If You Are Making Charitable Donations in 2018, the Same Way You Did in 2017, You Are Doing it Wrong (Part 2)

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If you are charitably inclined, you might want to think about how you give to charity in 2018, and into the future. As a result of the changes that went into effect as part of The Tax Cuts and Jobs Act (TCJA), you may not receive any tax benefit from making charitable donations. You are now much less likely to itemize your deductions due to the significantly increased standard deduction for income taxes. Last month, in Part 1 of this article, I suggested a way to obtain a tax benefit from your charitable gifts made in 2018, and future years, through stacking (or frontloading) your future charitable gifts all into one year. In this Part 2 of the article, I discuss some of the benefits that can be achieved through Qualified Charitable Distributions to charities from Individual Retirement Accounts ("IRA").

If you are over 70 ½ years of age and the owner of an IRA, you must take a required minimum distribution ("RMD") from your Traditional IRAs each year, whether you need the money or not. When you withdraw your RMD, you must report the distribution on your tax return and recognize taxable income on that amount. In years prior to 2017, if you made a charitable contribution, you could offset some of that income with a deduction for the contribution when you itemized your deductions. Many New Jersey residents took advantage of the ability to itemize their deductions, because the state and local taxes that they paid to New Jersey and their town in the form of real estate taxes were so significant that it was rather easy to achieve a greater benefit from itemizing than by simply claiming the standard deduction. The TCJA, which went into effect in 2018, changed everything, though.

In 2018 and future years, taxpayers can claim an itemized deduction for state and local taxes of up to $10,000, regardless of how much they actually pay. The standard deduction for a married couple filing a joint tax return is now $24,000 (plus $1,300 for each spouse over 65). This means that for a couple over age 65, unless you have additional itemized deductions including charitable contributions that will add up to over $16,600, you will get no benefit from itemizing your deductions. Thus, many older Americans who are required to withdraw a RMD will receive no tax benefit from the charitable contribution. Nonetheless, they will still be required to recognize the taxable income from the RMD.

So here is a tip: You should consider making a Qualified Charitable Distribution ("QCD") from the IRA directly to a public charity, which will be deemed to satisfy your RMD obligation dollar-for-dollar. This gives you the best of both worlds; you still receive the full standard deduction, but you have reduced your taxable income as the amount of the QCD is not taxable to you. The requirements for a QCD are straightforward: the donor may direct a transfer of up to $100,000 of an IRA, in any given year, to a public charity (other than a donor-advised fund). Following the QCD, the amount transferred to the charity is not included in the donor's federal taxable income and there is no charitable deduction for this amount.

So how does this work in real life? Let's assume that in 2018, John is 70 ½ years old and married to Jane (age 68). Together they have $30,000 of interest income, and John must take an RMD of $90,000 from his IRA. John and Jane always make a $10,000 contribution to their favorite charity, and their only other potential deduction is $10,000 for real estate taxes. John and his wife will claim the $26,600 standard deduction (because it exceeds their itemized deductions of $20,000) and have **$93,400 of taxable income** ($30,000 interest income plus $90,000 of RMD minus $26,600 standard deduction).

If instead, John directs the IRA trustee to transfer $10,000 of the $90,000 RMD directly to the charity as a QCD, John and Jane will have **$83,400 of taxable income** ($30,000 interest income plus $80,000 of remaining RMD minus $26,600 standard deduction). The RMD requirement will have been satisfied, the charity has still received $10,000, and John and Jane will have more money in their pocket because they will have reduced the taxable income by $10,000.

The attorneys at Einhorn Barbarito are happy to discuss this and other available tax planning opportunities that can still be employed to reduce your income tax liabilities.