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SECURE 2.0 Makes Changes to RMD and Excess Contribution Penalties

Penalties can happen to anyone. Just ask Bruce Springsteen. A few years ago, he was performing one of his famous marathon concerts in Foxborough, Massachusetts. The show ran too late, and "The Boss" ended up with a five-figure, concert-curfew fine. The same is true for retirement account owners.

Despite our best efforts, sometimes rules are violated, and penalties will ensue. Two common penalties that occur with IRAs are the required minimum distribution (RMD) penalty and the excess contribution penalty. SECURE 2.0 makes some big changes to both.

RMD Penalty Changes

When retirement account owners reach their required beginning date (RBD), RMDs must be withdrawn. The due date for most RMDs is December 31. However, account owners have extra time to receive their first RMD. That deadline is April 1 of the year following the first RMD year (under SECURE 2.0, the age 73 year). Beneficiaries, including Roth IRA beneficiaries, are also subject to RMDs. Some have annual RMDs while others must follow the 10-year or 5-year payout rules. For those beneficiaries subject to either the 5- or 10-year rule, the RMD is whatever remains in the account at the end of that period.

Missing an RMD deadline is consequential as it can result in a significant fine.

For years, the penalty for a missed RMD has been 50% of the amount not taken. SECURE 2.0 changes things beginning in tax year 2023. The missed RMD penalty is reduced from 50% to 25%. Additionally, the penalty can be further reduced to 10% if the missed RMD is withdrawn during a correction window. For most people, correction must be made by the end of the second tax year following the year for which the RMD was missed. The RMD would need to be taken and the 10% penalty paid during this window.

Example 1: Bruce Springsteen will celebrate his 74th birthday on September 23, 2023. He may be "born to run," but he cannot outrun his RMDs. He will have an RMD from his IRA for 2023 that he must take by December 31, 2023. If he fails to take this RMD, he will owe a 25% penalty on the amount not taken. However, this penalty will be reduced to 10% if he takes the 2023 RMD and pays the penalty by December 31, 2025.

While the changes to the RMD penalty are mostly good news for account holders who miss RMDs, there are still potential issues. SECURE 2.0 leaves intact previous rules which allow an individual

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