



## **SPECIAL OPPORTUNITY FOR CHARITABLE CONTRIBUTIONS OF IRA FUNDS BY INDIVIDUALS IN 2005**

The Hurricane Katrina Relief Act (HKR) contains several provisions that make qualifying cash gifts to charitable organizations of significant economic advantage to donors. Since a gift of funds from an IRA or other qualified plan is considered to be a gift of cash, there is now an opportunity under HKR to make unlimited tax-free gifts to charity. The gifts do not have to be restricted for Hurricane Katrina relief.

**This opportunity is available for individuals who make cash contributions to public charities between August 28 and December 31, 2005.** This 100% deductible gifts rule does not apply to cash gifts by individuals to private foundations, supporting organizations or donor advised funds and does not apply to gifts of property such as stock or real estate.

The amount of cash that an individual contributes from an IRA or from other cash assets may be unlimited.

How does this affect IRA gifts?

Under current law (before HKR), an individual over the age of 59 ½ could make a gift of IRA funds to a public charity but was required to include the withdrawal from the IRA as ordinary taxable income in the year distributed. In addition, the deduction of any gift of cash to a public charity was limited to 50% of the taxpayer's adjusted gross income (AGI), with carry forward for up to five years of amounts in excess of the 50% limitation, and was subject to reduction of the itemized deduction by the 3% "floor." Under HKR, neither the 3% "floor" nor the AGI deduction limit will be applicable. The "floor" will not be lifted by the charitable contribution; thus, the deductible amount of other items such as medical or casualty deductions will not be affected by the amount of cash contributions. Also, there will no longer be the "50% of AGI" limitation under U.S. tax rules although there may still be some limitations under the tax laws of certain states.

### Examples

- I. Martin and Rachel, husband and wife both over age 60, file their individual income tax return jointly. They regularly make and deduct charitable contributions to public charities. They expect to have \$100,000 in adjusted gross income for 2005. They decide to make a major gift to a particular charity before the end of 2005 by withdrawing \$100,000 from Martin's IRA. By withdrawing the \$100,000 from the IRA, their income for tax purposes is increased to \$200,000. They deduct the \$100,000 contribution amount withdrawn from the IRA as an itemized charitable deduction, thereby reducing their income for tax purposes to the original \$100,000 (before other deductions and credits). Thus, they will have paid no tax on the IRA funds used for charitable purposes since 100% of the cash gift is deductible against income.
- II. Jacob has a substantial IRA that may be subject to considerable taxes at the end of his lifetime. He had considered making charitable gifts from his IRA over the years but found it too costly since he

would have had to include the withdrawals from his IRA as ordinary taxable income in the years distributed and his charitable deductions would have been limited by the 50% of AGI rule. He desires to establish an endowment or special fund at a public charity he regularly supports. His income this year is expected to be around \$125,000. Jacob withdraws \$250,000 from his IRA and distributes the full amount to his favorite public charity. That distribution increases his income for the year to \$375,000. He is entitled to deduct the entire IRA payment to charity as an itemized charitable deduction, reducing his income back to \$125,000. He has also eliminated the estate and income taxes that the \$250,000 in his IRA would have been exposed to at the end of his lifetime.

- III. Miriam has made a pledge to a public charity's capital campaign. She had planned to pay the pledge in equal installments over five years. She decides to withdraw the full amount of her pledge from her IRA before the end of the year and distribute that amount to the charity to retire the pledge. Assume that the amount withdrawn and distributed from the IRA was \$500,000, Miriam will be able to deduct that full amount from income (increased by the distribution amount) and have no income tax obligations for the distribution. In addition, Miriam has removed \$500,000 in IRA funds from her estate and eliminated any estate or income taxes that might have been due at the end of her lifetime.
- IV. Sam makes regular major annual gifts to a public charity in the amount of \$25,000 each year. He wants to take advantage of the new short-term benefits under The Hurricane Katrina Relief Act and accelerate his giving before the end of 2005. Sam withdraws \$100,000 from his IRA and distributes it to the charity to pay his commitment for 2005 and to pre-pay his gifts for the following four years. The withdrawal from Sam's IRA will be free of income taxes, and Sam will have continued with his long-term support of the charity.

For individuals over age 59 ½ with assets in qualified retirement plans, tax-sheltered annuities ("a 403(b) annuity"), eligible deferred compensation plans maintained by a State or local government (a "governmental 457 plan") or in individual retirement arrangements (an "IRA"), the best strategy may be to withdraw the amount intended to be distributed to charity before the end of 2005 and make an eligible rollover distribution within 60 days to another IRA (a qualified rollover). It will be from the rollover IRA that the distribution will be made to charity before December 31, 2005. Nevertheless, the distribution may be made directly to charity without using the rollover IRA at the option of the taxpayer-donor.

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### **THE HURRICANE KATRINE RELIEF ACT OF 2005**

#### **BEFORE HKR**

IRA withdrawals included as ordinary income

Deduction of IRA distribution to public charity limited to 50% of adjusted gross income

Itemized cash charitable deductions subject to 3% deduction "floor"

#### **AFTER HKR**

IRA withdrawals included as ordinary income.

Deduction of IRA distribution to public charity unlimited.

Itemized cash charitable deductions not included in 3% deduction "floor"