



## 2009 Information Reporting Program Advisory Committee Public Report Cost Basis Subgroup

### Notice 2009-17, Reporting of Customer's Basis in Securities Transactions

#### Recommendations

IRPAC provided significant comments and recommendations to the IRS in response to Notice 2009-17 and to more direct questions that have arisen as terms of the new reporting regime are fleshed out. These recommendations are explained in great detail in IRPAC letters dated March 2 ([letter](#) and [full responses to questions](#)) and [June 23, 2009](#). Highlighted below are IRPAC's responses to the more significant issues raised by the questions in the Notice:

A. The IRS should consider issuing guidance on the new cost basis reporting regime in stages. Certain points of critical information are needed immediately; whereas other information may not be needed until later. The IRS should seek public comment to gain a sense of the optimal order in which guidance should be issued. IRPAC believes the following matters should be addressed first:

1. Clarify who is a middleman to which the rules attach.
2. Develop a draft Form 1099-B, Proceeds From Broker and Barter Exchange Transactions, and related instructions, and define the data that must be included on Basis Transfer Statements required under new IRC §6045A.
3. Clarify how to determine reportable S Corporations (S Corps).
4. Establish a course of action for resolving conflicts in classification (e.g., debt versus equity) of covered securities and exempted securities.
5. Outline curative actions on the part of the beneficial owner (burden of proof) where a transferring financial institution refuses to, or cannot pass the information or passes unreliable information.
6. Develop acceptable processes for forensic basis development, as well as allowable uses of data from other sources apart from an upstream financial institution that may have unreliable information.
7. Recognize and reconcile any conflicts with existing Form 1099-B regulations.
8. Release reporting requirements early for mutual funds and options in order for industry to have sufficient time (3-4 years) to develop new systems/change existing systems to comply. See IRPAC letter for suggested points on equity options.
9. Develop a glossary of terms and underlying principles, and consider adding it to the regulations to avoid reader confusion. Glossaries are in both the existing backup withholding regulations and the 1441 regulations.
10. Ensure that the February 15 payee statement due date and its application to all consolidated forms is made a permanent part of the regulations.

B. Although financial institutions, in general, should be well positioned to be the main repositories for basis information, they are unable to observe and track all of the events and taxpayer-level elections that could affect the basis of securities. IRPAC is concerned that customers may be given the flexibility to make or change elections in a manner that does not take into account what is workable for financial institutions. Since it is impractical to require that financial institutions be responsible for tracking all possible events and taxpayer-level elections that affect basis, financial institutions should be treated as passive repositories of basis information, rather than guarantors as to its accuracy.

C. IRS should not strive for perfect reconciliation between the information reported on Forms 1099-B that have cost basis information and the information on the taxpayers' tax returns. This would place an extreme burden on financial institutions, taxpayers, and the IRS.

D. IRS should request comments on defining the content of newly designed information returns and Basis Transfer Statements. As financial institutions will be required to modify their information systems and business practices, one of the most important points of information needed in order to proceed with their projects is a definition of the data that they must capture, store, report, and transmit. Delays in programming for the required data will consequently push back the timeline to become compliant. For example, financial institutions need to know if the following data will need to be reported on 1099s and Basis Transfer Statements:

1. Whether a security is covered,
2. The taxpayer's accounting method (FIFO, average cost, specific ID, etc.),
3. The source of the basis (from transferee financial institution, from taxpayer, etc.),
4. The acquisition date of the security, and
5. Any special taxpayer methodology or elections in place for the basis calculation or other unique information that should be conveyed to an acquiring financial institution regarding basis information.

E. IRPAC notes that recent "visual form" projects, like those in place for new Form 941X, Adjusted Employer's Quarterly Federal Tax Return or Claim for Refund, that partnered with the industry to develop the required schemas, should be considered as a model for the development of a newly designed Form 1099-B and Basis Transfer Statements. IRS should also seek input from organizations such as the Securities Industry and Financial Markets Association (SIFMA), the Investment Company Institute (ICI) and the Depository Trust & Clearing Corporation (DTCC).

F. Information Reporting to Subchapter S Corporations: Under current law, there is no Form 1099-B reporting to corporations, including S Corps. New IRC §6045(g)(5) requires financial institutions, after December 31, 2011, to treat S Corps in the same manner as partnerships, thus subjecting S Corps to Form 1099-B reporting. The following issues should be addressed soon in order to provide sufficient lead time for implementation:

1. Will IRS modify Form W-9, Request for Taxpayer Identification Number and Certificate, to require S Corps to identify themselves? IRPAC recommends simple modifications to Form W-9 to identify these entities, while at the same time recognizing that since the reporting falls under IRC §6045, the taxpayer identification number (TIN) certification is required to be made under penalties of perjury.
2. The IRS should describe how the S Corp reporting effective date would operate. New §6045(g)(4) provides that an S Corp (other than a financial institution) is reportable on Form 1099-B for any sale of a covered security acquired after December 31, 2011. Will S Corp reporting apply only to accounts opened after December 31, 2011, or will it apply to all accounts regardless of when opened? If it applies to all accounts, financial institutions will most likely need to solicit information from their existing account population to determine whether their corporate accounts are S Corps. The number of S Corps holding investment accounts is most likely small; it is difficult to justify the major expense of a mass mailing to all of a financial institution's existing exempt recipient accounts in order to uncover a small number of S Corps.
3. IRS should consider the programming changes financial institutions will need to implement to effect reporting on Forms 1099-B of only the covered assets sold and related basis information. Many financial institutions do not have the capability to screen reporting for only one form of reporting on Form 1099.
4. IRS should consider how IRC §3406 backup withholding provisions will be applied to S Corps.

G. The IRS should request comments regarding the impact that proposed regulations (REG-143686-07 issued January 21, 2009) have on the ability of financial institutions to develop and implement cost basis reporting systems. IRPAC is concerned that the complex method of calculating basis under these proposed and other existing regulations could impede the ability of financial institutions to modify their information systems and business practices in a timely manner. These regulations describe a system of stock basis recovery and stock basis allocation that is currently not used at any financial institution, and was not contemplated during the extensive deliberations on cost basis reporting that industry has had with Congressional and Treasury tax staff over the past several years. See further comments in IRPAC's letter to IRS.

H. The IRS should request comments on a financial institution's responsibility to file corrected basis information returns and Basis Transfer Statements due to information it receives after it files its Forms 1099. For example, if a publicly traded corporation releases new information about its merger or one of its distributions three or four years after the event occurred, should a financial institution be responsible for filing amended information returns and furnishing amended Basis Transfer Statements to reflect the new information? When should a broker's responsibility terminate for purposes of filing corrected information returns? Financial institutions have traditionally had to contend with post year-end adjustments to events that they report on Form 1099-DIV, Dividends and Distributions. However, when new information becomes available several years after the initial Form 1099 filing, amending information returns causes a significant disruption to taxpayers and financial institutions. For further explanations of these concerns and detailed recommendations on how to handle them, see IRPAC's March 2 and June 23, 2009 letters.

I. Conflicts on the meaning of "account" within the different industries affected by the new rules will make uniform application of the new reporting regime difficult. The definition of "account" can vary from one industry to another. Most brokers and banks are prepared to handle wash sale rules for all identical securities held in the same account and the generally understood definition of single account may not pose concern in this application. However, to impose a restriction that would force separate accounts for securities that are subject to tax lot accounting from those mutual

funds where averaging is being used would pose hardship. An imposition of a rule that would disallow the investments in the same account from having multiple tax basis calculation methods could cause harm to the capital market structure surrounding the accounts and have the unintended consequences of reducing investment. IRPAC suggests that consideration be given to reading this restriction regarding multiple methods of calculation in the same "account" as meant to apply to the same position (same Committee on Uniform Security Identification Procedure number) rather than all securities in the same account. IRS should restrict multiple ways of calculating basis to the same position in the same account, similar to the application of the wash sale rules to identical securities held in the same account.

J. The IRS should exercise additional discretion when imposing penalties for failure to comply with the new basis reporting rules, especially during the early years of the new regime. Basis reporting represents a major shift in responsibility for retrieving, maintaining, and processing large amounts of data. IRS should consider the following:

1. Complex systems development will take several years and in some cases actually affect the underlying trade processing systems;
2. The recent economic downturn has affected the financial community particularly hard so that funds available for systems development and training are minimal to none;
3. Developmental issues are complex, even on matters as simple as who owns needed data, and it will take time to work through the processes;
4. Financial service providers are traditionally not tax return preparers.

#### **Discussion**

IRPAC truly appreciates the opportunity to dialogue with the IRS and to provide comments on the development of a new cost basis reporting regime. IRPAC commends IRS efforts to seek comments from the public through Notice 2009-17. Cost basis reporting presents many complex challenges and will require close cooperation between the IRS and private industry.

This new venture will require a substantial learning curve, even for those with sophisticated cost basis systems already in place. Staff must be trained to perform cost basis work. Reporting tax basis information requires a new business culture that involves taking ownership of what traditionally has been the client's purview. IRPAC's comments reflect input from a variety of sources, including tax preparers, securities brokers, mutual fund companies, transfer agents, and tax advisors. IRPAC respectfully looks forward to continued engagement with the IRS in the coming years to discuss guidance and solutions toward practical and effective cost basis reporting.

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