The INVESTMENT LETTER

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"Money for nothing, and your (distributions) for free"

-Dire Straits

Many of us enjoy the benefits of an Individual Retirement Account ("IRA"), as these accounts allow a great deal of tax advantages over a long period of time. While an excellent tool to help compound growth, IRA accounts also carry with them Required Minimum Distributions at a certain age that are important to understand and manage.

Recent legislation, the Consolidated Appropriations Act of 2016, provides a tool that IRA account holders may use to realize certain tax benefits, satisfy the Required Minimum Distribution requirements, and also donate to a good, charitable cause. Specifically, the Act allows Qualified Charitable Contributions when certain conditions are met, which can be beneficial to investors with IRA accounts. It is always recommended that you consult your tax professional regarding tax implications associated with IRA accounts, but here are some points to keep in mind about the recent legislation.

Required Minimum Distributions

Required Minimum Distributions are relatively straightforward: they are the minimum amount of distributions an account holder must take from a qualified retirement account after reaching a certain age. With traditional IRA accounts, Required Minimum Distributions begin when the account holder reaches 70 ½. If the account holder does not take these Required Minimum Distributions, he or she is subject to strict tax penalties – usually to the tune of around 50% of the Required Amount!

When distributions occur from an IRA, they are treated as taxable income for that particular year. For example, say you are 72 years old and have $90,000 in income (including social security benefits) during this year. You would take your Required Minimum Distribution, which is $20,000. Your total taxable income this year would be $110,000 ($90,000 + $20,000). You are then subject to the income tax rate based on the $110,000 amount.

Many taxpayers who have IRA accounts and reach 70 ½ are in an excellent position financially and do not require the Required Minimum Distributions to maintain their lifestyle. This is great news, but it is important to keep in mind that some of your hard-earned money that you have been disciplined with over the years will be subject to an incredibly high tax rate if you do not complete the distributions. It is usually more financially prudent to figure out a smart way to use the Required Minimum Distributions rather than paying Uncle Sam a hefty sum.

Directly giving those distributions to a charitable cause, especially for individuals already making such donations, is a great way to meet the Required Minimum Distributions.

Give to a Good Cause

If you find yourself having to take Required Minimum Distributions yet do not need the funds to support your lifestyle and want to donate the distribution to a charitable cause, you could utilize the provisions of the Consolidated Appropriations Act. To do so, you must avoid acting as a "middle-man" – taking the distribution and then giving to the charitable organization. It may seem like a matter of logistics, but the logistics are important to maximize the tax benefits. Instead, you should make the contribution directly to the organization from your IRA account, as described below.

The big implication of not completing the transfer directly to the charitable organization is that the distributions will be included in the taxpayer's gross income for that year. Doing so may affect Medicare insurance premiums, income taxes on social security benefits, and even put the taxpayer into a different tax bracket altogether based on the increase. In short, these types of distributions – those not made directly to a charitable organization – do not fall within the provisions of the Consolidated Appropriations Act.

Instead, to utilize the provisions in the Consolidated Appropriations Act, you must make the transfers directly to the charitable organization from your IRA account.

Qualified Charitable Contributions

When you make the rollover directly to the charitable organization, and utilize the provisions of the Consolidated Appropriations Act, you are able to both satisfy your Required Minimum Distributions and will not be required to reduce your gross income by the amount given to the organization. This has tremendous income tax benefits, including: less restriction on Medical and miscellaneous deductions, less income taxes on social security benefits, reduced Medicare insurance premiums, less alternative minimum tax, and less State Tax. For those not necessarily requiring the distributions and who are already involved with a charitable cause, these Qualified Charitable Contributions tend to make a lot of sense.

The next step of the process is to identify the specific organization to which you would like to give the funds. The Consolidated Appropriations Act sets forth certain criteria that an organization must meet in order for the qualified Charitable Contributions to be valid. Most organizations that qualify for a charitable deduction for individual income taxes also qualify under the Act, but this is a good topic to double-check prior to making the transfer.

Last, but not least, the organization will then produce an acknowledgement of the contribution, which should be preserved by the account holder/tax professional. Without this acknowledgement, the Qualified Charitable Contribution is not valid. At this point, you have made a contribution to a charity of your choice, met your Minimum Required Distributions, and minimized taxes.

Let Us Help

At Investment Counsel, we never want our clients to feel stressed about investments – so don't go at it alone! We continually review each of our client's accounts to note any Required Minimum Distributions that should be taken given the person's age. Investment Counsel is happy to work with clients to identify possible organizations that fit the criteria under the Act. We also work with our client's tax professionals to discuss each client's specific situation with the goal of minimizing tax implication.

Should you require any opinions on your Required Minimum Distributions, or any other financial topic, please do no hesitate to contact us. While the tax law constantly evolves, there are often new legislation and tax provisions that may have a beneficial impact on investors. ■

Investment Counsel News

Inside the Office

We are currently reviewing client accounts that require Required Minimum Distributions and will be sure to contact any client if they require these distributions.

Outside the Office

Chris's daughter, Jessica (pictured right), recently traveled with her law firm to Washington D.C., where the firm represented a pro bono client before the U.S. Supreme Court.