

MEMORANDUM

TO: ██████████
FROM: Lora Bishop
DATE: September 27, 2023
RE: Overview – IRA-funded Charitable Gift Annuities

QUESTION PRESENTED

Is the donation of funds from an IRA account for the purpose of establishing a charitable gift annuity strictly an IRA issue where federal laws apply, or does Alabama tax law apply for people residing in the state?

BRIEF ANSWER

Federal tax law governs an IRA-funded charitable gift annuity under the new 2023 SECURE Act 2.0, which can be found in the Internal Revenue Code of 1986 in Title 26, section 408(8)(F)(i-v) of the United States Code. However, Alabama is one of nine “registration states” that regulate the issuance of charitable gift annuity contracts from charities to the donor. These requirements that an eligible charity must meet can be found on the Alabama Securities Commission website under the “For Industry” and “Alabama Filing Requirements” tab.¹

DISCUSSION

- I. Background – The new Secure Act 2.0 authorizes the donation of up to \$50,000 from the IRA account of a person 70 and a half years or older.**

¹ Those tabs can be accessed here: <https://asc.alabama.gov/>

Section 310 of House Resolution 2954 proposed a “one time election for [a] qualified charitable distribution to [a] split-interest entity[, and an] increase in qualified charitable distribution limitation[s].”² The purpose of the bill, introduced to the House floor on May 4, 2021, was to “increase retirement savings [and] simplify and clarify retirement plan rules.”³ The act was cited as the “Securing a Strong Retirement Act of 2022,” better known as the “SECURE Act 2.0” (Setting Every Community Up for Retirement Enhancement).⁴

This proposal, starting on page 93 of a 139-page resolution, amended Section 408(d)(8) of the Internal Revenue Code of 1986 by adding a new subparagraph (F) at the end that states:

In general – A taxpayer may for a taxable year elect under this subparagraph to treat as meeting the requirement of subparagraph (B)(i) any distribution from an individual retirement account which is made directly by the trustee to a split-interest entity, but only if . . . an election is not in effect under this subparagraph for a preceding year, the aggregate amount of distributions of the taxpayer with respect to which an election under this subparagraph is made does not exceed \$50,000, and such distribution meet the requirements of [the clauses following this subparagraph.]^{5 6}

The proposal then goes on to define a “split-interest entity,” and explains how a distribution might meet the requirements of the clause above.⁷ This Act’s effective date applies “to distributions made in taxable years ending after the date of the

² Securing a Strong Retirement Act of 2022, H.R. 2954, 117 Cong. § 310 (2021).

³ *Id.*

⁴ *Id.*

⁵ *Id.* at § 310.

⁶ 26 U.S.C. § 408(8)(F)(i-v)

⁷ H.R. 2954 at § 310.

enactment of this Act,” which means that these changes went into effect for the 2023 tax year. ⁸

II. Federal law under the Internal Revenue Code of 1986 governs CGA transactions, and several rules must be followed.

“Under SECURE 2.0 legislation, IRA owners aged 70 [and a half] can choose to make a one-time, tax-free distribution up to \$50,000 (in 2023) from an IRA to fund a new charitable gift annuity.” ⁹ There are several rules that govern this practice:

- 1) The IRA distribution must go directly from the IRA to fund a new immediate CGA (not a deferred CGA),
- 2) There is no charitable income tax deduction allowed for the CGA, but the distribution counts toward the donor’s required minimum distribution (if one is due) and the donor owes no tax on the distribution,
- 3) Spouses may each direct up to \$50,000 from individually held IRAs to create one joint-life CGA,
- 4) The CGA may not make payments to anyone but the IRA owner and/or the owner’s spouse,
- 5) While there is no charitable income tax deduction allowed, the CGA must otherwise qualify for a charitable deduction by passing the 10% minimum income tax charitable deduction test and having a minimum 5% payout rate,
- 6) The CGA must be nonassignable; and
- 7) All annuity payments are taxed at ordinary income tax rates. ¹⁰

As previously discussed, these funds must be transferred to a split-interest entity.

“A split-interest entity may be a charitable remainder unitrust, charitable

⁸ Id.

⁹ You can view a full explanation of charitable gift annuities funded from an IRA, along with examples of using a qualified charitable distribution to create a CGA under this act at https://www.endowdevelop.com/etech_pal/Content/charitable_gift_annuities/charitable_gift_annuities.htm.

¹⁰ Id.

remainder annuity trust, or charitable gift annuity.”¹¹ The implication of this Act is that it “opens the door for tax-exempt organizations to receive increased funding from certain charitable vehicles and provides new incentives for donors to make charitable donations from their IRAs in 2023 and beyond.”¹²

III. Alabama has some regulations governing gift annuity contracts that must be considered before initiating any distribution.

Alabama is known as a “registration state,” where “charities are required to meet statutory minimums and file an application to obtain a permit to issue gift annuities”¹³ Documents that are often required in registration states include “samples of each type of annuity agreement meeting state requirements (disclosure language, etc.), the annuity payout rate schedule, the most recent form 990, and proposed gift annuity advertising materials.”¹⁴ In these states, “charities are not authorized to issue gift annuities until the application is approved and a permit is granted . . . [m]ere submission of an application is not sufficient.”¹⁵

While federal law governs the SECURE Act 2.0 and an individual’s distribution of funds under the Internal Revenue Code, Alabama regulates the issuance of gift annuity contracts from charities to donors. Alabama is one of nine states where “a charity is required to submit its form of agreement for review and

¹¹ Clarke, McPeak, Moran, and Hoke, *Enactment of the SECURE Act 2.0 Brings Some Important Changes for Certain Charities and Donors*, Jan. 30, 2023, <https://taxnews.ey.com/news/2023-0172-enactment-of-the-secure-act-20-brings-some-important-changes-for-certain-charities-and-donors#:~:text=The%20Secure%20Act%202.0%20expands,as%20a%20charitable%20gift%20annuity>.

¹² Id.

¹³ Read more about regulation states and the four types of state regulations here: https://giftlawpro.giftlegacy.com/glawpro_subsection.jsp?WebID=GL1999-0001&CC=3&SS=3&SS2=6

¹⁴ Id.

¹⁵ Id.

approval”¹⁶ An issue arises where general gift annuity contract language provides that “the annuity is not assignable ‘except that it may be assigned to the charity.”¹⁷ As noted above, charitable gift annuities funded from an IRA account under the 2023 Act are not assignable. As a result, charities would need to remove this language from any contract governing an IRA-funded distribution. In states that regulate the issuance of these contracts like Alabama, “removing fixed text (as distinguished from modifying variables such as names, dates, or dollar amounts) is not generally allowed without submitting new forms of agreement for approval.”¹⁸

Charities may update the forms of agreements used for charity gift annuity contracts with the state that they are registered in. In this communication, a charity should “note that [it is] already registered in the state and that [it is] submitting forms of agreement for review and approval.”¹⁹ Additionally, a charity should “indicate whether [it is] adding new variations, and thus leaving all previously submitted/approved forms as they are, or whether [it is] replacing previously submitted forms.”²⁰

The issuance of a charitable gift annuity from a charity to a donor in Alabama is governed by the filing requirements of the Alabama Securities Commission. It states in relevant part that an annuity agreement should contain:

- a) The value of the property or securities to be transferred to the charitable organization,

¹⁶ Edie Matulka, *Gift Annuity Contracts Filed with State Regulators and the Legacy IRA Act*, PG Calc., February 10, 2023. <https://info.pgcalc.com/gift-annuity-contracts-and-the-legacy-ira-act>

¹⁷ Id.

¹⁸ Id.

¹⁹ Id.

²⁰ Id.

- b) the amount of the annuity to be paid to the donor or other annuitant (annual amount),
- c) the manner in which and the intervals at which payment is to be made,
- d) the date of birth and gender of the person or persons during whose life payment is to be made,
- e) the name and address of annuitant; and
- f) the date that payments are to begin. ²¹

Also important to note is filing requirement number 11(a-h), which lists what an issuer of a charitable gift annuity contract should include in a disclosure statement that is to be signed by the donor and provided to the state. ²²

CONCLUSION

While Alabama does regulate the issuance of charitable gift annuity contracts by charities to donors, federal tax law under the Internal Revenue Code of 1986 governs an individual's actual distribution from an IRA account. These transactions were codified under 26 U.S.C. § 408(8)(F)(i-v), and any issue arising under the SECURE Act 2.0 would need to be reconciled with the Internal Revenue Service.

²¹ You can read the full list of filing requirements on the Alabama Securities Commission website here: https://asc.alabama.gov/Registration%20Filing%20Req/req_charitable_gift_annuities.aspx

²² Id.