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Dec. 26, 2014

[This is the first in a series of articles on tax breaks temporarily extended by tax legislation late in 2014.]

The time for clients to take required minimum distributions from their IRAs is rapidly dwindling. They have until December 31, 2014 to arrange for an RMD for the 2014 tax year. Otherwise, they could be slapped with a stiff tax penalty.

But now there's another option to consider. Thanks to a new tax law temporarily extending a slew of expired tax provisions – the Tax Increase Protection Act of 2014 – clients who are older than age 70½ can directly transfer amounts from their IRAs to charity without paying a plugged nickel of tax. Barring any subsequent legislation, this unique tax break expires again after December 31, 2014. Its future fate remains uncertain.

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The IRS explains the rules for IRA transfers to charity in 2014 in a news release issued just after the Tax Increase Prevention Act was signed into law (IR-2014-117, 12/23/14).

Here's a recap of the main rules: After a client reaches age 70 ½, he or she must begin

distributions from an IRA of up to $100,000 in 2014. Thus, a married couple can transfer a total of up to $200,000 tax-free before 2015 if they each have one or more IRAs in their own name. The distribution isn't reported as taxable income nor is it treated as a deductible charitable contribution on your 2014 tax return. In effect, it's a wash.

Note that the distribution must otherwise qualify as a charitable donation. For example, if the deduction would be reduced if you receive a benefit in return or the contribution isn't properly substantiated under the charitable deduction rules, the exclusion isn't available for any part of the IRA distribution. Furthermore, donations must be made directly from the IRA to the charity; you can't use the money in the interim.

Significantly, the distribution from an IRA counts as an RMD even if it goes immediately to a charity. This can satisfy a client's year-end obligation at the same time he or she is supporting a favorite cause. The IRA-to-charity transfer may also provide other tax-related benefits, depending on the client's situation (e.g., reducing AGI for other purposes).

Finally, be aware that this extended provision is available for Roth IRAs as well as traditional IRAs, but it usually makes more sense to use a traditional IRA if you have a choice. With a Roth IRA in existence at least five years, qualified distributions –such as those made after age 59 ½ — are completely tax-free anyway. Plus, you're not required to take lifetime RMDs from a Roth like you are with a traditional IRA.

Don't let your retired clients miss this deadline. Make sure they understand all their options, including transferring IRA funds directly to charity, during the last few days of the year.

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