SIFMA
Securities Industry and
Financial Markets Association

April 9, 2009

Mr. Stephen Schaeffer
Office of Associate Chief Counsel (Procedure & Administration)
CC:PA:LPD:PR (Notice 2009-17)
Courier Desk
Internal Revenue Service
1111 Constitution Avenue, NW
Washington, D.C. 20224

Re: Reporting of Adjusted Basis in Securities Transactions – Notice 2009-17

Dear Mr. Schaeffer:

The Securities industry and Financial Markets Association[1] (SIFMA) appreciates the opportunity to provide comments on the implementation of the new information reporting requirements enacted under the *Energy Improvement and Extension Act of 2008* (P.L. 119-343). IRS guidance is critical for clarifying brokers' responsibilities under the new law and creating consistent rules to carry out the law's requirements. Our comments in response to Notice 2009-17 are attached.

Please feel free to call me at 202-962-7300 if you have any questions of if we can be of further assistance.

Sincerely,

Shahira Knight
Managing Director

Attachment

[1] The Securities Industry and Financial Markets Association brings together the shared interests of more than 650 securities firms, banks and asset managers. SIFMA's mission is to promote policies and practices that work to expand and perfect markets, foster the development of new products and services and create efficiencies for member firms, while preserving and enhancing the public's trust and confidence in the markets and the industry. SIFMA works to represent its members' interests locally and globally. It has offices in New York, Washington D.C., and London and its associated firm, the Asia Securities Industry and Financial Markets Association, is based in Hong Kong.

Attachment – SIFMA Submission (Notice 2009-17)

Applicability of Reporting Requirements

1. **How to determine who is a "middleman" subject to the broker reporting and transfer reporting statement requirements and how to minimize duplication of reporting by multiple brokers.**

   - The universe of entities subject to the broker reporting requirements is different than the group subject to the transfer reporting requirements.

     - Under the statute, the broker reporting rules apply to any "broker" that is required to report gross proceeds under Code section 6045(a) with respect to the sale of a covered security. Accordingly, the definition of "broker" under the regulations for section 6045 should be adopted for purposes of the new information reporting rules.

     - The transfer reporting rules apply to "applicable persons" as discussed in #2.

2. **Who, in addition to brokers, should be treated as "applicable persons" subject to the transfer reporting requirements;**

   - Any entity that warehouses securities for a client, record keeps on behalf of a taxpayer, or transfers a physical security from one location to another should be required to maintain cost basis information for covered securities and should be treated as an "applicable person" subject to the transfer reporting requirements. This would include (but should not be limited to) brokers and their agents, transfer agents, banks, depositories, mutual fund companies, qualified and nonqualified stock plan administrators, and trust administrators or trustees of a trust.

   - Regulations should make clear that brokers are not required to validate whether a person transferring basis information is, in fact, an "applicable person." Regulations should also make clear (as provided in #31) that brokers are not required to validate the accuracy of the cost basis information they receive from applicable persons.

3. **Whether the issuer's classification of an instrument (e.g., as stock or debt) should determine which effective date applies;**

   - The issuer classification of an instrument for federal income tax purposes should be used to determine which effective date applies because issuers and their advisors are in the best position to determine the security's classification. Moreover, using the issuer's classification will ensure consistency among holders and ensure the effective date is evenly applied throughout the industry.

   - Regulations should require issuers to include a security's classification for federal income tax purposes in the tax section of the prospectus, and brokers should be able

to rely on that determination without penalty. For securities that are exempt from registration with the Securities Exchange Commission (SEC), the classification should either be filed with the Internal Revenue Service (the "Service") or made available in public documents in a timely manner. If filed with the Service, the information could be distributed in an electronic publication.

- With respect to some securities, such as hybrid instruments and structured products, the classification may be unclear even if information is provided in the issuer's prospectus. Some suggestions for addressing classification problems with respect to complex financial instruments include:

    1. Regulations could require issuers to provide information about the tax character of income in the prospectus or proxy statements of publicly-traded securities.

    2. The Service could establish a clearing facility (like Pub. 1212 for Original Issue Discount) that lists and classifies securities that pose the most problems. Ideally, the clearing facility would be established before hybrid securities become subject to the new reporting rules.

    3. Brokers and applicable persons could be allowed to make their own determination if the tax classification of the financial instrument or the income is unclear. This is the current practice with respect to determinations about whether an income item should be reported on Form 1099-INT or Form 1099-DIV. Penalty relief would be ne needed if this option is adopted.

Basis Method Elections

4. **How to ensure that customers are adequately informed of the broker's default basis determination method and that brokers are adequately notified of a customer's election of a different acceptable method for an account;**

- *Informing customers of the default method.* Customers could be informed of the broker's default basis method through: (1) broker websites, (2) monthly statements, (3) brochures, (4) client notices, (5) broker disclosure statement, (6) confirms, (7) Form 1099, and/or (8) new account documents. The Service should provide flexibility with respect to notification methods because the best way of informing customers will vary depending on how the customer interacts with the broker.

- *Notifying brokers of customer elections.* Similarly, customers could notify brokers of their election to use a method other than the default through various forms of communication, such as: (1) new account forms, (2) brokers websites, (3) a written statement submitted by mail, fax or email, (4) a statement submitted through an electronic communications system established by the broker for this purpose and/or (5) by recorded phone line. Again, the Service should provide flexibility with respect to the way in which customers notify brokers of their election because the best notification method will depend on how the customer interacts with the broker.

5. **How to facilitate customer elections of acceptable basis determination methods, including average cost basis, for an account to maximize customer flexibility and minimize broker burden;**

- A customer should be allowed to elect the average cost method or the first-in first-out (FIFO) method when the account is opened or anytime prior to the first trade.[2] If the customer chooses to identify the specific tax lots to be sold, the selection should be made at the time of the trade as provided under existing Treasury regulation 1.1012-1(c)(3)(a), and the specific lots sold would be shown on the trade confirmation or other statement. If an election is not made prior to the first trade, and the customer does not identify the specific lots to be sold at the time of the trade, then the broker's default method would be used.

- To facilitate customer elections and minimize burdens, regulations should address whether brokers will be required to accommodate customer elections affecting basis, such as alternate estate valuation, amortizing bond premium on taxable bonds and accruing market discount.

- Finally, we recommend that basis methods be simplified. In particular, the double category method for calculating average cost should be eliminated. It would cause complications if basis is calculated using one method, and then shares are subsequently transferred to an account using the other method. Moreover, SIFMA is not aware of any broker that currently uses the double category method.

6. **Whether and under what circumstances a customer may elect to change from the average cost basis method to the first-in first-out or specific identification method and, if so, what cost basis rules and adjustments should apply;**

- Switching from the average cost method to the FIFO or specific identification methods is very problematic because it requires the broker to restate lots and reinvest shares. This makes reconciliation difficult, if not impossible. It also increases the likelihood of inconsistencies between broker and customer reporting. As a result, customers should not be allowed to change from the average cost method to the FIFO or specific identification methods unless the requirement to restate lots is eliminated.

- If final regulations eliminate the requirement to restate lots, customers who switch from the average cost method to the FIFO or specific identification methods should receive consent from the Commissioner as required under existing Treasury regulation 1.1012(e)(2). It should be noted that brokers cannot represent customers before the Service. As a result, it must be the customer's responsibility to receive the appropriate consent from the Commissioner, and presumptions should be established so that brokers can rely on a customer's representation that consent was received.

[2] Standing instructions of the specific lots to be closed (e.g., highest-in first-out) could also be elected prior to the first trade date.

7. **What it means to apply the basis determination conventions on an "account-by-account" basis;**

- Applying the basis determination conventions on an "account-by-account" basis means the rules would apply separately to each account. In other words, brokers would not be required to take into consideration any position in a security held in any other account when determining the basis of a security that is sold under the applicable convention.

- For purposes of stock in a brokerage account, an "account" generally means all the positions held in a specific numbered account (but not all positions held by the customer at that firm). For purposes of stock in a regulated investment company, an "account" generally means each separate fund identified by a particular CUSIP number.

- If the customer elects the average cost method or to specifically identify tax lots sold, brokers should be allowed to apply the accounting method or identification at the CUSIP level rather than the account level. This is consistent with the existing Treasury regulations that govern the identification of tax lots sold..

- Subaccounts, such as cash and margin accounts, should not be treated as separate accounts for this purpose.

Dividend Reinvestment Plans

8. **How to determine what qualifies as an "arrangement under which dividends on any stock are reinvested in stock identical to the stock with respect to which the dividends are paid" (that is, as a "dividend reinvestment plan");**

- Under current regulations, the average cost method is not a permissible method for calculating the adjusted basis of stock (other than shares in a mutual fund). Consequently, the use of the average cost method with respect to stock in a dividend reinvestment plan (DRIP) has the potential to create significant complications when the shares are transferred from the DRIP to a brokerage account. Moreover, it is likely to create taxpayer confusion because identical stock acquired outside the DRIP will not be eligible for the average cost method. SIFMA understands that the ability to use the average cost method with respect to DRIPs was intended to be a simplification provision for entities that may not currently have the ability to do lot-by-lot tax accounting, such as transfer agents and issuers. As such, we believe the ability to use the average cost method was intended to be at the broker's election – not the customer's election. If transfer agents and issuers are forced to comply with a customer election to use the FIFO method or specific identification, then the provision would not provide the intended simplification. Regulations should clarify that the ability to use the average cost method with respect to stock (other than shares in a mutual fund) acquired in connection with a DRIP is at the broker's election, and that brokers do not have to comply with a customer's election for shares acquired in a DRIP.

- If this clarification is made, the term "DRIP" can be defined broadly to include any program or plan for which customers request that dividends and other income in the account be automatically reinvested into shares of the identical security. Identical securities are those with the same Committee on Uniform Security Identification Procedures (CUSIP) number. This should include Depository Trust & Clearing Corporation (DTCC) reinvestment, transfer agent DRIPs, direct stock purchase (DSP) plans, issuer dividend reinvestment plans, and broker-sponsored DRIPs.

- If this clarification is not made, the term should be defined narrowly to include only issuer plans and transfer agents.

9. **How to determine which stock qualifies as "acquired in connection with" a dividend reinvestment plan, for which the average cost basis method is available beginning in 2011, and to which the later effective date of 2012 for information reporting applies**;

- *Effective Date for Availability of the Average Cost Method*. Under the statute, the average cost basis method is available for stock acquired in connection with a DRIP beginning in 2011. This effective date is highly problematic because the average cost method is not a permissible method for stock (other than shares in a mutual fund) under current regulations. As a result, most brokerage systems cannot currently accommodate the average cost method for shares in a DRIP. It would be difficult to update systems to accommodate the average cost method for DRIPs by January 1, 2011.

- *Effective Date for Basis Reporting*. Under the statute, basis reporting for stock is required:

  - Beginning in 2011 if the average cost method is NOT permissible and
  - Beginning in 2012 if the average cost method IS permissible.

  Under the statute, the average cost method is permissible (beginning in 2011) for stock acquired in connection with a DRIP. As a result, basis reporting for stock DRIPs is required beginning in 2012. In contrast, basis reporting for stock (other than shares in a mutual fund) acquired in a brokerage account is required beginning in 2011. This disparity could create considerable customer confusion because shares of an identical security purchased in the same year will be "covered" in some cases but not others (i.e., depending on whether the shares were purchased through a brokerage account or a DRIP). This will be very confusing for customers who ultimately consolidate all of their shares into a brokerage account.

- *Recommendations*. We recommend that use of the average cost method for stock (other than stock in a mutual fund) acquired in a DRIP should be solely at the broker's election. If use of the average cost method is not solely at the broker's election, then we recommend that the average cost method should not be available for shares in a DRIP until 2012. Delaying the availability of the average cost method would address two problems: (1) It would give brokers sufficient time to update their systems to accommodate the average cost method for DRIPs, and (2) it would resolve the customer confusion that may result from disparate effective dates.

10. **Whether and to what extent the average cost basis method applies to subsequent additions to dividend reinvestment plan accounts by purchase or transfer;**

- It is unclear what is meant by "subsequent" (i.e., subsequent to the effective date or subsequent to depositing shares into the plan?) Regardless of the definition, all "subsequent" purchases and transfers into the plan should be eligible for the average cost basis method as long as the plan is coded for reinvestment at the time the purchase or transfer is made.

11. **How to maximize the utility of the single-account election for stock acquired in connection with a dividend reinvestment plan or stock held in a regulated investment company, particularly where basis and holding period information for pre-effective date stock is weak or unclear;**

- Brokers who choose to combine pre- and post-effective date shares into a single account should be confident of the accuracy of the basis information for the pre-effective date shares. If they are not confident of this information, the shares should not be combined into a single account.
    - The Service may wish to consider providing guidelines for a "standard of reliability" with respect to pre-effective date basis information. Brokers who include pre-effective date shares in the average cost calculation for covered securities would not be penalized if they meet the standard of reliability. Similarly, brokers would be subject to penalties if they use pre-effective date basis information that does not meet the reliability standards.
    - Instead of an "all-or-nothing" rule, the Service may also want to consider allowing brokers to exclude any pre-effective date shares that have no or unreliable basis information from the combined account. The excluded shares would then be treated as uncovered shares for which no basis reporting is required. This alternative would encourage brokers to use all of the reliable information available in determining the basis of the shares sold.
- The single/bifurcated account election will create numerous issues because brokers who choose to aggregate pre- and post-effective date shares into a single account are likely to receive non-covered securities with unreliable basis information after the election to aggregate is made. Industry would like to work with the Service to develop workable guidelines for the single/bifurcated account election.

Other DRIP Issues

The DRIP provisions of the statute allow brokers to use the average cost method with respect to stock acquired in connection with a DRIP. If the shares are transferred out of the DRIP, the transferor is required to aggregate all shares with the same holding period into a single lot with a single basis number. This will allow the receiving broker to seamlessly incorporate the lots into the broker's FIFO or specific identification tax lot accounting system. Regulations need to clarify at least two issues.

- As discussed in #8, SIFMA believes the option to use the average cost method in connection with a stock DRIP should be at the broker's election. Requiring brokers to accommodate customer elections in a stock DRIP would appear to defeat the intended purpose of the provision, which is to simplify basis calculations for issuers, transfer agents, and other entities that are not capable of lot-by-lot tax accounting.

- Regulations should clarify the procedures for transferring shares out of the DRIP. Specifically, all shares held for at least five years must be aggregated into a single "long-term lot" and all shares held between one and five years must be aggregated into a single "mid-term lot."[3] Each of these lots would have a single basis number. Shares held for less than one year would not be aggregated (consistent with the single category method for calculating average cost).

Reconciliation with Customer Reporting

12. **How to ensure that broker reporting on Form 1099-B and customer reporting on Schedule D of Form 1040 are maximally consistent, including whether brokers should report separately for securities subject to basis reporting or report the basis of securities that are not covered securities, for example, securities purchased by their customers prior to 2011;**

- In general, the statute requires brokers to use the basis determination method selected by the customer.[4] The intent of this requirement is to help improve consistency between customer and broker reporting. Accordingly, customers should be required to report on their federal income tax returns the same information shown on the Form 1099-B. However, if a taxpayer has more accurate basis information than what is reported on Form 1099-B, the taxpayer should be allowed to make adjustments from the broker-provided number and provide substantiating documentation with their tax return. Moreover, the broker should not be required to amend the Form 1099-B or adjust basis of remaining shares to conform to the taxpayer's records.

- As explained in #5 and #6, simplifying the allowable basis methods and limiting the number of times customers can switch methods will help preserve the integrity of the basis information and further improve consistency between broker and customer reporting.

- To facilitate reconciliation, we recommend that taxpayers report each sale on the Schedule D using the same tax lot as shown and identified (by CUSIP number and quantity) on the Form 1099-B.

[3] Under current law, the 18-percent capital gains tax rate for securities held at least five years will return beginning in 2011 when the basis reporting requirements take effect.

[4] Although the general rule under the statute requires brokers to accommodate the customer's basis method, SIFMA believes the ability to use the average cost method for stock DRIPs is intended to be solely at the broker's election.

- Brokers should have the option to include basis information for non-covered securities on the Form 1099-B and should have the option to report this information to the Service. Brokers who choose to report this information on the Form 1099-B should include an indicator that the security is not covered. Moreover, if the broker chooses to furnish basis information to the customer, but *not* to the Service, the broker should clearly inform the customer that the information is not being reported to the IRS. There should be no confusion to customers regarding which basis information is reported to the Service.

13. **How to ensure consistency between customers making specific identification of securities sold or transferred and broker reporting;**

- In general, consistency between customer and broker reporting should not be a significant problem when customers specify the lots to be sold or transferred. Procedures already exist under section 1012 for making a specific identification and the need for broker confirmation of that identification. Under these rules, once a security has been identified as sold, the basis of the specified security needs to be captured in the broker's information reporting systems. The same basis information will then be provided on both the trade confirmation (or other statement) and on the Form 1099-B. The confirmation includes enough detail about the cost lot to help ensure consistency.

- Moreover, the statute requires that only lots held in the account from which the shares are being disposed may be specifically identified (i.e., the "account by account" basis determination). This rule will also help ensure consistency.

14. **How to ensure that reconciliation is possible if broker reporting should differ from customer reporting;**

- The Form 1099-B provides detailed information (i.e., CUSIP number, quantity and sale date) for each tax lot sold. This level of detail ensures reconciliation is possible if the broker's basis information differs from the customer's information. As provided in #12, customers who choose to make adjustments to the information provided on the Form 1099-B should be allowed to reconcile the differences on the Schedule D and provide substantiating documentation. However, reconciliation should be solely the taxpayer's responsibility.

- The Service may want to specify in regulations the situations in which customers can adjust the basis information reported by the broker (i.e., the situations in which reconciliation is allowed).

15. **Whether customers, after a sale, may identify or change the identification of specific stock sold and, if so, for what period of time or by what deadline;**

- Current Treasury regulation 1.1012-1(c)(3)(a) requires that customers notify their broker of any specific identification of a tax lot sold "[a]t the time of sale or transfer."

A specific identification cannot be made after close of business on the trade date. To avoid affecting the integrity of the reporting process, the section 1012 rules should be followed and changes should not be allowed after the sale.

Special Rules and Mechanical Issues

16. **The scope of the wash sales exception, including the definition of "identical securities" (including identical options), the wash-sale period, and any de minimis or other exceptions;**

- *Scope of Wash Sale Exception*. Under the statute, wash sales are taken into account for purposes of determining adjusted basis only if the acquisition and sale transactions occur in the same account and are in identical securities.

- *Definition of Identical Securities*. As provided in the legislative history,[5] securities are considered identical for purposes of the wash sale exception only if they have the same CUSIP number. Thus, a broker is not required to account for securities that are "substantially identical" but not "identical" to the securities sold at a loss when reporting adjusted basis..

- *Wash Sale Period*. The wash sale period should continue to be 30 days, as provided under current law.

- *De Minimis Exceptions*. Brokers should not be required to take into account dividend reinvestments for purposes of determining whether there is a wash sale.

- *Other Issues*. Regulations should clarify how the wash sale rules would apply when part of the position is covered and part is non-covered.

17. **How to apply the rules for basis reporting of options;**

Information reporting with respect to options does not take effect until January 1, 2013. As a result, we would appreciate the opportunity to submit comments with respect to the reporting of options at a later date.

18. **Whether rules, including transition rules, are required to address the change in timing for reporting of short sales from the date the short sale is entered into to the date the short sale closes;**

- We do not believe transition rules are needed to address the change in timing for reporting short sales. For short sales that are entered into before the applicable effective date, the taxpayer should follow the usual practice of reconciling the Form 1099-B on Schedule D so that no gain or loss is recognized in the year of the short sale. For short sales covered after the applicable effective date, the taxpayer should

[5] Joint Committee on Taxation, "General Explanation of Tax Legislation Enacted in the 110th Congress," JCS-1-09, March 2009.

report the adjusted basis shown on the Form 1099-B and recognize the resulting gain or loss.

- Regulations should make clear that brokers do not have to take into account section 1259 (regarding constructive sales) when reporting short sales because there is no transaction or process-able event to capture in the system. As a result, there is no capability of capturing constructive sales.

19. **How to address mechanical issues relating to the computation of basis, such as adjustments for debt securities (for example, as a result of original issue discount, market discount, acquisition premium, or bond premium), gift-related adjustments, death-related adjustments, section 1043 basis rollovers, regulated investment company and real estate investment trust distributions representing return of capital, regulated investment company load adjustments, and the mark-to-market method of accounting for securities;**

- *Debt Securities*. Information reporting with respect to debt securities does not take effect until January 1, 2013. As a result, we would appreciate the opportunity to submit comments with respect to the reporting of debt securities at a later date.

- *Gifted and Inherited Securities*. Under the statute, a security is "covered" if it is: (1) acquired through a transaction in the account in which the security is held or (2) transferred to that account from an account in which the security was covered. This definition was intended to capture only those securities for which the broker has reliable basis information and can observe events affecting basis. The legislative history provides that: "Under this rule, certain securities acquired by gift or inheritance are not covered securities." Regulations should clarify what is meant by "certain" (i.e., under what circumstances are gifted or inherited securities "covered" by the reporting requirements and how should basis adjustments be made since the receiving broker may not know the security's fair market value on the date of the gift.

- *1043 Basis Rollovers*. We have no comments relating to 1043 basis rollovers at this time.

- *RIC and REIT distributions representing return of capital*. Post-year end reclassifications representing a return of capital are problematic because they require basis adjustments and corrected information returns. In some cases, the reclassifications may be received after a position has already closed. Moreover, taxpayers who have already filed tax returns may not amend their return to reflect a post-year end reclassification, especially if it is small or would not result in additional tax liability. As a result, we recommend the following:

    - *Filing Deadline Extensions*. The Service should continue to grant, upon request, 30-day extensions for brokers to furnish payee statements so that reclassification data can be processed if it is received within a reasonable amount of time.

- *De Minimis Exception*. There should be a de minimis exception for reporting basis adjustments due to income reclassifications on Form 1099-B. The exception should apply to original reporting and to corrected reports resulting from an income reclassification published by a RIC, a REIT or a regular corporation. Current law already provides a $10 de minimis exception for reporting on Forms 1099-DIV, 1099-INT and 1099-OID. We recommend the de minimis exception for reporting basis adjustments should be based on a percentage (e.g., 2 percent) of the dividend payable on the payment date. For example, if a dividend payable in March 2012 is reclassified, brokers would not be required to make basis adjustments if the reclassification represents a de minimis percentage of that specific dividend payment.

- *Cutoff Date*. In addition to a de minimis exception for adjusting and reporting income reclassifications, a cutoff date for reclassifications should be established to avoid the need for continued revisions. If reclassifications are received after the cutoff date, brokers should not be required to adjust closed investor positions, and taxpayers should not be required to file amended tax returns. A cutoff date is desirable because, at some point in time, taxpayers should be able to rely on their 1099 statements without the fear of future corrections that require amendments to their tax returns. We suggest the cutoff date should be no later than March 15th following the end of the 1099 tax reporting calendar year. This would allow reasonable time for processing, printing and mailing payee statements to taxpayers and enough time to file tax returns before the original due date.

- *Application of Penalties*. The regulations under Code section 6721 (regarding failure to file correct information returns) should be modified so that if a reclassification of income causes a failure which affects more than a single information return, the penalty imposed would not be greater than the amount of the correction. At a minimum, section 6724 should be modified to allow for a penalty abatements based on reasonable cause.

- *RIC load adjustments*. We defer to the recommendations and comments of the mutual fund industry regarding RIC load adjustments.

- *Mark-to Market method of accounting for securities*. Most brokers' retail systems are not capable of handling mark-to-market accounting for clients. Several issues must be considered before administer-able rules can be developed. Moreover, we do not believe the statute contemplates basis reporting for traders and dealers because "payees" are considered to be "investors" for information reporting purposes.

20. **What, if any, translation conventions or computation adjustments should be allowed when securities are purchased with foreign currency in an account subject to United States taxation at the time of purchase or in an account that later becomes subject to United States taxation, for example, when an owner of securities becomes a United States citizen;**

- The latest spot rate available on the trade date should be used to report basis in US dollars for US taxpayers who purchase securities in a foreign currency.

- With respect to an account that later becomes subject to US taxation, mandatory reporting should apply only to securities acquired after the broker is notified of the change in the customer's tax status.

- In general, basis reporting should not apply to a customer who is only presumed to be a US non-exempt recipient under the section 1441, 6045 and 6049 regulations by virtue of not having provided sufficient documentation to prove his/her/its foreign status. This rule should be incorporated into the definition of a covered security regardless of whether the transaction is conducted in a foreign currency. This exception from basis reporting should apply even if reporting of gross proceeds and backup withholding continue to apply.

Transfer Reporting

21. **What information about the transferring person, the customer, the security transferred, and the underlying lots should be required on the transfer reporting statements;**

- To ensure consistency among different transferors, regulations or other guidance will need to set forth the types of information required to be shown on the transfer reporting statement. Examples of the information and data fields that we recommend be included are listed below. It should be noted that this is not an exclusive list, and all of this information would not need to be provided in all cases.

    - Originating and receiving account numbers
    - Identifying code (e.g., control#, certificate#, DRS#, DWAC#)
    - Account title
    - CUSIP number
    - Quantity
    - Acquisition date
    - Acquisition price
    - Original cost basis
    - Adjusted cost basis
    - Tax lot accounting method used (e.g., FIFO, average cost, etc.)
    - Type of transfer (e.g., account transfer, gift, inheritance, etc.)
    - Covered/Uncovered indicator
    - Reason code (i.e., if it's uncovered, what is the reason)
    - The date the security was last adjusted for a corporate action
    - Holding period indicator (in lieu of acquisition date when average cost is used)
    - Dividend reinvestment indicator (for purposes of the de minimis exception recommended under #16 with respect to wash sales)

- Brokers will need to know the transferring person's entity type (e.g., brokerage firm, transfer agent, etc.) and some type of contact information, such as a telephone number. Account information is needed (as provided above), but specific information about the customer is not necessary.

22. **Whether fifteen days is the proper period for furnishing transfer reporting statements, and under what circumstances a different time period, if any, should apply;**

- Fifteen days is ample time for furnishing transfer reporting statements.

23. **Whether the basis determination rules and customer elections governing sales of securities should apply equally to transfers of securities, for example, when a customer transfers some, but not all, holdings of a security to another broker;**

- Customers should be allowed to determine which lots to transfer, and additionally whether multiple lots should be transferred on a pro-rata basis.

- The basis determination rules and customer elections that govern sales of securities should apply equally to partial and full transfers. The rules should not differ if a customer transfers only a portion of their holdings.

24. **Whether electronic transfer reporting may be appropriate and, if so, whether a common format should apply;**

- Electronic transfer reporting is preferable and a standard format, such as CBRS, should apply for all transfers. This will ensure that all "applicable persons" are transferring and receiving data in a format that can be understood and used across all brokers, agents and record keepers. Given the volume of transfers, written or manual information would be unworkable and could create numerous problems, including errors and lost information.

- Brokers already have access to CBRS through the Automated Customer Account Transfer Service (ACATS) system. However, there is currently no single method that is used to transfer share positions and/or cost basis information between broker-dealers, banks, mutual fund companies, and DRS plans. It is our understanding that access to the Depository Trust & Clearing Corporation may be expanded to provide more entities with access to electronic reporting in a standard format.

25. **Whether brokers and transferring parties may utilize reporting services of third party intermediaries to meet their transfer reporting requirements;**

- Yes. Brokers and transferring parties should be allowed to utilize outside services. Existing regulations provide that payors are responsible for the actions of their agents. These regulations should continue to apply. In other words, firms that choose to use third party services should be required to have adequate checks and balances in place to assure the firm is in full compliance with the tax law requirements.

- Regulations should make clear that the transferring broker is responsible for sending the basis information to the receiving broker, even if a third party vendor is used. In other words, the receiving broker should not be required to accept basis information directly from the third party vendor.

26. **Whether the transferring person should communicate any information or justification to the transferee broker when no transfer reporting statement is required because the security is not a covered security;**

- Transferring persons should be required to provide a record for all non-covered securities with an indicator that the security is not covered. As recommended in #21, the transfer report could include a reason code to explain why the security is not covered.

Issuer Reporting

27. **What information about the issuer and organizational action should be required on the issuer returns and reporting statements;**

- The statute requires the issuer to provide a description of the action, the quantitative effect on basis, and the name, address and phone number of the issuer. The "quantitative" effect of the basis adjustment should include any and all pertinent information that organizational actions have on the cost basis of shares, including:

    - The effective date
    - Type and terms of corporate action
    - Whether the transaction is taxable (including whether gains and losses are taxable or nontaxable in the case of cash and stock mergers)
    - The taxable nature of the corporate action
    - The Code section under which the investor is taxed
    - The treatment for US holders and how basis is to be calculated (with examples)
    - If loss is allowable
    - Specific information, such as whether the basis is to be increased or decreased and by what amount
    - Whether there is an adjustment to basis of existing shares or a proportional amount of the cost basis assigned to newly-issued shares, as in the case of a spin-off or merger.
    - The percentage of allocation to the non-taxable stock in the case of a cash and stock merger.

- Regulations should require issuers to determine fair market value and fair market value date(s) using the rules provided under existing regulations.

28. **How to maximize the timeliness of issuer returns and statements and promote public reporting by issuers in lieu of return filing;**

- Issuers should post the information described in #27 on their websites so it is available to both shareholders and brokers. However, issuers should also be required to make the information publicly-available by providing it to an industry resource, such as a vendor or clearing organization. Such a requirement would make the information broadly available without requiring the issuer to report to the Service.

- In addition, issuers should have a tax opinion rendered regarding the proper way to account for the cost basis adjustments, and the opinion should be published in shareholder offering documents and on issuer websites. The opinion should be rendered at the issuer's expense as it would be unreasonable to require thousands of securities firms to research the matter independently and potentially reach different conclusions.

29. **How to account for basis-changing organizational actions by foreign issuers of securities to the extent that foreign issuers are not subject to the issuer reporting requirements;**

- We believe foreign issuers of "covered securities" are subject to the issuer reporting requirements of the statute. However, enforcing the requirements may be difficult. As a result, the Service may want to consider various enforcement mechanisms through other regulatory authorities, such as the SEC or Financial Industry Regulatory Authority (FINRA), or a US clearing organization or depository located in the United States.

- In addition, default rules should to be established so that brokers know how to adjust basis if information is not received from foreign issuers. We recommend the default rule should provide that a security is fully taxable as an exchange, and the broker should use its best effort to determine fair market value of taxable securities or other property received.

30. **How to coordinate broker transfer reporting with issuer corporate action reporting to avoid duplicate broker adjustments when accounts are transferred and whether a universal timing standard should apply;**

- In general, the operating assumption should be that adjustments have been made for all events for which issuers have provided information prior to the date of transfer unless the corporate action is effective *after* the date of transfer.

- The firm that processes the reorganization or corporate action should be responsible for adjusting basis. If the securities are transferred prior to the time an issuer reports the tax consequences of a corporate action, the transferor should be required to amend the transfer report to show the adjusted tax basis resulting from the corporate action.

Broker Practices and Procedures

31. **To what extent a broker should verify the reasonableness of basis information and what document retention requirements should apply;**

- Brokers should be responsible for the reasonableness of basis information captured through trade activity (i.e., purchases, sales, exchanges, redemptions and closing transactions) they (or their agents) process on their own books. However, brokers should not be responsible for validating the reasonableness of information received from a transferor or issuer. Brokers should be allowed to fully rely upon the information received from transferors because the transferring entity is in a better position to know the basis in the transferred security.

- The statute allows brokers to rely on the initial cost basis information that is provided when a security is transferred from another broker or other non-broker transferor. Clearing brokers sometimes share responsibilities for record keeping with introducing brokers, investment managers, mutual fund companies, hedge funds and insurance companies who are not responsible for preparing Forms 1099-B. Introducing brokers or hedge funds may develop and maintain their own systems for order executions. Trades may be executed away from the clearing broker on a receive versus payment or delivery versus payment basis. Clearing brokers should be allowed to rely on basis information received from such non-reporting financial entities on an ongoing basis (not just at the time of the initial transfer). If this information is used by the clearing broker on Forms 1099-B filed with the Service, the clearing broker should not be penalized for inaccurate basis information provided by an of these non-reporting financial entities because the information is outside the clearing broker's control.

- Record retention rules should be the same as provided under existing regulations governing the retention of the information needed to produce the Form 1099.

32. **What procedures a broker should follow if the broker derives basis and holding period information for or from customers with respect to a security that is not a covered security, including potential reporting of such information to either the customer or the Service;**

- As provided in #12, brokers should be allowed to maintain basis information for non-covered securities and should be allowed to report the information on Form 1099-B. However, brokers should not be required to furnish information on non-covered securities to the Service. If brokers choose to report basis information for non-covered securities on Form 1099-B, an indicator should be included to inform the customer and the Service that the security is not covered.

- Brokers should also be allowed to transfer basis information if the non-covered position is transferred to another account.

- Finally, brokers should not be prohibited from using cost basis information provided by customers for non-covered securities if the documentation supplied meets a defined standard of reliability (e.g., copies of old statements or price within the

high/low price range on date of purchase). Brokers that use customer-provided basis information for non-covered securities should include an indicator so that the Service knows the information was provided by the customer.

33. **What procedures a transferee broker should follow if the broker does not receive a transfer reporting statement;**

- If a broker does not receive a transfer reporting statement within the 15-day time limit provided under the statute, the broker should treat the security as non-covered.

34. **What procedures a transferee broker should follow if the broker receives transfer reporting information with respect to a security that is not a covered security, or from a transferor who is not subject to the transfer reporting requirements;**

- As provided in #12 and #32, if brokers receive basis information on non-covered securities, they should have the option to maintain the basis information and use it in preparing a Form 1099-B for filing with the IRS. They should also have the option to report this information to the customer for informational purposes only, but should not be required to furnish the information to the Service.

- As provided in #2, brokers should not be required to validate whether a person transferring basis information is an "applicable person" subject to the transfer reporting requirements.

35. **What procedures a broker should follow with respect to basis adjustments if an issuer report on a corporate action is insufficient or untimely; and**

- If information on corporate actions is not received from the issuer, brokers should use their best efforts to obtain the information needed to adjust basis. In this case, reporting penalties should not apply because brokers should not be penalized for noncompliance by the issuer. Alternatively, a default rule could be applied if the information is not received.

- If the issuer is merely untimely, the broker should make the necessary basis adjustments, even if this requires issuing a corrected Form 1099-B. Again, penalties for filing a corrected return should not apply.

36. **Under what circumstances penalties may apply to brokers or other reporting entities and when relief from penalties should be available.**

- Penalties should not be assessed in the first one or two years after the reporting requirements take effect if the firm shows reasonable efforts to comply with the regulations. Brokers have taken this legislation seriously and are using their best efforts to develop the systems and procedures needed to comply with the new

requirements. Penalties should only apply if the firm shows complete disregard of the requirements.

- After the initial reprieve, penalties should apply to:
    - Applicable persons who fail to provide transfer reporting statements within 15 days of the transfer date (or January 15 of the year following the transfer);
    - Issuers that fail to provide information on corporate actions and security classifications in a timely manner and
    - Brokers that do not maintain, calculate and report basis on covered securities.
- The existing reasonable cause regulations should apply to the basis reporting requirements so that brokers can request relief from penalties in the event of extenuating circumstances. Moreover, penalties should not apply if default methods are used (pursuant to regulations) or if issuer information is not provided in a timely manner. Finally, brokers should be allowed to rely on information received from third-party financial entities without penalty.

Reporting for S Corporation Customers

The statute requires brokers to report gross proceeds and basis information with respect to securities sold by customers that are S corporations. These reporting requirements are effective for securities acquired after January 1, 2011. We would like to offer the following recommendations with respect to the S corporation reporting requirement.

- *Identification of S Corporations*. Many firms have not segregated S corporations from other entities on their databases for *existing* accounts. As a result, broker will need guidance in order to identify S corporations in a consistent manner. While some firms have an S corporation identifier, they may not have used it consistently since it did not affect tax reporting or withholding. We recommend adding a box to entity section of the Form W-9 for S corporations. The check box would be used by all brokers to accurately identify S corporations for reporting purposes. The Service should provide a new Form W-9 and instructions as soon as possible so that brokers can meet the effective date of the legislation.
- *New regulation for W-9 mailings*. We recommend the Service issue a regulatory requirement to solicit or re-solicit W-9 Forms from all corporate payees. The purpose of this solicitation is to require corporations to identify themselves as S or C corporations so that brokers can comply with the statute's requirements.

Changes to the 1099-B Form

Changes will need to be made to the Form 1099-B to accommodate the new basis reporting requirements. The list below represents preliminary recommendations for changes that need to

be made to the form. The list is not exclusive, and we hope to provide broader recommendations for proposed changes to the Form 1099-B in the near future.

- *Combine boxes used for reporting an acquisition of control or a substantial change in capital structure (Form 1099-CAP transactions)*. Old box 5 (No of shares exchanged), box 6 (classes of stock exchanged), and the un-numbered box labeled "Corporation's name" are eliminated. This information is reported in box 7 (formerly called "Description"), which we now propose to call "Description or Corporation's Name."

- *Holding Period*. Box 5 is renamed "Holding Period" with checkboxes to indicate whether the holding period for the securities sold is long-term, mid-term or short-term.

- *Adjusted Basis*. Box 6 is renamed "Adjusted Basis."

- *Covered Security Indicator*. New box 13 is added with checkboxes to indicate whether a security is covered under the new basis reporting law.

- *Source of Basis*. New box 14 is added to indicate the source of the basis information, which could convey the data's reliability. Six sources are suggested: Taxpayer, Broker, Transferor, Issuer, Multiple Sources and Unavailable (i.e., to be used when the cost is truly zero).