THE PORTSMOUTH COMMUNITY FOUNDATION

CHARITABLE IRA'S FREQUENTLY ASKED QUESTIONS

Now it's easier than ever to make the gift of a lifetime
IRAs can qualify for tax-free charitable distributions

The Portsmouth Community Foundation can help turn your individual retirement accounts (IRAs) into tax-saving charitable gifts. New tax benefits allow more people to experience the joy of giving during their lifetimes.

You can give more for less - Charitable IRA

For years, estate planners have recommended that retirement assets may be the most tax-effective asset in larger estates to distribute to charity. These assets are not only vulnerable to heavy taxation as part of an estate but also can be taxed again as income in respect to a decedent on the tax returns of heirs.

Until now, there was a disincentive for retirees to give IRAs to charity during their lifetimes because withdrawals from IRAs were subject to income tax—even those given to charity.

New tax law. As of January 1, 2006, retirement assets may become a preferred charitable gift for seniors. IRA distributions to charity can now receive new tax advantages. Americans age 70½ and up can make tax-free IRA contributions to public charities such as your community foundation.

You can make a difference.

By giving through your community foundation, you can use your gift to meet ever-changing community needs—including future needs that often cannot be anticipated at the time your gift is made. Your gift can target the causes and programs you care about most.

The Portsmouth Community Foundation understands our community's most pressing issues and can help you establish a fund to make an impact in areas of need or opportunity that are important to you. Here are three great ways to turn your IRA into community good:

The Community Needs Fund—Meeting ever-changing community needs.
Address a broad range of current and future needs. The Portsmouth Community Foundation evaluates all aspects of community well-being—arts and culture, community development, education, environment, health and human services—and awards strategic grants to high-impact projects and programs.

Field of Interest Fund—Connecting personal values to high-impact opportunities.
Target gifts to the cause most important to you: arts, AIDS services, urban education, neighborhood revitalization, youth welfare and more. the Portsmouth Community Foundation awards grants to community organizations and programs addressing your special interest area.

Designated Fund—Helping local organizations sustain and grow.
Support the good work of a specific nonprofit organization—a senior center, museum or any qualifying nonprofit charitable organization—by creating a specially Designated Fund. The community foundation will invest your gift for long-term growth and issue grants to your favorite nonprofit on a regular basis.

Frequently Asked Questions - Charitable IRA

Why do donors want to give IRA assets to their community foundation?
After decades of deliberate saving and favorable investment returns, some retirees have more money in their IRAs than they'll ever need. For larger estates, a good portion of IRA wealth goes to estate taxes and income taxes of non-spousal beneficiaries; heirs may receive only 25 percent to 30 percent of IRA assets passed on to them through estates.

Instead, IRA holders may choose to leave their IRAs to qualified charitable organizations—choosing charity over taxes.

Which donors stand to benefit most from giving their IRAs to charity?
Because charitable IRA transfers are not included in taxable income and not available for itemized charitable deductions, these special rules may benefit many different types of individuals:

• High-income earners—Donors who itemize deductions may find that they cannot take full advantage of their tax deductions. Often referred to as the 3 percent floor, a taxpayer must reduce itemized deductions by 3 percent of the amount by which the taxpayer's adjusted gross income exceeds a certain amount that is adjusted annually for inflation (currently $150,500 or $75,250 each for married people filing separately). For the years 2006 and 2007, the reduction on itemized deductions for affected taxpayers is reduced by one-third.

Example: In the 2006 tax year, a married couple filing jointly has $1,000,000 in adjusted gross income (AGI). Because the couple's AGI exceeded $150,500, the phase-out rules will apply to the couple's itemized deductions. A complex formula shows that the couple's itemized deductions will be reduced by $16,990 and, as a result, the couple can claim $133,010 in itemized deductions. Presuming the couple's tax rate is 35 percent, the reduction in itemized deductions potentially results in additional taxes of approximately $5,945. (Note that this is a simplified example; please see your professional tax advisor for how it may affect you.)

• Generous donors—When making a major gift, some taxpayers may give more to charity than they can deduct that year. Donors cannot deduct more than 50 percent of their income for gifts of cash to public charities (30 percent, if giving to private foundations). Although amounts over 50 percent can be carried forward and deducted in future years, taxpayers will face an immediate tax bill and may lose some of the benefit of the deduction if they die before the gift has been fully deducted. Donors who consistently give above the limit will not be able to take advantage of the carry forward provisions.

- Non-itemizers—Donors who regularly give a portion of their income to charity are not able to enjoy a tax break from the contribution because the standard deduction is still greater than the total of all itemized deductions. This may be especially true if state and local income taxes are low.

• Financially comfortable—Individuals or couples who distribute the minimum from their IRA—and have other forms of income to pay living expenses—may find that transferring their minimum distributions to the community foundation helps fulfill personal charitable goals, tax-free.

In the past, how did the tax law treat charitable gifts made from IRAs?
Under past law, IRA holders faced a disincentive for giving retirement assets to charity during their lifetimes because all withdrawals from traditional IRAs were subject to income tax. Thanks to the new tax provision, retirees will be able to give far more support without being penalized, doing so during their lifetimes and seeing their gifts benefit their communities.

In the past, when a donor of any age withdrew IRA funds to make a charitable gift, he or she was liable to pay income tax on the withdrawal, offset to varying degrees by a charitable deduction for the gift. (Charitable deductions are limited by legal restrictions, such as the percentage of adjusted gross income [AGI] limitation on charitable deductions and the 3 percent floor on all itemized deductions. If an individual does not itemize on his or her income tax return, no charitable deduction can be taken.)

As a consequence of this unfavorable tax treatment, very few individuals donated IRA funds to charity during their lifetimes.

How has the tax law changed?
The Pension Protection Act of 2006 permits individuals to transfer up to $100,000 from individual retirement accounts directly to a qualifying charity without recognizing the assets transferred as income for federal tax purposes. In tax years beginning after December 31, 2005, a donor who has reached age 70½ is now allowed to exclude from his or her income tax calculations certain IRA withdrawals. In most circumstances, these charitable contributions are not tax deductible unless the retirement accounts were funded with after-tax dollars.

This provision is time-limited. It will not apply to any distribution made in taxable years beginning after December 31, 2007.

What are the advantages of this new law?
The tax benefits now available to American seniors will encourage new contributions from individuals who will no longer have to pay tax on a charitable gift of IRA funds. When given through a community foundation, these contributions can support all aspects of community well-being: arts and culture, economic development, education, environment, health and human services, neighborhood revitalization and more.

Now it is easier than ever for more people to enjoy the experience of making the tax-free gift of a lifetime using their excess retirement assets.

What if a donor contributes more than $100,000 from an IRA?
Because the amount that the donor is able to exclude from income is limited to $100,000 under the act, the remaining amount would be recognized as income. Within a married couple, each person can transfer $100,000 from his or her account. A $100,000 charitable distribution may be made in 2006 and again in 2007.

Donors may choose to contribute additional amounts to charity; however, the extent to which additional amounts can be deducted from their income will be determined following general rules of itemized deductions where the charitable percentage limitations and itemized deduction reduction are factors.

Does a donor also receive a charitable deduction when he or she transfers assets to a charity under this provision?
No. The benefit under this provision is that the individual does not realize the amount contributed directly from the IRA to a qualifying charity. Because a donor does not include the amount in his or her gross income, the individual may not take a charitable contribution deduction for the contribution. To do so would allow a donor to receive a double benefit from the contribution. For this reason, charitable contribution deductions are explicitly prohibited.

How will charitable distributions affect the minimum required distributions from a taxpayer's IRA?
Shortly after an individual reaches age 70½, he or she is generally required to receive distributions from his or her traditional IRA. Distributions from an IRA to a charity will receive the same treatment as distributions to the individual taxpayer for the purposes of minimum required distributions.

Are there any IRA transfers to the community foundation that do not qualify for preferred tax treatment?
Yes. Transfers to Supporting Organizations and Donor Advised Funds do not qualify. In addition, split interest gifts, such as Charitable Annuities, Charitable Lead Trusts and Charitable Remainder Trusts, do not qualify. Further, an individual may not receive a benefit in return for an IRA distribution.

Because such transfers do not count as qualified distributions under these special rules, the donor will have to first recognize those distributions as income. The donor's charitable deduction must then be calculated as a regular itemized deduction.

How can an IRA gift be made?
IRAs are typically held by a financial service or trust company. These custodians will likely provide a form that could be used to transfer the IRA directly to charity, with no tax incurred.

The information provided here is based on continuing analysis of the Pension Protection Act of 2006. Every effort has been made to ensure accuracy of the answers to these questions. However, due to the complexity of the bill and the fact that many of these provisions introduce issues that are new to the Internal Revenue Code, this information may be subject to change. It is not a substitute for expert legal, tax or other professional counsel and we strongly encourage donors to work with their professional advisors to determine the impact of this legislation on their particular situations. This information may not be relied upon for the purposes of avoiding any penalties that may be imposed under the Internal Revenue Code.