



Understanding the Hidden Tax Benefits of Using the Qualified Charitable Deduction

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Harold Thompson, an 82-year-old retired teacher, sat at his kitchen table, reviewing his financial statements. His Required Minimum Distribution (RMD) from his IRA had arrived, and he knew it would push his taxable income higher than he wanted. Harold had lived modestly and had more than enough for his needs. What he truly cared about was ensuring his legacy supported the causes closest to his heart.

That's when he remembered his professional advisor mentioning the **Qualified Charitable Distribution (QCD)**. Instead of taking his RMD as income—and paying taxes on it—he could **directly donate up to \$100,000** to a qualified charity, tax-free. Excited, he called his alma mater's scholarship fund and arranged for a **\$15,000 QCD**, ensuring a new generation of students could afford college.

A month later, he received a heartfelt letter from a young woman named Sarah, a first-generation college student, thanking him for his generosity. Tears welled in Harold's eyes. Not only had he reduced his tax burden, but he had also **changed a life**.

That year, Harold's Christmas card list grew by one name—Sarah's. And he knew, for as long as he lived, his **charitable giving** would remain **his greatest investment**.

At this point, you may be asking where the novel tax planning tool has been all my life?

Factoid: In 2023, charitable giving in the United States reached an estimated **\$557.16 billion**, marking a 1.9% increase in current dollars compared to 2022. However, when adjusted for inflation, this represents a **2.1% decline**.

The **Qualified Charitable Distribution (QCD) law** was first introduced after Congress allowed IRA owners to donate directly from their IRAs to worthy charities after Hurricane Katrina struck the Gulf Coast in August 2005. The following year, it was made part of the **Pension Protection Act of 2006** (PPA 2006). This allowed individuals aged **70½ or older** to make direct tax-free charitable donations of up to **\$100,000 per year** from their **IRA** to a qualified charity.

Originally, this provision was set to expire, but Congress extended it multiple times before making it **permanent in 2015** under the **Protecting Americans from Tax Hikes (PATH) Act**.

Since then, adjustments have been made, including indexing the QCD limit for inflation starting in 2024 under **SECURE 2.0 Act of 2022** (finalized into law in 2024). For 2026, the QCD limit per donor is \$111,000.00.

For those over the age of 70 ½ years of age, using the QCD strategy may be a better use of your funds to support your worthy causes. Let me explain “WHY” this may be better for most seniors.

Key Features of a QCD:

1. **Tax-Free Distribution** – The amount transferred to the charity **does not count as taxable income**, unlike a normal IRA withdrawal.
2. **Counts Toward RMD** – If the donor is **73 or older**, the QCD satisfies all or part of their Required Minimum Distribution (RMD).
3. **Annual Limit** – The maximum **QCD amount per person per year is \$111,000** (adjusted for inflation starting in 2026).
4. **Direct Transfer Required** – The funds **must** be transferred directly from the IRA custodian to qualifying charity. If the IRA owner withdraws the funds first, it becomes taxable income.
5. **Eligible Charities** – The recipient must be a **501(c)(3) public charity**. *Donor-Advised Funds (DAFs), private foundations, and supporting organizations do not qualify.*
6. **No Additional Charitable Deduction** – Because the QCD is excluded from taxable income, you **cannot** also claim it as an itemized charitable deduction.

Why Use a QCD?

- **Lowers Adjusted Gross Income (AGI)** – This can help avoid phaseouts of tax deductions, Medicare surcharges, and Social Security taxation.
- **Ideal for Non-Itemizers** – Since the QCD excludes the gift from taxable income, it provides a tax benefit even for those who take the standard deduction.
- **Maximizes Charitable Impact** – The full amount goes to charity tax-free, rather than being reduced by income tax.

As you know, when you make a gift to a charitable foundation approved by the US Treasury (see IRS Publication 78 for a list of approved charities), you are eligible to claim that gift as a charitable deduction. As an example, we will use a single person who made charitable gifts totaling \$5,000.00 to their worthy charities in 2025. When tax season arrives, you give the donation letters from the charities you supported to your tax professional expecting them to include those donations onto our tax return, specifically Form 1040 or 1040-SR, Schedule A.

The question for this taxpayer / donor becomes, how much did the \$5,000.00 donation reduce his or her tax liability? Sadly, the answer is ZERO.

Let’s review the facts. By default, you may elect to use the IRS Standard Deduction as a single filer of \$15,000.00 (\$30,000.00 Joint) for 2025 or the total amount from Schedule A. In this case, Schedule A, the Itemized Deductions were \$5,000.00. You have the right to use either Schedule A or the standard deduction, but the bulk of taxpayers will elect the higher of the two to capture the maximum tax benefit. If you have other qualifying deductions to increase your Schedule A to a value greater than \$15,000.00, only then your charitable gift has helped reduce your tax liability for that year.

Knowing the above, let's take another look at Harold Thompson's method of charitable giving. In his case, because he is over age 73, he is required to take a Required Minimum Distribution by the end of the year. Harold has \$275,000.00 in his Traditional IRA. Therefore, he (at age 82) is required to take an RMD of \$14,864.86 by the end of 2025. Whether he wants or needs the RMD, the IRA Custodian, absent other directions, shall send him a taxable distribution.

If Harold takes the RMD, it will be added to his overall income reporting for 2025 and pay tax based on his new, adjusted taxable income. If Harold makes a charitable gift from his checking account of the same amount, \$14,864.86, he will be entitled to report a 2025 charitable income tax deduction for that amount. If \$14,864.86 is the sole entry on Schedule A, Harold would be wise to claim the \$15,000.00 Standard Deduction to minimize his tax due. On the surface, a person not trained in tax might wrongfully assume there is no difference in this exercise, but read on.

Harold leveraged several tax benefits by informing his IRA Custodian to gift funds directly from his IRA straight to his favorite charity. First, by directing the RMD amount to charity, he did not take receipt of the funds as ordinary income. As such, it should not push him into a higher income tax bracket. Second, his IRA grows compound tax deferred. Therefore, growth recovery to replace the value donated is faster in his IRA than growth recovery in his non-qualified accounts (everything being equal). Next, since his IRA upon his death will be transferred to his heirs as taxable income, by using the QCD model of giving untaxed funds from his IRA, his non-qualified asset funds should increase (eventually transferring tax free to heirs) and his IRA account should be smaller, thus less tax for his heirs when they inherit his IRA.

*Factoid: In 2017, approximately 31% of U.S. individual income tax returns included Schedule A for itemized deductions. However, following the **Tax Cuts and Jobs Act (TCJA) of 2017**, which significantly increased the standard deduction and limited certain itemized deductions, this percentage dropped notably. By 2020, only about 9% of taxpayers chose to itemize deductions.*

Authors Note: This clearly supports the notion we Americans donate to worthy charitable causes, whether we enjoy a tax deduction or not!

If Howard lives another 10 years, by using the QCD strategy, he will significantly increase the value of his gifts and increase the tax smart wealth transfer to his heirs.

In Review. A Qualified Charitable Distribution (QCD) is a strategic financial tool used in charitable giving. It allows individuals aged 70½ and older to donate directly from their IRAs. The donation goes to a qualified charity like your church, hospital, universities, or charities listed on IRS Publication 78 (your RMD cannot go to a Donor Advised Fund, Supporting Organization or Private Foundations).

QCDs provide a way for retirees to fulfill their charitable goals tax efficiently. This strategy will help donors meet their Required Minimum Distributions (RMDs) without the tax burdens typically involved. This can make charitable giving more tax-efficient for many individuals.

By giving directly from an IRA, a QCD keeps the distribution amount from increasing taxable income. This can be especially beneficial in maintaining a lower tax bracket. It also helps avoid higher taxes on Social Security benefits.

QCDs do not impact Itemized Deductions (Schedule A). This makes the QCD a valuable option for those who do not itemize. However, they must follow specific rules and limitations. You MUST coordinate with your IRA Custodian, preferably not less than three months before the end of the tax year.

Without question, this giving model has been legal since 2006, about twenty years ago. So yes, this strategy is not well known by all the professional advisors in the country. If your professional advisor(s) are unaware of this powerful strategy, provide them with a copy of this book. If you are over age 70 ½ and plan to gift less than \$111,000.00 a year to worthy public charities, your professional advisor will be hard pressed to optimize your gifting in another manner.

Understanding what a QCD is can open doors to more strategic giving. This can enhance not only your financial standing but also your philanthropic impact.

Factoid: What is the Source of Charitable Dollars?

- **Individuals:** \$374.40 billion (67% of total giving), a 1.6% increase in current dollars but a 2.4% decrease when adjusted for inflation.
- **Foundations:** \$103.53 billion (18% of total giving), up 1.7% in current dollars but down 2.3% with inflation adjustment.
- **Bequests:** \$42.68 billion (8% of total giving), showing a 4.8% rise in current dollars and remaining relatively flat (0.6% increase) after inflation adjustment.
- **Corporations:** \$36.55 billion (7% of total giving), a 3.0% increase in current dollars but a 1.1% decrease when adjusted for inflation.

State Tax Impact

There are at least three different categories of states with respect to the charitable IRA rollover. First, some states do not presently provide charitable income tax deductions. In Indiana, Ohio, Massachusetts, Connecticut, Illinois, Pennsylvania, and Wisconsin, there are no state charitable itemized deductions. Therefore, donors will effectively benefit from the IRA rollover by reducing their state taxable income and reducing their state taxes. Both these donors and federal nonitemizer donors benefit directly by making charitable gifts from their IRAs.

Second, some states permit charitable deductions but use the federal adjusted gross income as an initial reference number for determining state tax. In this circumstance, the reduced adjusted gross income because of the charitable IRA rollover will also reduce state taxes. For example, the California Franchise Tax Board website states that "Taxpayers may now exclude up to \$111,000 in 'qualified charitable distributions' from their adjusted gross income for both federal

and state purposes. To qualify, the distribution must be made directly by the IRA trustee to a charitable organization after the taxpayer reaches age 70½."

Finally, there may be some states in which the state does not recognize the IRA charitable rollover and requires IRA reporting for state income tax purposes. In those states, the distribution to charity would normally be deductible on state income tax returns, but may be subject to state limits, such as the 60% of adjusted gross income limit for charitable gifts in one year. New Jersey does not recognize the IRA rollover, but because it also does not permit most charitable deductions, the IRA rollover will increase state income tax.

IRA Rollover Gifts Not Permitted

There are a few restrictions on the "qualified charitable distribution" (QCD). The QCD may not be made to a supporting organization (SO) or to a donor advised fund (DAF). Since the QCD rollover is limited to organizations in private foundations are also excluded, apart from the conduit private foundation.

Finally, the "entire distribution" transferred to the charity must qualify for a charitable deduction. Therefore, a "quid pro quo" transfer is not permitted. The QCD may not be used to purchase a banquet table for a donor, family and friends at the annual charitable auction. Similarly, the gift may not be used to qualify for preferential seating at athletic events or other types of "quid pro quo" gifts.

Author Notes:

I strongly recommend the use of a professional advisor when using the QCD strategy. This is a simple way to donate with improved tax efficiency - provided the process is properly executed in the appropriate manner and timely executed.

Books by Edward W. Cotney

Tax Secrets Made Simple

The Great IRA Tax Grab (Private Distribution)

The Business Owners Guide to Tax Freedom

The Business Owners Guide to Selling Your Business Tax Smart

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