

RMD Penalty Waiver Letter Sample

RMDs are mandatory annual withdrawals from your retirement accounts. The IRS requires these distributions to occur, even during rocky periods of life. Fortunately, if you failed to take an RMD during your retirement plan, you can avoid the looming penalty with a tax form waiver letter. Here's what you need to know about the penalty and a waiver letter template to help preserve your nest egg. For proper retirement withdrawal planning, consider working with a financial advisor.

What Is an RMD?

A required minimum distribution (RMD) is the amount of money that individuals with pre-tax retirement accounts, such as traditional IRAs, 401(k)s and 403(b)s, must withdraw from their accounts each year once they reach a certain age. The IRS mandates these distributions to ensure that individuals begin to withdraw and pay taxes on their retirement savings, which have typically been tax-deferred.

Remember, Roth IRAs do not require RMDs during the original owner's lifetime because they have already paid taxes on the dollars invested.

RMDs generally start at age 72 for individuals who turn 70½ after Dec. 31, 2019. However, if you reached 70½ before that date, you would have started taking RMDs at that age. RMDs must be taken annually by Dec. 31. You can calculate what you need to withdraw using the IRS RMD table.

Fortunately, you can delay your first RMD until April 1 of the year following the year you turn 72. Then, you must take all subsequent RMDs by Dec. 31 each year. It's essential for retirees to understand and comply with RMD rules to avoid penalties and ensure they are taking the appropriate distributions from their retirement accounts.

Likewise, designated and non-designated beneficiaries have rules to follow. Specifically, designated beneficiaries receive their own RMD calculation from the IRS and then must take distributions accordingly. On the other hand, non-designated beneficiaries must empty the account within ten years of receiving it. Minor non-designated beneficiaries are exempt from this rule until they reach adulthood.

What Happens If You Miss Your RMD?

According to current tax regulations, missing your RMD incurs a 25% penalty on the distribution you were supposed to take during 2023 and onward. For years 2022 and before, the RMD penalty is 50%.

For example, if your RMD was \$20,000 in 2023, the penalty would be a maximum of \$5,000 for not taking it. Remember, missing your RMD requirement results in a penalty for the amount not taken. In addition, amounts taken over the RMD threshold in the previous year don't count toward your RMD amount for the current year.

What Is a Penalty Waiver Letter?

An RMD (Required Minimum Distribution) penalty waiver letter is a written request submitted to the IRS to request the waiver of the 25% penalty imposed for failing to take the required minimum distribution from a retirement account. This penalty waiver letter is for if you miss taking your RMD for a reasonable cause and wish to avoid or reduce the penalty.

Steps to Take If You've Missed Your RMD

There are ways you can try to correct your mistake if you missed taking your RMD. Here's are steps you should take immediately if you've realized that this has happened:

1. Withdraw the Money Now

If you realize you missed taking the RMD, withdraw it from your account immediately. In other words, take the amount necessary as a lump sum to get you to the RMD threshold instead of increasing your monthly distributions for that year.

2. File Form 5329 with the IRS

After receiving the funds, file Form 5329 with the IRS for each year you missed the RMD. Remember, the form has a specific version for each year, so filling out the form for the matching year is essential. The IRS website has forms for 1975 and onward.

Here's how to complete Form 5329:

Line 52: Write your RMD amount for each account for which you missed the distribution.

Line 53: Write the amount you withdrew. This figure could be \$0.

Line 54: Write zero on this line. Then, write "RC" (abbreviation for reasonable cause) to the left of the line and the amount of the RMD shortfall. For example, if your RMD was \$20,000 and you withdrew \$5,000, the shortfall was \$15,000.

Line 55: Those requesting a penalty waiver will enter zero. In any case, taxpayers don't have to pay the penalty upfront.

Then, mail the completed form and your penalty waiver letter to the IRS.

Remember, filing a Form 1040-X to amend your taxes for the RMD is unnecessary. You'll owe taxes on the amount withdrawn to satisfy the RMD in the year your plan administrator distributes the money.

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Here's a template to use when writing your RMD penalty waiver letter:

To Whom It May Concern:

On [the date you realized the RMD shortfall], while I was [whatever you were doing when you uncovered the mistake, such as reviewing your financial statements], I discovered that for the tax year(s) [tax years for missed RMDs], my distributed amounts were insufficient to satisfy my Required Minimum Distribution. The amount of the RMD shortfall for each year in question is as follows:

[Tax Year A: Shortfall amount, such as \$5,000]

[Tax Year B: Shortfall amount]

[Etc.]

During the years listed above, I was unaware of the error(s), as I was [list reasonable cause, such as suffering from a severe physical or mental illness impairing you from functioning. Provide a full explanation to illustrate why the cause was unavoidable and a justifiable reason for missing your RMD].

Upon discovering my error(s), I took immediate and corrective action by taking the following distributions, as evidenced by the attached documentation [copies of checks, financial statements showing proof of transactions, etc.] on [specific dates].

As my filing history demonstrates, I do my utmost to remain compliant with IRS regulations. In the interest of preventing such errors in the future, I have decided to [list steps taken to prevent future errors, such as hiring a financial manager or increasing your monthly distribution from your plan administrator].

For these reasons, I believe my actions warrant a penalty waiver and I am attaching Form 5329 to request that the penalties be waived regarding my RMDs for years [insert relevant years]. I am also including my physician's report regarding the time of my illness.

Signed,

[Your signature and name]

Bottom Line

RMD shortfalls result in heavy penalties for the missed amount. Fortunately, Form 5329 allows you to appeal to the IRS for a penalty waiver. Sending a penalty waiver letter is an essential part of your request, as it outlines your situation and explains why you missed your RMD. This situation is another reason to keep detailed financial records and work with a financial manager to ensure tax compliance during retirement.

This information is not intended to be a substitute for specific individualized tax or legal advice. We suggest that you discuss your specific situation with a qualified tax or legal advisor.

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