INVESTING SPECIALISTS

# Clearing Up QCD Confusion

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Starting with 2018, employing a qualified charitable distribution, or QCD, from an IRA became a more attractive strategy than ever.

The QCD, which allows eligible investors to steer their required minimum distributions into charity and exclude the contribution from income, became a permanent part of the tax code in 2015.

The benefits of the QCD really came to the fore last year, however, as the new tax laws went into effect. The near-doubling of the standard deduction meant that the expected percentage of taxpayers who itemize their deductions (including charitable contributions) dropped precipitously starting with the 2018 tax year. The QCD, however, gives RMD-subject taxpayers the chance to contribute to charity and still gain a tax benefit. That's because the amount contributed to charity via the QCD, up to $100,000, can be excluded from adjusted gross income while also satisfying required minimum distributions. And that exclusion is allowable regardless of whether the taxpayer itemizes or takes the standard deduction.

The net effect is that any eligible RMD-subject taxpayer with IRAs who's making any sort of charitable contribution and not itemizing deductions would most benefit from using the QCD; without it, they'd gain no tax benefit from charitable contributions. And retirees executing this maneuver have the opportunity to pull off a four-fer: They can reduce risk in their portfolios by pruning appreciated securities to meet their RMDs, fulfill their RMD requirements, give to charity, and reduce their taxable income.

But as QCDs become more widespread as a charitable giving tool for older adults, more questions will naturally crop up.

## QCD Basics

One of the most basic questions is who's eligible for a QCD; not everyone who's subject to RMDs or who has an IRA can take advantage of the

maneuver. Whereas younger people may be subject to RMDs--for example, if they've inherited an IRA--only people who are age 70.5 or older and subject to RMDs can employ the QCD. Moreover, the charity must qualify as a 501(c)(3) organization; the QCD isn't available for contributions to donor-advised funds or private foundations. But you can make donations to more than one charity via the QCD, and you can do multiple QCDs throughout the year; your contributions don't have to come in one fell swoop.

In addition, as retirement expert Ed Slott points out in this video, the QCD is not available for every account type, even if those accounts are subject to RMDs. The QCD is only available for traditional, rollover, inherited, and inactive SEP and SIMPLE IRAs. (Inactive in this context means they're no longer receiving employer contributions.) Other RMD-subject balances, such as 401(k)s, are not eligible for QCD treatment. Because the chief benefit of the QCD is to lower taxable income and satisfy RMDs, the strategy would rarely be used with Roth IRAs, in that qualified distributions wouldn't typically be taxable and Roth IRA accounts aren't subject to RMDs.

**Timing Matters**

That all seems straightforward enough, but there can be additional issues around QCD timing, according to Slott; some investors with the best intentions ran into this problem in 2018.

For starters, there's no "grace period" for doing a QCD. In contrast with IRA contributions, which can be made up until the tax-filing deadline in mid-April, you couldn't do a QCD in mid-April 2019 and expect it to count on your 2018 tax return.

Additionally, an RMD, once taken, can't retroactively be classified as a QCD, according to Slott. For example, let's say that a 74-year-old needs to take a $22,000 required minimum distribution from his traditional IRA for 2019. He likes to take his RMD early in the year so he won't forget, so he takes his $22,000 RMD in March. If, later on this year, he's thinking about charitable contributions and would like to do a QCD, he can't recharacterize his early-year withdrawal as a QCD. Rather, because of what's called the "first dollars out" rule, which holds that the first dollars pulled out of an IRA by RMD-subject investors are applied to satisfy RMD amounts, that early-year withdrawal will count as his RMD and affect his adjusted gross income accordingly. He can still do a QCD later that year, by steering additional funds from his account to charity (more on contributions in excess of RMDs below),

but that amount would be on top of the amount he already withdrew to satisfy his RMDs. In other words, if his goal was to align his RMD with the QCD, he blew it.

Because of that "first dollars out" rule, Slott and other tax experts urge RMD-subject IRA holders to strategize about QCDs and RMDs at the beginning of each year, before withdrawing any funds from the IRA.

**Giving More**

In addition, it's important to remember that even as QCDs can be used to satisfy RMDs, the amount available each year for QCD isn't limited by the RMD amount. Say, for example, your RMD is $10,000 but you'd like to give $15,000 in total to charity. That's permissible; you just can't exceed the $100,000 total annual limit.

Married couples filing jointly can give up to $200,000 via the QCD. Importantly, however, the QCDs would need to come from each of their respective IRA accounts (with the $100,000 limit applying to each); the full $200,000 couldn't come from one spouse's account.

It's also important to point out that even as the QCD may be particularly useful for taxpayers who aren't itemizing their deductions, because it lets them gain a tax benefit from their charitable contributions that they otherwise wouldn't be eligible for, using the QCD wouldn't automatically rule out itemizing charitable contributions, and vice versa. While any amounts gifted to charity via the QCD can't also be itemized, taxpayers may itemize additional contributions made above and beyond their QCD amounts. This strategy can be especially appropriate for large givers who are gifting to charity using highly appreciated securities in their taxable accounts, and itemizing those amounts on their tax returns, while employing the QCD with their IRAs.