admin - Fri, 1/24/2014 - 10:17

Defined in the Jobs and Growth Tax Relief and Reconciliation Act of 2003 (JGTRRA), qualified dividends are the ordinary dividends received in 2003 or after that were subject to the same 5% or 15% maximum tax rate that applied to net capital gain. The American Taxpayer Relief Act of 2012 (signed on January 2, 2013) made qualified dividends a permanent part of the tax code but added a 20% rate on income in the new highest 39.6% tax bracket.

Qualified dividends are subject to a 15% maximum capital gains rate if the applicable ordinary income tax rate is 25% or higher. If the applicable ordinary income tax rate is lower than 25%, qualified dividends are subject to 0% tax.

To qualify for the 0%, 15% or 25% maximum rates, ***all*** of the following requirements must be met:

1. The dividends must have been paid by a U.S. corporation or a qualified foreign corporation. *(See qualified foreign corporation below).*
2. The dividends are not of the type listed later under *Dividends that are not qualified dividends.*
3. The proper holding period is met (discussed next).

Holding Periods

Generally, to meet the holding period requirement, a shareholder must have held the stock for more than 60 days during the 121-day period that begins 60 days before the ***ex-dividend*** date. The ex-dividend date is the first date following the declaration of a dividend on which the buyer of a stock will not receive the next dividend payment. Instead, the seller will get the dividend.

A stock bought on the last day before the ex-dividend date (the latest purchase date for collecting a dividend) can still meet the holding period test for that dividend, since there are 61 days left in the 121-day period. A stock sold on the ex-dividend date (the earliest selling date after entitlement to a dividend) can also meet the test, since that is the 61st day in the period. So if a taxpayer holds a stock for at least 61 continuous days, the holding period test should be met for any dividend received.

When counting the number of days the shareholder held the stock, the shareholder should include the date the stock was sold but **not** the date the stock was acquired.

Exception for Preferred Stock

In the case of preferred stock, the shareholder must have held the stock more than 90 days during the 181-day period that begins 90 days before the ex-dividend date ***if*** the dividends are attributable to periods totaling ***more than*** 366 days. If the preferred dividends are attributable to periods totaling ***less than*** 367 days, the 60 day holding period discussed in the previous paragraph applies.

Flow-Through Holding Periods

Mutual funds, other regulated investment companies, and real estate investment trusts that pass through dividend income to their shareholders must meet the holding period test for the dividend-paying stocks that they hold in order for corresponding amounts that they pay out to be reported as qualified dividends on Form 1099-DIV. Investors must then meet the test relative to the shares that they hold directly, from which they received the qualified dividends that were reported to them.

Qualified Foreign Corporation

A foreign corporation is a qualified foreign corporation if it meets any of the following conditions.

1. The corporation is incorporated in a U.S. possession.
2. The corporation is eligible for the benefits of a comprehensive income tax treaty with the United States that the Treasury Department determines is satisfactory for this purpose and that includes an exchange of information program. For a list of those treaties, see *Table 9 –1* in IRS Publication 17.

3.The corporation does not meet (1) or (2) above, but the stock for which the dividend is paid is common or ordinary stock, or an American depository receipt in respect of that stock, which is listed on one of the following markets:

- The New York Stock Exchange,
- The NASDAQ Stock Market,
- The American Stock Exchange,
- The Boston Stock Exchange,

- The Cincinnati Stock Exchange,
- The Chicago Stock Exchange,
- The Philadelphia Stock Exchange or,
- The Pacific Exchange.

Dividends that are not qualified dividends

The following dividends are ***not*** qualified dividends.

- Capital gain distributions.
- Dividends paid on deposits with mutual savings banks, cooperative banks, credit unions, U.S. building and loan associations, U.S. savings and loan associations, federal savings and loan associations, and similar financial institutions. These amounts are reportable as interest income.
- Dividends from a corporation that is a tax-exempt organization or farmer's cooperative during the corporation's tax year in which the dividends were paid or during the corporation's previous tax year.
- Dividends paid by a corporation on employer securities that are held on the date of record by an employee stock ownership plan (ESOP) maintained by that corporation.
- Dividends on any share of stock to the extent that the shareholder is obligated (whether under a short sale or otherwise) to make related payments for positions in substantially similar or related property.
- Payments in lieu of dividends, but only if the shareholder knows or has reason to know that the payments are not qualified dividends.

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