductions or subject to limitation. Generally, the maximum deduction for cash gifts on Schedule A (Form 1040) is limited to 60% of AGI. Unused portions can be carried forward up to five years.
- **Tax credits limitation.** Many tax credits are limited or disallowed for taxpayers with a higher AGI.
- **State income tax.** Many states' income taxes are based on federal AGI. Therefore, a QCD could produce a lower state tax bill.

Offset of QCDs by amounts contributed after age 70½. The amount of QCDs that you can exclude from income is reduced by the excess of the total amount of IRA contributions that you deducted for the tax year and any prior tax year after 2019 that you were age 70½ or older over the amount of IRA contributions that were used to reduce the excludable amount of QCDs in all earlier years.

Example: *Augie became age 70½ in 2020 and deducted $5,000 for contributions that he made in 2021 and 2022. Augie does not make any QCDs for 2021 but makes a QCD of $6,000 for 2022.*

He determines that he has no excludable QCD for 2022. His 2022 qualified charitable distribution of $6,000 is reduced to zero by the total of $10,000 for the contributions that he deducted in 2021 and 2022. However, the $4,000 that did not reduce the excludable amount of qualified charitable contributions must be used in a future year.

Augie decides to make a qualified charitable distribution of $6,500 for 2023. His excludable qualified charitable distribution for 2023 is $2,500 ($6,500 – $4,000).

QCDs from an IRA with deductible and nondeductible contributions. If you make QCD from an IRA and the QCD exceeds the deductible contributions and earnings in the IRA, your QCD may be reduced and you may need to complete Form 8606, *Nondeductible IRAs,* to determine the taxable amount of the distribution and the revised basis in the IRA. However, you may be able to deduct the unused QCD as a charitable contribution. Because this situation can be complex, consult with your tax professional.

Contact Us

There are many events that occur during the year that can affect your tax situation. Preparation of your tax return involves summarizing transactions and events that occurred during the prior year. In most situations, treatment is firmly established at the time the transaction occurs. However, negative tax effects can be avoided by proper planning. Please contact us in advance if you have questions about the tax effects of a transaction or event, including the following:

- Pension or IRA distributions.
- Significant change in income or deductions.
- Job change.
- Marriage.
- Attainment of age 59½ or 73.
- Sale or purchase of a business.
- Sale or purchase of a residence or other real estate.
- Retirement.
- Notice from IRS or other revenue department.
- Divorce or separation.
- Self-employment.
- Charitable contributions of property in excess of $5,000.