

Dividend reinvestment plan

A **dividend reinvestment program** or **dividend reinvestment plan** (DRIP) is an equity investment option offered directly from the underlying company. The investor does not receive quarterly **dividends** directly as cash; instead, the investor's dividends are directly reinvested in the underlying equity. (The investor must still pay tax annually on his or her dividend income, whether it is received or reinvested.)

This allows the investment return from dividends to be immediately invested for the purpose of price appreciation and **compounding**, without incurring brokerage fees or waiting to accumulate enough **cash** for a full share of stock. Some DRIPs are free of charge for participants, while others do charge fees and/or proportional commissions.

Similarly **income trusts** and **closed-end funds**, which are numerous in Canada, can offer a **Distribution Reinvestment Plan** and a **Unit Purchase Plan** which operate principally the same as other plans.

Because DRIPs, by their nature, encourage long-term investment, rather than active trading, they tend to have a stabilizing influence on stock prices.

1 Cash purchase

Although the name implies that reinvesting dividends is the main purpose of these plans, many companies offer a complementary **Share Purchase Plan** (SPP). An SPP allows the enrollee to make **Optional Cash Purchases** (OCPs) periodically of company stock. The dollar amount of the OCP is sometimes subject to minimum and maximum limits, e.g. a minimum of \$ 25 per OCP or a maximum that cannot exceed \$100,000 per year. Low-fee or no-fee Share Purchase Plans are important to enrollees as they offer a quick and cost-effective way to increase their holdings. And just like when dividends are reinvested, optional cash purchases are for fractional shares to 3 or 4 decimal places.

DRIPs have become popular means of investment for a wide variety of investors as they enable them to effectively take advantage of **dollar-cost averaging** with income in the form of corporate **dividends** that the company is paying out. Not only is the investor guaranteed the return of whatever the dividend yield is, but he or she may also earn whatever the stock appreciates to during his or her time of ownership. However, he or she is also subject to whatever the stock may decline to, as well.

2 Acquiring stock

The majority of plans require the potential investor to become a registered shareholder, as opposed to a beneficial shareholder. Registered shareholders are direct owners of company stock and are listed with a company's transfer agent, whereas beneficial shareholders hold their stock through a proxy, such as a brokerage account or an investment dealer. In the past, this meant having to keep stock certificates as proof of ownership, but now most plans are in paperless, "book-entry" format. In Canada, you must start a DRIP with a certificate and, as such, Canadian enrollees must safekeep any certificates themselves or transfer them to another individual. All subsequent shares acquired through the DRIP or SPP would be in "book-entry" format.

In addition, certain DRIPs offer (with SEC approval) a direct enrollment option, in which the initial share purchase may itself be made through the DRIP, thereby avoiding retail brokerage fees and commissions. This option is often called a "Direct Share Purchase Plan" or "Direct Stock Purchase Plan" (DSPP). DRIP expert Charles Carlson has dubbed such plans "no-load stocks." However, describing such plans as "no-load stock" plans is extremely misleading. In the mid-1990s, when investing through company-sponsored plans became more popular, such "no-load" plans were created and promoted by certain transfer agents in order to create fees each time an investment is made through the plan (and, in many cases, for each dividend reinvestment). Traditional DRIPs, those available only to those who are already shareholders, are more likely to be "no-fee" plans. There are many no-fee versions of DRIPs, SPPs and DSPPs which are an efficient way to build holdings over time by making small regular investments on a **dollar-cost averaging** basis.

In some DRIPs, the investor has the option of receiving some or all dividends by check, as opposed to full reinvestment. Also, if a DRIP is discontinued, the investor's shares typically continue to be held in book-entry form, either including fractional shares or with a refund check issued for the fractional part of the position.

A downside of using DRIPs is that the investor must keep track of cost basis for many small purchases of stock, and maintain records of these purchases in paper or elec-

tronic form. This assures that the investor can accurately calculate the **capital gains tax** when any **shares** are sold, and document cost basis to their government if requested. This record keeping can become burdensome (or costly, if done by an accountant) if the investor participates in more than one DRIP for many years. For example, participating in 15 DRIPs for ten years, with all of the stocks paying quarterly dividends, would result in at least 615 share lots to keep track of—the 15 initial purchases, plus 600 reinvested dividends. Further complications arise if the investor periodically buys or sells shares, or if the company is involved in an event requiring adjustments to cost basis, such as a **spin-off** or **merger**.

While the term “DRIP” is usually associated with company-sponsored plans, reinvestment of stock dividends is also available at no cost through some brokerage firms. This is called a synthetic DRIP. The drawback to broker “DRIPs” is that they do not allow for optional cash purchases. If the investor wants to acquire additional shares, he or she must pay a commission for each subsequent purchase.

3 External links

- [How To Invest For Free How To Buy Stocks With No Commission Charges](#)
- [Are DRIPs Worth it? Pros and cons of using dividend reinvestment plans](#)
- [DRIP Investing Resource Center](#) A community of people involved in dividend reinvestment programs
- [Dividend Information](#) A searchable database of dividend payouts and history for all stocks
- [Canadian DRIP Primer](#) Step by step guide to starting a Canadian dividend reinvestment plan and lists of Canadian companies and trusts with DRIPs
- [Australian DRIPs](#) resources, information, and guides to Dividend Reinvestment Plans in Australia including a searchable database of listed DRIPs.
- [FirstShare](#) membership organization that helps investor’s acquire one share of stock for DRIP enrollment.
- [What is a Dividend Reinvestment Plan](#) An article about dividend reinvestment plans (DRIPs) including a variety of examples so you can easily understand how DRIPs work.
- [directinvesting.com](#) educational articles, resources and a complete list of Dividend Reinvestment Plans.
- [Things to consider before buying a share and enrolling in a dividend reinvestment plan](#) This article takes an in-depth look at the things you need to consider before buying a share and enrolling in a dividend reinvestment plan (DRIP).

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