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Uptick in taxes not just for rich

As more turn to dividend stocks, wealthy won't be only group affected by increase

BY BRIAN J. O'CONNOR

When experts talk about letting the tax break on corporate dividends expire in December, the discussion often focuses on making wealthy Americans pay more. But thanks to the ongoing damage of the Great Recession, any higher taxes on dividends could end up hitting the not-so-rich, too, including retirees.

Thanks to the dividend tax break, Republican presidential nominee Mitt Romney has caught flak for paying as little as 13 percent in income tax. But dividends are one of the few ways that retirees and other savers offset the low interest rates paid on bank accounts and government bonds. In fact, shares that yielded high dividends used to be called "widows' and orphans' stocks."

The bottom line: Dividends checks aren't just for the 1 Percenters anymore.

"With Treasury bonds yielding next to nothing, there's been a big move toward high-dividend-paying stocks for income," says David Kudla, CEO of Mainstay Capital Management in Grand Blanc.

Investors calculate the value of a dividend by dividing the total annual dividend payments by the cost of share of the firm's stock, or dividend yield. Apple Inc. announced it would pay its first dividend in the company's history, a quarterly cash dividend of $2.65 per share starting in August.

That $10.60 in annual dividends sounds like relatively rich distribution from the iPod maker, but with shares trading around $660, it has the relatively low dividend yield of 1.6 percent. General Electric's annual dividend of 68 cents sounds paltry by comparison, but with shares around $23, the dividend yield is a more substantial 3 percent. At about $10.15 per share, Ford Motor Co.'s new 20-cent annual dividend yields 2 percent.

Compare that with the five-year U.S. Treasury bond, which yielded 0.66 percent. For the 12 months ended in July, however, the consumer price index gained 1.4 percent, pushing investors to find anything that can keep their money from being eroded by inflation. Meanwhile, some dividend-focused investments are paying returns of 6 percent, Kudla notes.

The icing on the cake is that for even the wealthiest investors, the tax on qualified dividends tops out at 15 percent — less than half of the top 2012 personal tax rate of 35 percent. For lower-income investors who fall in the 15 percent and 10 percent tax brackets, the dividend tax rate is 0 percent.

If the Bush tax cuts all expire as scheduled at the end of the year, investors would pay 15 percent, 28 percent, 31 percent, 36 percent and 39.6 percent when dividends become taxed as ordinary income. Wealthy investors will pay even more, under a 3.8 percent surtax added to pay for the country's expanded medical care. …

…Whether or not Congress steps in to keep the dividend break from expiring with the rest of the Bush tax cuts, dividend stocks should continue to be popular, even if investors face higher taxes on their payouts. …