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“Making sure we all have time to smell the roses.”<sup>™</sup>

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### **New law allows IRA owners over 70½ to donate RMD to charity**

The Pension Protection Act of 2006 allows IRA owners age 70½ or older to make direct transfers of up to \$100,000 per year from their IRA to a charity. The provision became available for IRA distributions taken after Aug. 17, 2006 and applies only through the end of 2007. Distributions can be made from taxable funds in an IRA or Roth IRA, but not from employer plans or SEP and SIMPLE IRAs. The distribution will not be taxable and there is no charitable deduction allowed on the tax return. But the provision allows those who want to contribute some of their IRA funds to a charity during their lifetime to do so without having to add the distribution amount to their income. This is better – because you do get a charitable deduction if you take the IRA withdrawal and report that amount in income. The reality, though, is that it often doesn't offset perfectly, which is why this new law is more favorable.

The direct transfer from the IRA to the charity can also satisfy a person's required minimum distribution for the year. If you are charitably inclined, it may be best to contribute from the IRA, at least up to the RMD amount thereby avoiding that amount being included in income. This will lower your adjusted gross income (AGI) and might avoid or lessen the amount of Social Security benefits that are taxed. The reduction in AGI can also increase tax deductions, exemptions or credits that are pegged to AGI either in terms of specified amounts or as a percentage of AGI. The distributions are deemed to come from income first if the IRA has non-deductible contributions. This contrasts with the normal pro-rata rule that applies to other IRA distributions where there are after-tax funds in the IRA.

If you want to take advantage of this provision for 2006, then you must make a direct IRA transfer to the charity before year end. The distribution must be made directly from the IRA custodian/trustee to the charity. It cannot be distributed to the IRA owner, who subsequently writes a check to the charity. If that is done, then the provision will not apply and the distribution will be taxable. However, you may be able to take a tax deduction for the contribution (under the regular rules that applied before this provision became effective). Finally, to qualify for this provision, you must have documentation to substantiate the donation (something in writing from the charity showing the date and amount of the contribution, and certifying that nothing of value was obtained in exchange for the contribution). It is generally a good idea to send the charity a letter notifying them of the amount of the contribution and where the contribution is coming from as well as requesting verification of receipt of the gift.

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Charities must fall under IRS code section 170(b) to be eligible. Donor advised funds, charitable remainder trusts and private foundations are ineligible. The IRS has not yet provided guidelines regarding coding for 1099 forms or 1040 reporting. Until guidelines are published, many firms are relying on advice from the Investment Company Institute. For instance, the IRA owner is responsible for maintaining documentation to verify with the IRS that requirements were met. The IRA owner is responsible for verifying the charity is a qualified charity for this purpose. The IRA owner is also responsible for verifying their compliance with the annual limit of \$100,000.

Most firms will report the distribution as a normal distribution, but will advise the IRA owner to make a note of "charitable distribution" on their records. The IRA owner must provide instructions to waive withholding since the distribution will not be taxable.

The IRA owner is responsible for any reporting the IRS requires regarding the nature of the distribution. For most securities-based accounts including mutual funds, the IRA owner must obtain a signature guarantee on the request form since the distribution is being sent to someone other than the shareowner at the address of record.

It's a good idea to consult with your financial planner before making your donation.

November 2006— This column is produced by the Financial Planning Association, the membership organization for the financial planning community, and is provided by Jim Frazin, CFP®, AIF®, a local member of FPA

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