Charitable IRA Maximization

WHAT IS CHARITABLE IRA MAXIMIZATION?

Many affluent individuals own IRA accounts that aren't needed for retirement income. IRAs with large account balances could see a reduction in value upon the owner's death, due to estate and income taxes, of 70 – 85 percent of the IRA balance. Often, these wealthy individuals have significant charitable interests that may include current/deferred charitable gifting. By bequeathing their IRA to a charitable organization, their estate receives a full estate tax deduction for the charitable bequest and the charity doesn't report "income in respect of a decedent" (IRD), thus eliminating both estate and income taxes on the IRA.

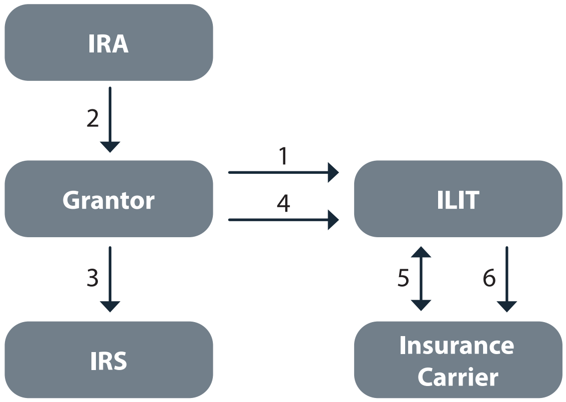
Since the IRA owner will continue to own the account until death, required minimum distributions (RMDs) must be distributed to the IRA owner beginning at age 70½. These RMDs could be used to do either of the following:

- To fund life insurance owned outside of the taxable estate, in order to replace the value of the IRA for heirs.
- To make current tax-deductible gifts to a charitable organization. An IRA owner can make up to a $100,000 annual charitable distribution directly from their IRA to a charitable organization without including the distribution in income. The charitable distribution is credited against the IRA owner's RMD, and because the charitable rollover completely avoids the donor's tax return, the donor can effectively get both their standard deduction and the charitable contribution deduction without any AGI limitation. Additionally, the proceeds could be used to purchase life insurance on the donor(s), further enhancing the benefit to charity.

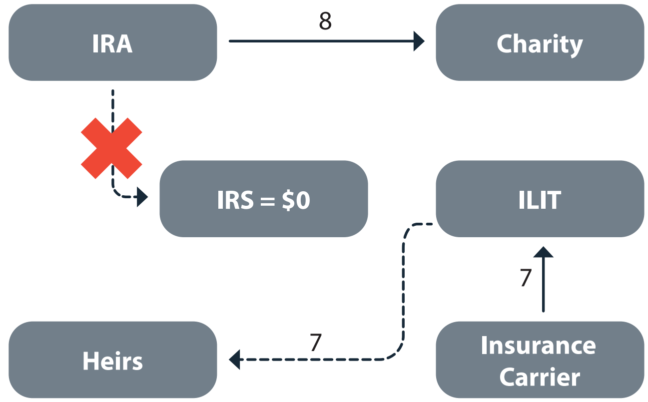
HOW DOES IT WORK?

The IRA owner takes income from the IRA by taking the required withdrawals (or an additional amount). Income tax is paid on the withdrawals and the after tax proceeds are then gifted to an irrevocable life insurance trust (ILIT) to fund a life insurance policy. The ILIT will receive a tax-free death benefit upon the death of the insured(s). The IRA is left to charity upon the owner's death.

Now:



In the Future:



1. Grantor creates an ILIT.
2. Grantor receives distributions from IRA.
3. Grantor pays income taxes on IRA distributions.
4. Grantor gifts after-tax proceeds to ILIT.
5. ILIT applies for life insurance on the life of the grantor(s).
6. ILIT pays annual premiums to insurance carrier.
7. At death of the insured(s), ILIT receives life insurance death benefit estate and income tax-free for the benefit of heirs, replacing the value of the IRA.
8. IRA is left to charity, eliminating estate and income taxes on the account value.

ADVANTAGES

- **Elimination of IRA Tax Inefficiencies –** Charitable bequests are fully deductible from the taxable estate, and charitable organizations don't pay IRD taxes.
- **Potential Leverage –** Purchasing life insurance can potentially replace the IRA account value left to charity for heirs or increase the benefit to charity.
- **Income Tax Advantages –** In general, life insurance cash values grow on a tax-deferred basis and the proceeds are received income-tax free.
- **Estate Tax Advantages –** If the life insurance is purchased in a properly drafted ILIT, the proceeds are generally received estate tax free.
- **Creditor Protection –** Depending on the state, life insurance can offer creditor protection.

DISADVANTAGES

- **Tax Implications –** Income taxes are incurred on withdrawals taken from the IRA, unless distributions ($100,000 annual maximum) are made directly to a charitable organization.
- **Early Withdrawal Tax –** Where the owner is younger than age 59½, they must take substantially equal periodic payments to avoid the 10 percent early withdrawal penalty tax.
- **Impact on Plan Balance –** Withdrawals greater than the required minimum distribution (RMD) may reduce the overall value of the IRA.
- **Additional Costs –** Life insurance policies have charges associated with them, such as the cost of insurance and potential surrender charges.

THE BOTTOM LINE

Charitable IRA maximization converts a tax-inefficient IRA into a significant charitable legacy and, by using a tax-efficient life insurance death benefit, may potentially increase the amount left to heirs or to charity.

This material was created by NFP Corp., its subsidiaries or affiliates for distribution by registered representatives, investment adviser representatives and/or agents. This material was created to provide accurate and reliable information on the subjects covered. It is not intended to provide specific legal, tax or other professional advice. The services of an appropriate professional should be sought regarding your individual situation.

Securities may be offered through Kestra Investment Services, LLC (Kestra IS), Member FINRA/SIPC. Investment Advisory Services offered through Kestra Advisory Services, (Kestra AS), an affiliate of Kestra IS. PartnersFinancial is a platform of NFP Insurance Services and is not affiliated with Kestra IS or Kestra AS. Kestra IS and Kestra AS are not affiliated with NFP Corp. and may not be affiliated with the firm branded on this material.

266814 | 05/20 | 17-PCR-LIFE-PC-0930 | Copyright © 2020 NFP. All rights reserved.