



September 23, 2014

Pamela Lew
Office of the Associate Chief Counsel (Financial Institutions & Products)
Internal Revenue Service
1111 Constitution Avenue, N.W.
Washington, D.C. 20024
Pamela.lew@irscounsel.treas.gov

Re: Supplemental Comments on Basis Reporting by Securities Brokers and Basis Determination for Debt Instruments and Options

Dear Ms. Lew,

The Securities Industry and Financial Markets Association (“SIFMA”)¹ is pleased to provide additional comments regarding the final regulations that require brokers to include the customer’s adjusted basis when reporting on the sale of covered securities (the “2013 final regulations”).² We appreciate your attention to our questions raised in previous letters and the opportunity to ask for additional clarifications so SIFMA members may better serve our customers and satisfy the statutory and regulatory reporting requirements.

Difference in 2013 Final Regulations Preamble and Regulation Text

SIFMA would like to call your attention to a difference in the preamble to the 2013 final regulations and the text of those regulations and respectfully request a reconciliation of the two. The text of the preamble appears to indicate that the regulations will require a transferor to include

¹ The Securities Industry and Financial Markets Association (SIFMA) brings together the shared interests of hundreds of securities firms, banks and asset managers. SIFMA’s mission is to support a strong financial industry, investor opportunity, capital formation, job creation and economic growth, while building trust and confidence in the financial markets. SIFMA, with offices in New York and Washington, D.C., is the U.S. regional member of the Global Financial Markets Association (GFMA). For more information, visit <http://www.sifma.org>.

² T.D. 9616 (Apr. 17, 2013).

the date a bond was last amortized on transfer statements.³ However, the text of the regulations does not list the date the bond was last amortized as a required data element. SIFMA requests that the IRS should amend the text of the regulations to clarify that the date the bond was last amortized is a required data element on the transfer statement.

Compensatory Options and Other Equity-Based Compensation Arrangements

SIFMA filed comments on October 4, 2013 requesting that the IRS should allow, but not require, brokers to continue the practice of making basis adjustments to account for the income component of compensatory options and other equity-based compensation arrangements. Such a rule would be consistent with the rule permitting brokers to make basis adjustments to stock rights and warrants under Sections 305 and 307, depending on the brokers' capabilities. Additionally, in order to provide notice to the IRS and the taxpayer that basis has been adjusted, we recommended the IRS add an indicator on the Form 1099-B to identify the sale of compensation-related stock for those brokers that choose to adjust basis. Upon transfer, brokers generally agree to send to the receiving broker the cost unadjusted for the income component, making it unnecessary to add an indicator to transfer statements.

We have attached to this letter our October 4, 2013 letter and respectfully request that the IRS revisit this issue. SIFMA remains concerned that preventing brokers from making basis adjustments related to compensatory options will be more confusing and more challenging for taxpayers and the IRS, and we are happy to meet with you to explain in more detail why this is the case.

Accretion of Market Discount on Defaulted Bonds

SIFMA requests additional guidance to clarify whether, in the case of default, brokers should continue to accrete and report market discount or, whether brokers should cease to accrete as of either: (a) the date of last interest payment or (b) the date of default. Where a bond purchased at a market discount goes into default, and the default announcement is made after a bond is transferred and before the next interest payment, this guidance should clarify if the delivering firm

³ T.D. 9616 at p. 1069 (Stating that the final regulations will require transferors to include "the date through which the transferor broker made adjustments.").

has an obligation to send a corrected transfer statement. In addition, the guidance should clarify if the broker has an obligation to produce a corrected Form 1099-INT, Form 1099-OID or Form 1099-B in a situation where a bond purchased at a market discount goes into default and the default announcement is made after year-end or after the sale of a bond and before the next interest payment date.

Carryforward Reporting

SIFMA also requests clarification regarding the reporting of bond premium when the bond premium allocable to an accrual period is greater than the amount of interest paid. SIFMA believes that firms should be able to report the entire premium allocable for a period, regardless of any possible limits on the deductibility of such premium. This would enable the taxpayer to deduct any available excess bond premium currently to the full extent allowed. Additionally, the broker would be able to keep the cost basis adjustments in sync more easily with the bond premium offset calculated at the time of purchase. This approach appears to be contemplated in the instructions of the 2014 Form 1099-INT below, regarding Box 11:

*“**Box 11.** For a covered security, shows the amount of premium amortization for the year, unless you notified the payer in writing in accordance with Regulations section 1.6045-1(n)(5) that you did not want to amortize bond premium under section 171. If an amount is reported in this box, see the instructions for Form 1040 (Schedule B). If an amount is not reported in this box for a covered security acquired at a premium, the payer has reported a net amount of interest in boxes 1, 3, 8, or 9, whichever is applicable. If the amount in this box is greater than the amount of interest paid on the covered security, please see Regulations section 1.171-2(a)(4).”*

SIFMA members request clarification that they are not required to adjust the amount of bond premium reported when there are possible limitations on the deductibility of such premiums or prior carry-forward.

SIFMA members believe it would be an unreasonable burden to expect brokers to know if the taxpayer is allowed to deduct this excess amortization, particularly in a transfer situation. We

request confirmation that the broker responsibility is to only report the total unadjusted accrued bond premium even if it exceeds the amount of interest paid.

We also request guidance for firms that are netting Boxes 1, 3, 8, or 9 on Form 1099-INT when this same scenario occurs. We recommend a solution under which brokers report zero interest and report the excess amortization in Box 11.

Wash Sales for Debt Instruments

SIFMA members seek clarity in determining how to apply the disallowed loss and holding period acquisition date with respect to wash sales for debt instruments. SIFMA members believe that disallowed loss is an adjustment to basis at sale or maturity and should not be included in adjusted cost for purposes of amortization and accretion calculation.

1256 Contracts

The 2013 final regulations state that transferors are not required to furnish transfer statements for Section 1256 options.⁴ However, we believe that without transfer statements, the receiving broker may not have adequate information for Form 1099-B reporting purposes. The Form 1099-B for regulated futures contracts requires brokers to report: profit (loss) on closed contracts, unrealized profit (loss) at the end of the previous tax year, unrealized profit (loss) for the current tax year, and an aggregate profit (loss) figure. To calculate these amounts, brokers must know, among other things, the purchase price of the contract. The absence of a transfer statement with cost information on 1256 options will render the receiving broker incapable of reporting the required information on Form 1099-B at year end.

SIFMA therefore requests that the IRS require transfer statements for the transfer of 1256 options. We further request that the IRS require the transferor to provide the original basis on the contract as well as the difference between the original basis and the year-end mark-to-market, reported to the IRS in box 10⁵ (Unrealized profit [loss] on open contracts - 'prior year'). In these circumstances, the burden to include unrealized profit or loss in box 11 on Form 1099-B in the

⁴ Treas. Reg. § 1.6045A-1(a)(1)(vi)

⁵ 2014 Form 1099-B

following year should transfer to the receiving broker. SIFMA further requests that the IRS provide an example of the above 1256 option transfer scenario, describing the requirements of the delivering and receiving brokers.

Additionally, Publication 550 provides the following guidance to taxpayers:

“The marked-to-market rules also apply if your obligation or rights under section 1256 contracts are terminated or transferred during the tax year. In this case, use the fair market value of each section 1256 contract at the time of termination or transfer to determine the gain or loss. Terminations or transfers may result from any offsetting, delivery, exercise, assignment, or lapse of your obligation or rights under section 1256 contracts.”

If the IRS intends that delivering brokers consider the transfer of 1256 options to be a closing transaction and that receiving brokers consider the transfer an acquisition, SIFMA members request clarification on the value that should be used in the closing and opening transaction. Brokers use a number of different pricing vendors, and there are a number of ways to value a security. As such, there is considerable risk that the value at which a delivering broker closes a transferred 1256 option will not be the same as the value at which the receiving broker will open the position upon receipt of the asset.

1099-OID (Box 6) – Acquisition Premium

For original issue discount (“OID”) bonds purchased at a bond premium (i.e., above par) the acquisition premium effectively offsets the OID, which makes the OID reportable amount effectively \$0.00. In this instance, SIFMA members request that the IRS clarify what brokers are required to report in the OID and accrued market discount fields.

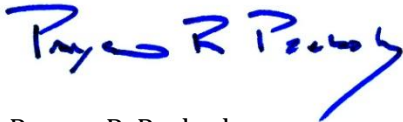
Separately, if an OID bond that pays a coupon is purchased at a bond premium, an additional field would be required to offset the interest income. To account for this reporting requirement, SIFMA requests the IRS add a box 11 to the Form 1099-OID.

1099-B (Box 1g)

The 2014 Form 1099-B has combined the boxes for reporting wash sale loss disallowance and market discount amounts. A problem arises when brokers need to report both amounts on a bond since the treatment of wash sale loss disallowance and market discount is different. Additionally, the amount reported in Box 1g would be used to make an adjustment to the Schedule D. SIFMA requests future versions of the form split Box 1g into separate boxes, since the two values (wash sale disallowance and market discount) cannot be netted due to the difference in reporting requirements.

We appreciate the IRS's continued work relating to cost basis reporting requirements and consideration of our additional and remaining concerns. As our member firms develop compliance systems, SIFMA anticipates sending additional comments in the future regarding guidance on transfer requirements and requirements for complex debt. We also would be happy to meet to discuss the foregoing recommendations at your convenience. Please do not hesitate to contact me or Jillian Enoch at (202) 962-7300 if you have any questions or if we can be of further assistance.

Sincerely,



Payson R. Peabody
Managing Director & Tax Counsel
Securities Industry and Financial Markets Association