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Original Articles

Dividend taxation and household dividend portfolio decisions: evidence from the U.S. Jobs and Growth Tax Relief Reconciliation Act of 2003

Daeyong Lee

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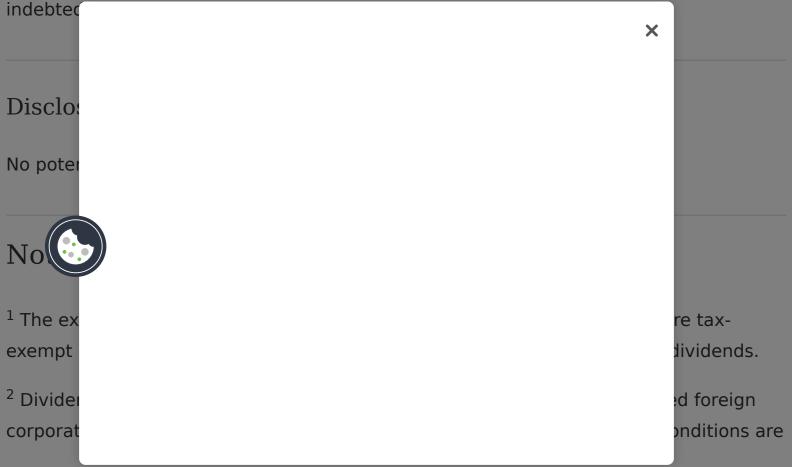
dividends under JGTRRA. That is, households in the upper tax bracket hold significantly greater shares of qualified dividends relative to ordinary dividends after the tax act.

KEYWORDS:



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not satisfied, dividends are considered ordinary ones. For a detailed explanation of qualified dividends versus ordinary dividends, see <u>Section II</u> and <u>Appendix 1</u>.

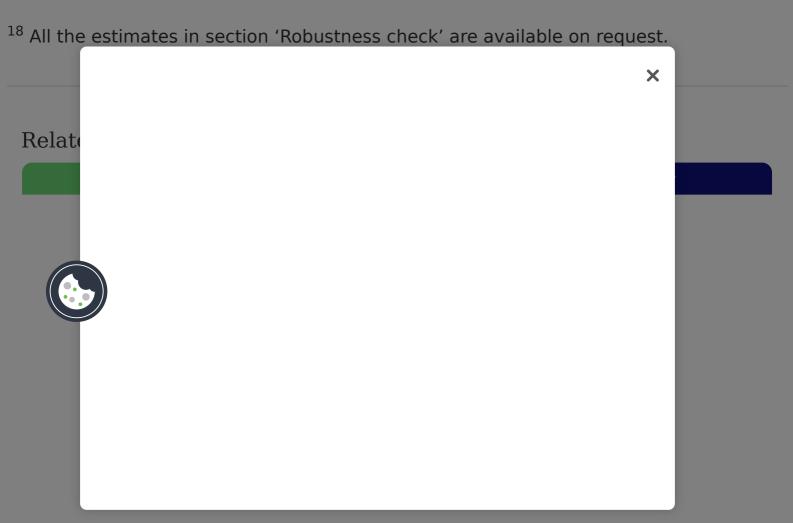
- ³ Capital gains can be either short-term or long-term, and the type of capital gains does not affect the main argument here.
- ⁴ When the subscript i represents stocks paying qualified (ordinary) dividends, the subscript j refers to stocks paying ordinary (qualified) dividends in <u>Equation (3)</u>. The derivative of the share of qualified dividends with respect to the tax rate differentials is positive; that is, $\partial IQD*/IQD*+IOY*/\partial \tau OY-\tau QD>0$.
- ⁵ TAXSIM is the NBER's FORTRAN program that calculates tax liabilities and marginal tax rates under U.S. federal and state income tax laws from individual data (http://www.nber.org/~taxsim/). For more details on marginal tax rates, see Appendix 2.
- ⁶ Several cut-off levels (1%, 3% and 5%) are tested in the sensitivity analysis, and the empirical results verify that the main estimates are robust to the different cut-off levels.
- ⁷ All averages are weighted by the Public Use Tax File sampling weights, and all the dollar values for financial income are adjusted to 2006 U.S. dollars.

⁸ According to the IRS tax stipulation, if net capital gains are positive, households pay either 5% or 15% long-term capital gains tax depending on their ordinary income tax bracket. ong-term capital g n their other types of er year. ⁹ Divide post-2003 tax act i 10 Becau I gains portfolio. As reali a robus analysis; the results v ¹¹ Althou the tax rate different

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- information costs (Barber and Odean 2008).
- ¹³ Because wealthier households can handle adverse income shocks relatively easily, they are less likely to depend on periodical income of dividends and more likely to focus on long-term investments (Amromin 2008).
- ¹⁴ The weak instrumental variable test rejects the null hypothesis (H0:Instrument variable by the first dollar method is weak).
- ¹⁵ This counter-intuitive result might also be due to the timing of capital gains realization around the 2003 tax reform. Households that waited until the scheduled tax rate reduction on capital gains deferred capital gains realization and did so to a great extent after the 2003 tax act. This timing behaviour increases the values in the denominator of the dependent variable, which rather weakens the significance of the results. As such, the timing of capital gains realization does not drive the result.
- ¹⁶ The Hausman test for the model specification rejects the null hypothesis at a 1% significance level (F-statistics: 7.93; p-value: 0.005). Thus, the Tobit estimates using the instrumental variable are consistent for true parameters.
- ¹⁷ This is because the analysis was based on the post-2003 tax data.



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