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Gifts of IRAs and Other Qualified Plans

Date: January 27, 2022

Time: 1:00 – 2:30 Eastern

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Potential for Retirement Fund Gifts

Retirement assets of all types	$34.9 trillion
IRAs	$12.2 trillion
401(k) plans	$6.7 trillion

Retirement funds constitute ~35% of household wealth

12/31/2020 Investment Company Institute data

Agenda

- Retirement fund basics
- Gifts of retirement funds during life
- Gifts of retirement funds at the end of life

Types of Retirement Plans

- **Defined Benefit Plans**, Employer-funded
  - ✓ Employee receives income for life based on service
  - ✓ Traditional pension plans
  - ✓ No post-death benefit

- **Defined Contribution Plans**, Employee-funded
  - ✓ Tax-deferred contributions and investment
  - ✓ Benefit depends on contributions and investment returns
  - ✓ *Can be used for lifetime and post-death gifts*

Qualified Retirement Plans

- "Qualified" for special treatment by IRS
- Employee Retirement Income Security Act of 1974 (ERISA)
- Includes 401(k), 403(b), SEP plans, SIMPLE plans, etc.
- Traditional IRAs are not qualified plans

Qualified Plan and IRA Rules

- Withdrawals prior to 59½ subject to 10% penalty
- Withdrawals between 59½ and 72 discretionary and taxable
- At age 72, required to take traditional IRA required minimum distribution (RMD)
- Failure to take RMD subject to 50% penalty tax on the shortfall

Required Minimum Distribution

- RMDs calculated using Uniform Lifetime Distribution Table (See page 4)
  - ✓ 3.65% of the balance at age 72
  - ✓ 4.95% of the balance at age 80
  - ✓ 8.20% of the balance at age 90
  - ✓ 14.71% of the balance at age 99
- Donor may not need or want the RMD
- Donor can make a gift of RMD and offset income with deduction

Negative Impact of RMD

- Larger adjusted gross income (AGI) can lead to:
  - ✓ Increased Social Security taxes
  - ✓ Decreased Medical Expense Deductibility
  - ✓ Decreased contributions for Roth IRA
  - ✓ Increased Medicare Premiums
  - ✓ Charitable deduction limits

Gifts of Retirement Plan Withdrawals

- Withdrawals from plan subject to ordinary income tax
- Gift to charity generates income tax charitable deduction
- Deductions itemized only if they exceed standard deduction
- Deduction may not offset taxes on withdrawal

Qualified Charitable Distributions (QCD)

- QCD can only come from traditional IRA and Roth IRA
- Donor does not recognize income
- No income tax charitable deduction
- Counts toward donor’s RMD
- Does not increase donor’s AGI

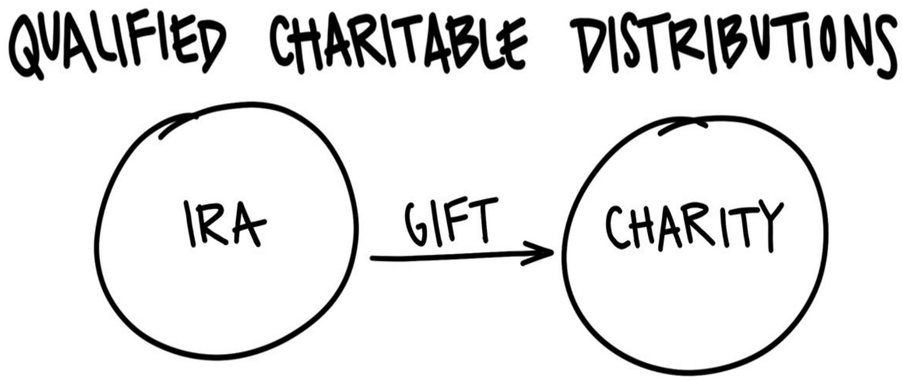
QCD Rules

- Donor must have reached 70½ birthday
- QCD would have been 100% deductible
- May not exceed $100,000 per year*
- Charity must acknowledge receipt and that no goods or services received
- QCD *can* fulfill a pledge (see IRS Notice 2007-7, Q. 44)

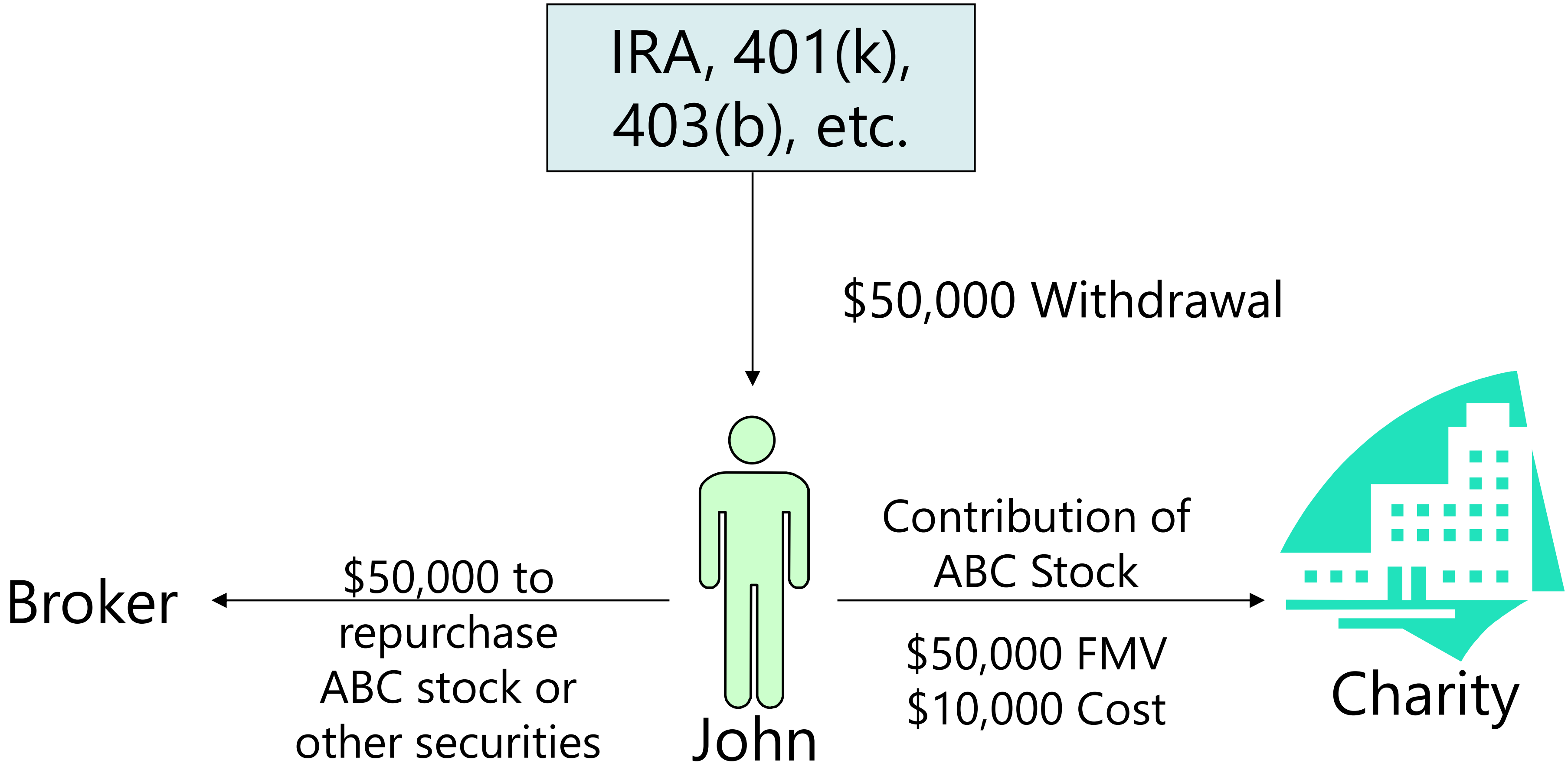
* Amount excludable from income reduced dollar-for-dollar by deductible IRA contributions made after 70 ½.

To Whom Do QCDs Appeal?

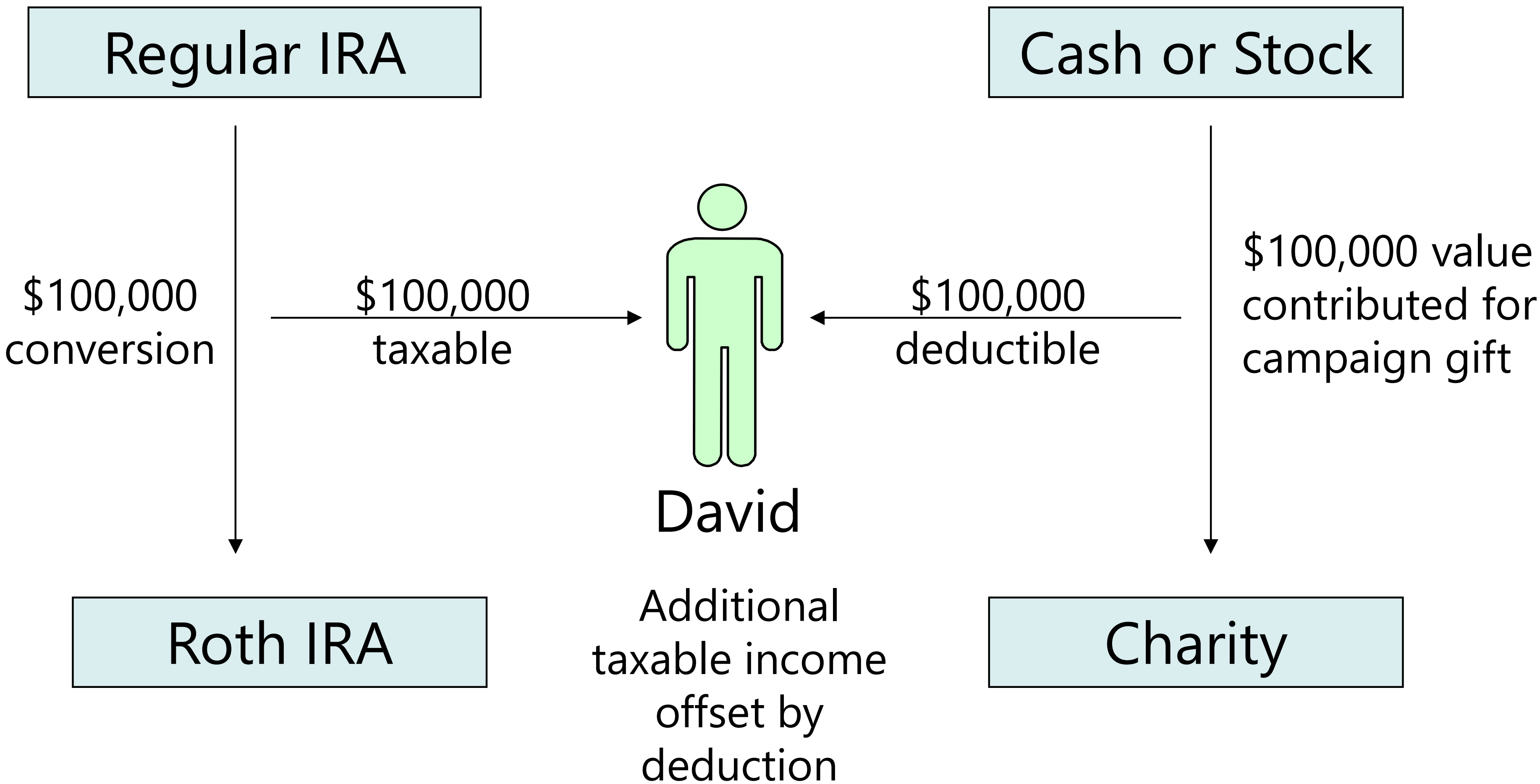
- Don’t itemize
  - ✓ Standard deduction doubled in 2018
  - ✓ Fewer than 10% of Americans itemize
- Want to reduce their AGI
  - ✓ See prior discussion of negatives of high AGI
- Live in one of the 11 states without a charitable deduction
- Like the simplicity of the QCD



Apprec. Property Gift & Retirement Fund Distribution



Combination of Gift with Roth IRA Conversion



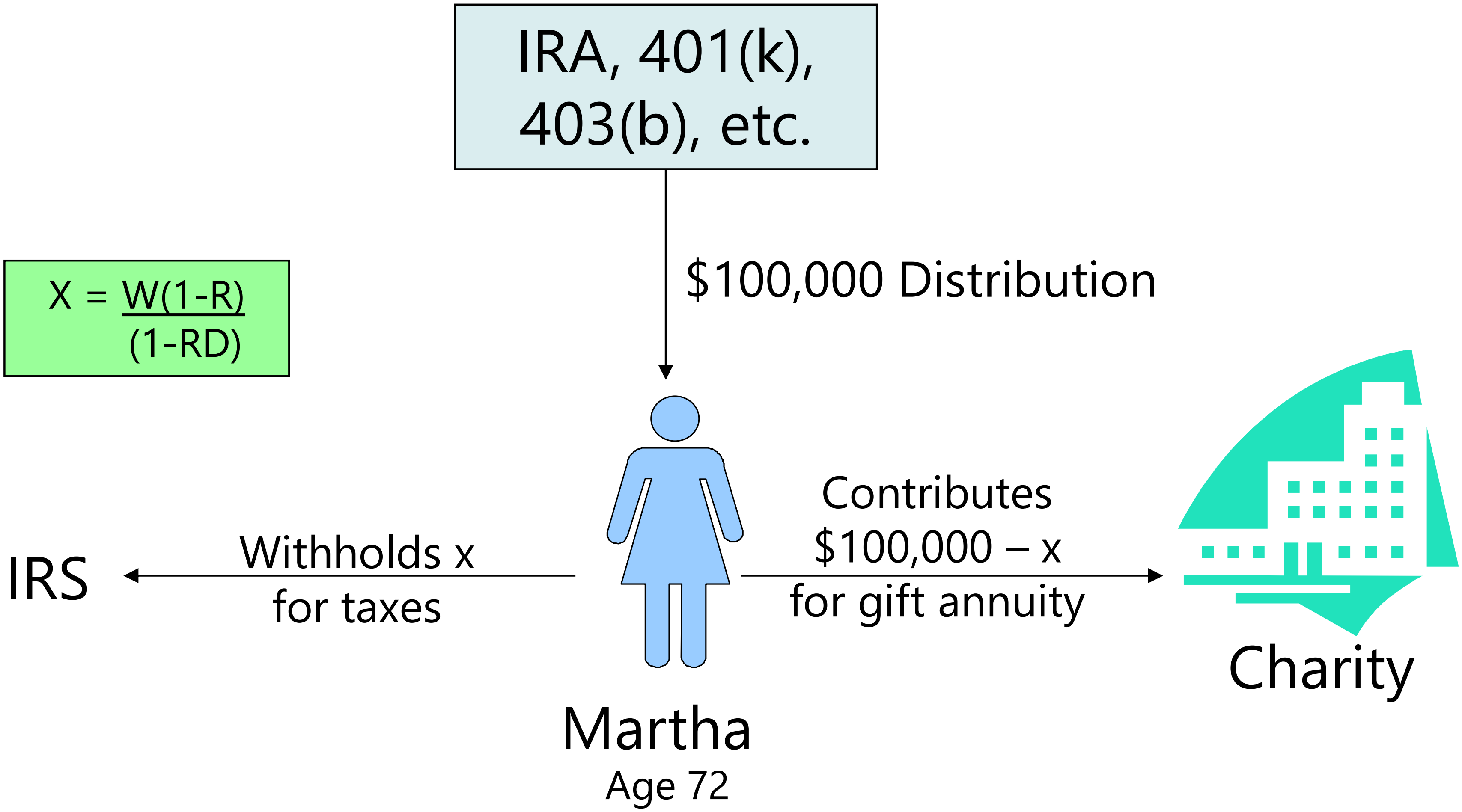
Combination of Life Income Gift with Roth Conversion

- Could work, but FMV of the asset contributed for the life income plan would have to be much more than the converted assets

  Example:

  $100,000 Roth IRA conversion
  $100,000 deduction requires $300,000 contribution to a CRT if deduction is 33.3%

Fund a CGA With a Retirement Fund Distribution



Fund a CGA With a Retirement Fund Distribution

If tax-free IRA rollover for a gift annuity were possible:

Current Law (Withdrawal, reserve portion for taxes, contribute balance)

After-tax annual cash flow for Martha	$3,883
Contribution to charity	$79,254

If Expanded IRA Rollover Enacted

After-tax annual cash flow	$3,614
Contribution to charity	$100,000

Divide IRA Into Two IRAs; Treat One Like a CGA

Brian is 73

IRA (1)
$700,000

Withdrawals as required

Brian

Children the beneficiaries

IRA (2)
$100,000

Withdrawals equal to CGA rate

$5,500/yr

Brian

Charity the beneficiary

In Summary . . .

- The QCD is beneficial to many donors and easy to market, but . . .
- There are many other attractive ways to make lifetime gifts of retirement funds, and . . .
- Unlike the QCD, they are not limited to IRAs

Testamentary Gifts of Retirement Plans

- *Most retirement plans converted to IRAs before death*
- IRAs not subject to probate
- IRAs are income in respect of a decedent (IRD)
  - ✓ IRD = income to which decedent was entitled at death
  - ✓ IRD paid to estate subject to income tax and estate tax
- IRAs left to charity bypass probate and avoid income tax

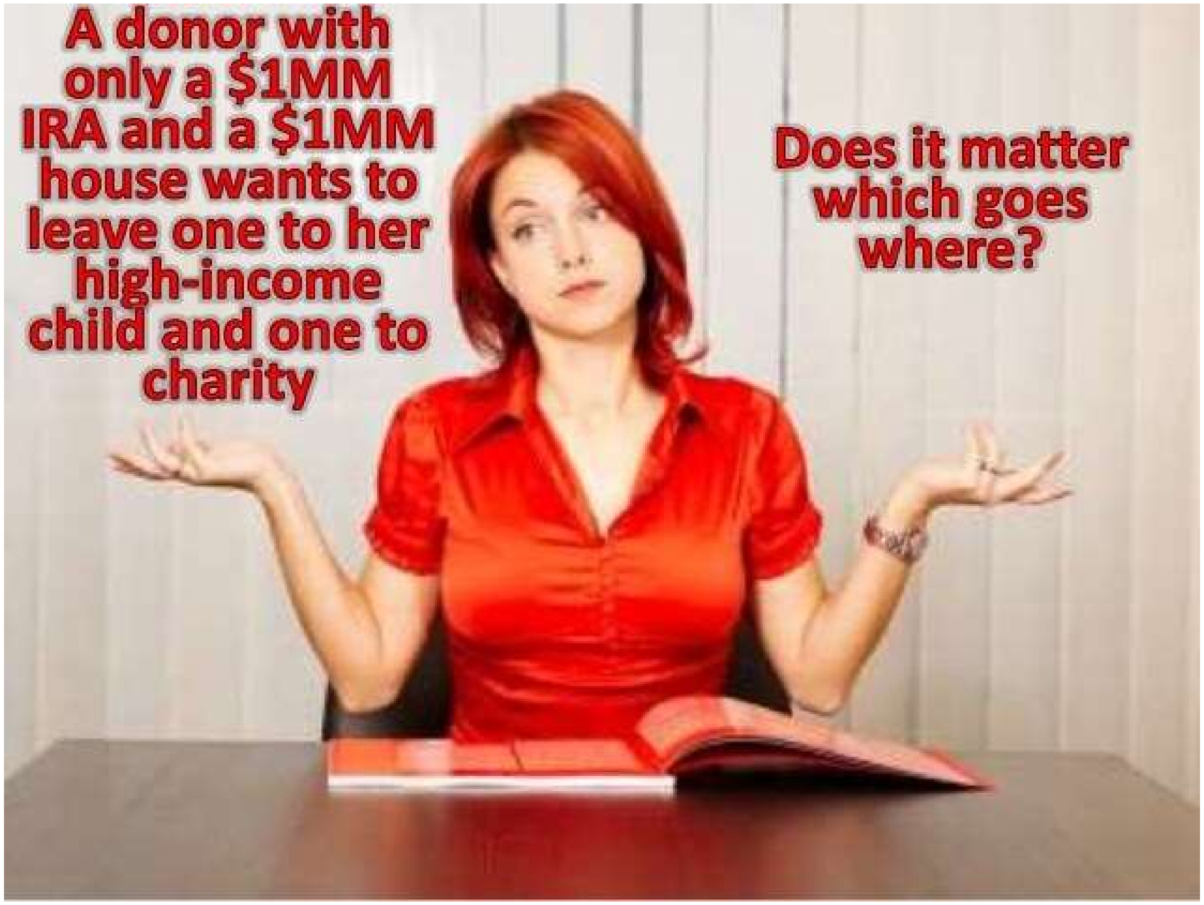
Beneficiary Designations

- IRAs (and most retirement plans) controlled by beneficiary designation form
  - ✓ Donor's estate planning documents do not control
- Donor may make charity beneficiary of some or all an IRA or other retirement plan
- Designations are by percentages, not dollar amount
  - ✓ Don't know balance in account at owner's death
- Spousal consent required for qualified plans (but not IRAs!)

Testamentary (at death) Gifts of Retirement Plans

- Qualified plans and IRAs grow tax-free
- At plan owner's death, as if donor took balance of account
- Entire account reported on owner's final tax return
- If estate is beneficiary of plan, significant taxes due
- Amounts for charity pass income tax free
  - ✓ Designation must be directly to charity
  - ✓ If paid to estate, then to charity, adverse tax situation

Does it Matter?



It Matters!

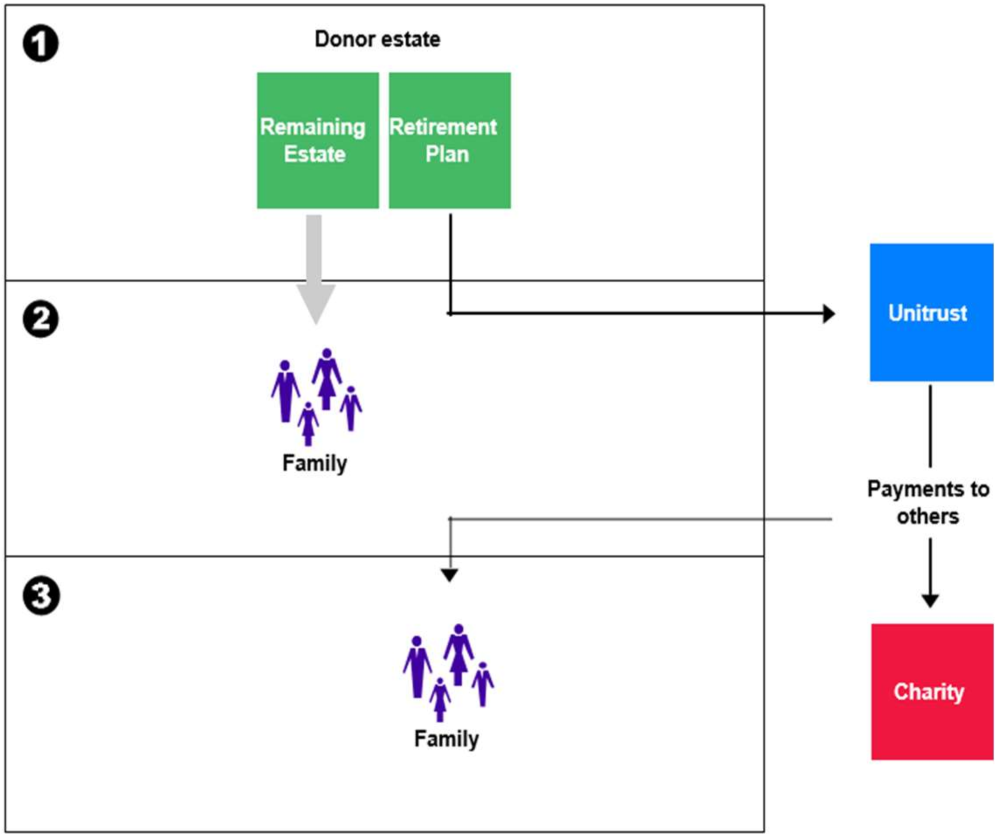
- $1M IRA to child:
  - ✓ Taxed at ordinary income tax rate
  - ✓ Assuming 37% income tax rate, $370,000 tax due
  - ✓ Net to child? $630,000
- $1M house to child:
  - ✓ Basis stepped up to date of death value
  - ✓ Child sells for $1M; taxes due = $0
  - ✓ Net to child? $1M!
- $1M to charity either way

Elimination of the Stretch IRA (Only IRAs!)

- What was a stretch IRA?
  - ✓ Tax-deferred benefits of inherited IRA to non-spouse beneficiaries
  - ✓ Inherited IRA RMDs were based on beneficiary's life expectancy-not account owner's
- Now, inherited IRA to a non-spouse more than 10 years younger:
  - ✓ Must be emptied within 10 years after death of account owner
  - ✓ More income compressed into fewer years ⟹ more tax
  - ✓ Wealthy plan owners looking for solutions

IRA Payable to Charitable Remainder Trust

- Alternative to a stretch IRA
- Payments to heirs for life (or up to 20 years)
- No income tax on IRA at death of donor
  - ✓ CRT is a tax-exempt trust



IRA Payable to Charitable Remainder Trust

- John and Marjorie, age 80 and 79
- Children, currently age 54 and 48
- Name CRUT or CRAT beneficiary of IRA
- Non-IRA assets/estate to children
- CRT funded at death of survivor of John and Marjorie
- Distributions 100% ordinary income at least until funding assets distributed
- Corrective distribution may be required
  - ✓ Property passing to CRAT at death considered one gift
- Estate tax deduction for remainder value (gift portion)

IRA Payable to Gift Annuity

- Beneficiary designation to establish CGA
  - ✓ Consider if IRA may be too small for CRT
  - ✓ May require negotiation with IRA administrator
  - ✓ Ideally CGA agreement completed during life
- Amounts distributed from IRA times annuity rate in effect at time of death
- CGA payments fully taxable as ordinary income
- Stretches out payments over life of annuitant
- Estate tax deduction for gift portion

IRA Payable to Gift Annuity

- Mona executes CGA agreement during life
- Files beneficiary designation payable to charity
- Charity to create CGA upon Mona's death for her sister
- Sister is 78 at Mona's death
- ACGA 2022 rate is 6%
- Assuming $300,000 funding, $18,000 for life to sister
- $146,772 estate tax deduction

Testamentary Solutions with Other IRD Assets

- Back up lifetime pledge to ensure balance paid at death
  - ✓ "My estate is obligated to pay the balance of my pledge…"
  - ✓ To be paid first with balance in IRA and other IRD assets
- Gifts of other IRD assets:
  - ✓ Unpaid wages
  - ✓ Unpaid dividends
  - ✓ Commercial annuities
  - ✓ Could name CRT or CGA as beneficiary of IRD assets

Collecting Retirement Plans Post-Death

- Beneficiary designations are:
  - ✓ Quick
  - ✓ Easy
  - ✓ No lawyer required (though recommended)
- IRA Administrators subject to significant regulation
  - ✓ Financial Crimes Enforcement Network (FinCEN)
  - ✓ Patriot Act
  - ✓ Financial Industry Regulation Authority (FINRA)
  - ✓ And others!!

Collecting Retirement Plans Post-Death

- IRA proceeds payable on death of account owner
- IRA administrators require IRA to pay to inherited IRA
  - ✓ Required even if charity is beneficiary
  - ✓ Charity then liquidates the inherited IRA account
- Only "individuals" may establish an IRA
  - ✓ See IRC 408(d)(3)(C)(ii)
- A charity is not an "individual"

Collecting Retirement Plans Post-Death

- Why not just set up the inherited IRA?
- Are you (or your boss) willing to provide?
  - ✓ Name
  - ✓ Home address
  - ✓ Home phone number
  - ✓ Social Security Number
  - ✓ Copy of driver's license
  - ✓ Statement of net worth

Collecting Retirement Plans Post-Death

- Possible solutions
  - ✓ Give in and fill out the forms
  - ✓ Establish inherited IRA for benefit of charity
  - ✓ Refuse to establish inherited IRA
- RIFT project (Release IRA Funds Timely)
  - ✓ See RIFT project on CGP web site
    https://charitablegiftplanners.org/ira-distribution-resource-center
  - ✓ List of cooperative IRA administrators
  - ✓ Sample letters linked to in Schultz article
  - ✓ Strategic advice

Conclusion

- Opportunities for lifetime and post-death gifts from retirement plans
- QCDs largest single opportunity for lifetime gifts
- Testamentary gifts of retirement plans are a tax-smart way to make a gift
- Use available resources to secure post-death gifts

Questions?

Still Have a Question?

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