REMAPPING DEBATE
Asking "Why" and "Why Not"

47 House Dems: Keep lower rates for rich on dividends, capital gains

Story Repair | By Greg Marx | Taxes

From the Editor:

In this feature, we select a story that appeared in a major news outlet and take it in for repairs. The stories we choose are not necessarily "fatally" flawed; on the contrary, in many cases, they'll bring genuinely newsworthy information to light. But our goal is to show how, with a similar investment of time, a different set of interviews or line of questioning could have produced a different — and, we hope, more illuminating — article.

The source material this week: "Dem letter: Keep tax cuts for rich" (Politico, Sept. 28).

October 12, 2010 — In a letter to House Speaker Nancy Pelosi released September 28, 47 House Democrats have urged that reduced capital gains and dividend rates tax rates for the wealthy, currently due to expire at the end of this year, be extended.

The top tax rates for income derived from capital gains and dividends were cut to 15 percent in 2003, when Congress passed the second round of Bush tax cuts. If Congress takes no action and the cuts expire, capital gains taxes will revert to a top rate of 20 percent, and dividends will again be treated as normal income, with a top rate of 39.6 percent.

President Obama has proposed that the top rate be set at 20 percent for both dividends and capital gains, part of his proposal to extend the broader set of cuts for all but the top 2 percent of households. Republicans in Congress are pushing to make all the cuts permanent.

Maintaining the lower rates on capital gains and dividends would directly benefit only the highest-earning households. But the letter, drafted by New Jersey Democratic Rep. John Adler and signed by nearly one-fifth of the Democratic caucus, argues that allowing the dividends rate to rise would hurt senior citizens more broadly, because they are disproportionately likely to collect dividend income.

Raising the rate "would likely cause some companies to forego paying dividends and others to pay a lower amount to shareholders," the letter states. It cites a private study prepared for utility companies which found that 3.7 million elderly households with incomes below $50,000, and 6.2 million with incomes below $100,000, earned taxable revenues from dividends in 2007.

Other studies, though, suggest that any impact would be modest. An analysis of the cut by a Federal Reserve economist found that, while dividend payments did rise after 2003, they likely did so for other reasons. And a recent report from the liberal-leaning non-profit group Citizens for Tax Justice found that two-thirds of dividends are paid to entities, such as pension plans, that are tax-exempt.

“It’s very hard to believe that corporations overall drastically change their practices in paying dividends because a minority of their shareholders are going to be taxed differently,” said Steve Wamhoff, the report’s author.

The same report also estimated that the bottom 60 percent of elderly households — those earning up to $42,000 annually — rely on dividends for just 1.3 percent of their income.

Adler’s office did not respond to a question about how large the impact on low- and middle-income seniors might be. Neither did spokesmen for Representatives Zack Space, Rick Boucher, and Steve Rothman, three of the letter’s signatories.

In addition to the potential effect on seniors, the Democrats’ letter argues that maintaining the lower rates on dividends and capital gains would boost growth and create jobs at a time when “our economy is fragile.”

On the same day the letter was released though, Doug Elmendorf, director of the Congressional Budget Office, warned that a permanent extension of the Bush cuts — either for all income, as Republicans want, or for the bottom 98 percent of earners, as Obama proposes — would reduce growth over the course of the next decade because of the effect on the deficit. (A temporary version of either proposal would be less harmful to long-run growth, Elmendorf said. The letter does not specify whether the Democrats have in mind a temporary or permanent extension of the lower rates.)

Estimates of the cost of maintaining the capital gains and dividend rates at 15 percent were not immediately available. But the budgetary impact of capping the top dividend rate at 20 percent — rather than treating them like ordinary income — has been put at more than $100 billion over the course of 10 years.

The congressmen also did not respond to questions about what the estimated fiscal impact of their proposal might be and how they might pay for the lower rates, or whether Elmendorf’s testimony had affected their thinking.