Two tax-smart tips for charitable giving with an IRA

Maximize charitable impact and minimize taxes. An IRA offers a tax-advantaged way to save money over many years and have an income stream in retirement. Additionally, there are two ways you can use a taxable IRA to maximize charitable impact and minimize taxes: making qualified charitable distributions (QCDs) and naming charitable beneficiaries.

1. Give to charity during retirement years through a QCD.

Starting at age 73 the IRS mandates IRA owners to take annual income withdrawals, known as required minimum distributions (RMDs). Failure to take these withdrawals could subject IRA owners to stiff penalties.

Retirement-age individuals and couples may not want to take an RMD for various reasons. They may have other sufficient sources of income for certain years. Also, the withdrawal, which is subject to ordinary income tax, may push them into a higher tax bracket, which may have adverse impacts on Social Security payments and Medicare benefits.

Thankfully, charitably-minded individuals and couples age 70½ and older have a tax-smart strategy called a qualified charitable distribution (QCD), also known as a charitable IRA rollover. The QCD allows a donor to instruct an IRA[1] administrator to send up to $100,000 per year—all or part of the annual RMD—to one or more operating charities.[2] Couples who submit tax returns with married filing jointly status each qualify for annual QCDs of up to $100,000, for a potential total of $200,000. Starting in 2023, donors can also direct a one-time, $50,000 QCD to a charitable remainder trust or charitable gift annuity as part of recently passed SECURE Act 2.0 legislation. And starting in 2024, QCDs will be indexed for inflation. So with QCDs, more of your assets can be used to support your favorite charities that are making a difference.[3]

The IRA assets go directly to charity, so donors don't report QCDs as taxable income and don't owe any taxes on the QCD, even if they do not itemize deductions. Some donors may also find that QCDs provide greater tax savings than cash donations for which charitable tax deductions are claimed. This is because adjusted gross income (AGI) is reduced, as shown in the case study below, and AGI is used in several key calculations, such as determining the taxable portion of Social Security benefits or what deductions and credits donors qualify for receiving.

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Case study: enhancing tax savings with a QCD gift

Bob is 75 years old in 2023 and needs to take a RMD from his traditional IRA. Bob's traditional IRA is valued at $1,050,000, resulting in a projected RMD of $42,683. His ordinary income in 2023 is $80,000 and he will submit tax returns with the single filing status.

Option 1: Bob's AGI is projected to be $80,000, but if he takes his RMD income of $42,683, it will increase his AGI to $122,683. If Bob then donates his RMD income to charity, he would take an itemized deduction of $42,683, assuming he has no other deductions to itemize. This results in $80,000 in federal taxable income.

Option 2: However, if Bob instructs his IRA administrator to direct his RMD as a QCD to an eligible charity, the RMD would be excluded from Bob's taxable income. Bob then takes the standard deduction of $13,850 for 2023, plus an additional standard deduction of $1,850 because Bob is over 65 and has a single filing status. Therefore, his standard deduction totals $15,700. As a result, his federal taxable income is reduced to $64,300.

	Option 1: Take RMD income and donate cash		Option 2: Tax-smart approach—make a QCD
Bob's adjusted gross income	$122,683	VS	$80,000
Bob's charitable gift	$42,683		$42,683
Itemized or standard deduction	$42,683 itemized deduction		$15,700 standard deduction
Bob's estimated federal taxable income	**$80,000**		**$64,300**

A QCD lowers taxable income by $15,700

Note: This example is only for illustrative purposes. Both examples assume no Social Security income and that the charitable gift is to an operating charity.

2. Give beyond your lifetime by naming a donor-advised fund account or other public charity as a charitable beneficiary.

Not all assets owned are treated the same when passed to heirs. In fact, a unique feature of traditional IRAs is that heirs pay income taxes on the inherited assets at their own income tax rate at the time of withdrawal.

This unique tax feature is why public charities can be ideal beneficiaries of IRA assets. Public charities—including donor-advised funds—do not pay income tax on IRA income, which means every penny of the donation can be directed to support the donor's charitable goals.

What's more, donors can ask their advisors about using IRA assets to fund gifts, such as charitable remainder trusts, that provide income to heirs. For example, charitable remainder trusts may:

- Provide a steady stream of income for heirs
- Enable an estate to claim an estate tax deduction, if needed
- Fund a charitable legacy by naming a donor-advised fund account or other public charity as the beneficiary of trust assets

Naming a charitable beneficiary is easy to do and may result in substantial tax savings for a donor's heirs and estate.

Summary of ways you can give to charity through your IRA and other retirement accounts

<table>
<tr><th>Account type</th><th>Can you make a QCD?</th><th>Can you name a donor-advised fund or other public charity as a charitable beneficiary?</th></tr>
<tr><td>Traditional IRAs</td><td rowspan="4">Yes</td><td rowspan="4">Yes</td></tr>
<tr><td>Inherited IRAs</td></tr>
<tr><td>Inactive SEP IRA plans</td></tr>
<tr><td>Inactive SIMPLE IRA plans</td></tr>
<tr><td>Ongoing SEP IRA plans</td><td rowspan="5">No
You can roll assets into a traditional IRA and then gift to charity using a QCD</td><td rowspan="5">Yes</td></tr>
<tr><td>Ongoing SIMPLE IRA plans*</td></tr>
<tr><td>Roth IRA plans**</td></tr>
<tr><td>401(k) plans</td></tr>
<tr><td>403(b) plans</td></tr>
</table>

* Generally, contributions to SIMPLE IRAs must be held for two years before they can be rolled into a traditional IRA.

** Roth IRAs are not subject to RMDs during an accountholder's lifetime and distributions are generally tax-free and therefore there may be no tax benefit to rolling over Roth IRA distributions. Consult with your tax advisor on specifics. There may be circumstances in which a QCD can be made from a Roth IRA, so consult your tax advisor about your specific situation.

Interested in learning more?

Schwab Charitable™ has tools, information, and other resources available online to inform and guide donors throughout their philanthropic journey.

- Learn about the benefits of a Schwab Charitable donor-advised fund account
- Plan your charitable legacy using a donor-advised fund
- Join the Schwab Charitable Charitable Legacy Program, available with a Schwab Charitable account, and identify charities to support beyond lifetime
- Learn about charitable remainder trusts, charitable lead trusts, and charitable gift annuities

Donors contemplating any of the strategies in this article should consult with their financial, tax and legal advisors, and contact Schwab Charitable to discuss giving intentions.

For questions or assistance with philanthropic planning or charitable giving:

Visit
schwabcharitable.org

Call Schwab Charitable at
800-746-6216

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[1] 401(k), 403(b), and ongoing SEP or SIMPLE plans do not qualify for the QCD gift option, but assets from these accounts may be rolled over into a traditional IRA and thereafter gifted to charity using a QCD.

[2] Operating charities, or qualifying public charities, are defined by Internal Revenue Code section 170(b)(1)(A). Donor-advised funds, supporting organizations, and private foundations are not considered qualifying public charities.

[3] Donors cannot receive any benefits from making a QCD, such as courtside seats at a university's basketball game, participation in a charity auction, or payment of fees for a charity golf tournament. Donors may be able to use a QCD to fulfill a donation pledge but should consult with a tax or legal advisor on specific limitations.