

Impose Basis Reporting Requirements for Publicly-Traded Securities

Present Law

In general

Gain or loss generally is recognized for Federal income tax purposes on realization of that gain or loss (for example, through the sale of property giving rise to the gain or loss). The taxpayer's gain or loss on a disposition of property is the difference between the amount realized and the adjusted basis.¹

To compute adjusted basis, a taxpayer must first determine the property's unadjusted or original basis and then make adjustments prescribed by the Code.² The original basis of property is its cost, except as otherwise prescribed by the Code (for example, in the case of property acquired by gift or bequest or in a tax-free exchange). Once determined, the taxpayer's original basis generally is adjusted downward to take account of depreciation or amortization, and generally is adjusted upward to reflect income and gain inclusions or capital outlays with respect to the property.

Basis computation rules

If a taxpayer has acquired stock in a corporation on different dates or at different prices and sells or transfers some of the shares of that stock, and the lot from which the stock is sold or transferred is not adequately identified, the shares deemed sold are the earliest acquired shares (the "first-in-first-out rule").³ If a taxpayer makes an adequate identification of shares of stock that it sells, the shares of stock treated as sold are the shares that have been identified.⁴ A taxpayer who owns shares in a regulated investment company ("RIC") generally is permitted to elect, in lieu of the specific identification or first-in-first-out methods, to determine the basis of RIC shares sold under one of two average-cost-basis methods described in Treasury regulations.⁵

Information reporting

Present law imposes information reporting requirements on participants in certain transactions. Under these requirements, information is generally reported to the IRS and furnished to taxpayers. These requirements are intended to assist taxpayers in preparing their income tax returns and to help the IRS determine whether taxpayers' tax returns are correct and

¹ Sec. 1001.

² Sec. 1016.

³ Treas. Reg. sec. 1.1012-1(c)(1).

⁴ Treas. Reg. sec. 1.1012-1(c).

⁵ Treas. Reg. sec. 1.1012-1(e).

complete. For example, every person engaged in a trade or business generally is required to file information returns for each calendar year for payments of \$600 or more made in the course of the payor's trade or business.⁶

Section 6045(a) requires brokers to file with the IRS annual information returns showing the gross proceeds realized by customers from various sale transactions. The Secretary is authorized to require brokers to report additional information related to customers.⁷ Brokers are required to furnish to every customer information statements with the same gross proceeds information that is included in the returns filed with the IRS for that customer.⁸

A person who is required to file information returns but who fails to do so by the due date for the returns, includes on the returns incorrect information, or files incomplete returns generally is subject to a penalty of \$50 for each return with respect to which such a failure occurs, up to a maximum of \$250,000 in any calendar year.⁹ Similar penalties, with a \$100,000 calendar year maximum, apply to failures to furnish correct information statements to recipients of payments for which information reporting is required.¹⁰

Present law does not require information reporting with respect to a taxpayer's basis in property but does impose an obligation to keep records, as described below.

Basis recordkeeping requirements

Taxpayers are required to "keep such records . . . as the Secretary may from time to time prescribe."¹¹ Treasury regulations impose recordkeeping requirements on any person required to file information returns.¹²

Treasury regulations provide that donors and donees should keep records that are relevant in determining a donee's basis in property.¹³ IRS Publication 552 states that a taxpayer should keep basis records for property until the period of limitations expires for the year in which the taxpayer disposes of the property.

⁶ Sec. 6041(a).

⁷ Sec. 6045(a).

⁸ Sec. 6045(b).

⁹ Sec. 6721.

¹⁰ Sec. 6722.

¹¹ Sec. 6001.

¹² Treas. Reg. sec. 1.6001-1(a).

¹³ Treas. Reg. sec. 1.1015-1(g).

If a taxpayer does not keep adequate records, the absence of those records may be used as evidence that, if they had been available, the records would have contradicted the taxpayer's assertions.¹⁴

Description of Proposal

In general

The proposal provides that in every case in which a broker is required under section 6045(a) to file with the IRS a return reporting a customer's gross proceeds with respect to any applicable security, that broker is required to include in the return the customer's adjusted basis in each applicable security and information necessary to determine the customer's holding period in that security. The broker also is required to include this information in the statement required to be furnished to a customer under present-law section 6045(b).

Present-law penalties for failure to comply with the requirements of section 6045 also apply to failures to comply with the new basis and holding period reporting requirements.

The proposal applies to applicable securities acquired by purchase or by other means such as gift or inheritance.

Applicable security

An applicable security is any one of the following securities if market quotations for the security are readily available on an established securities market (within the meaning of section 7704) on the date of the acquisition of the security: a share of stock in a corporation; a partnership or beneficial ownership interest in a widely held or publicly traded partnership or trust; a note, bond, debenture, or other evidence of indebtedness; an interest rate, currency, or equity notional principal contract; evidence of an interest in, or a derivative financial instrument in, any security described immediately above or any currency, including any option, forward contract, short position, and any similar financial instrument in such a security or currency; and a position that is not a security described immediately above, is a hedge with respect to such a security, and is clearly identified as such in the dealer's records before the close of the day on which it was acquired or entered into (or such other time as the Secretary may prescribe in regulations).

An applicable security also includes (whether or not market quotations are readily available on an established securities market) any interest in a regulated investment company (as defined in section 851); any interest in a real estate investment trust (as defined in section 856) that is subject to registration with the Securities and Exchange Commission; and any other financial instrument designated in Treasury regulations.

¹⁴ E.g., *Schooler v. Commissioner*, 68 T.C. 867 (1977) (failure to substantiate alleged gambling losses).

An instrument issued by a foreign entity is an applicable security if the instrument otherwise satisfies the requirements for being an applicable security.

Application to publicly-traded options and to corporate recipients

Notwithstanding any Treasury regulations prescribed before the date of enactment of the proposal, the proposal makes the present-law gross proceeds reporting requirements and the new basis and holding period reporting requirements applicable to options for which market quotations are readily available on an established securities market on the date of the acquisition of the options. Also notwithstanding any Treasury regulations prescribed before the date of enactment of the proposal, the proposal applies the gross proceeds, basis, and holding period reporting requirements to applicable securities held for customers that are corporations.

Furnishing of information on transfers of applicable securities

Under the proposal, every broker that transfers an applicable security to another broker must furnish to that other broker a written statement with information necessary to enable that other broker to comply with the new basis and holding period reporting requirements. The Secretary may prescribe regulations setting forth the manner of furnishing this statement and the information required to be included in the statement. The proposal permits the Secretary to provide regulations extending this new information statement requirement to persons other than brokers. For example, regulations may require individuals to provide basis and holding period information to brokers when those individuals transfer applicable securities to brokers. It is not intended that an individual be able to avoid basis reporting requirements by, for example, directing a broker to transfer to that individual certificates for shares and by subsequently transferring those shares, without basis and holding period information, to a new broker.

Any required statement must be furnished not later than the earlier of (1) 45 days after the date of the transfer of an applicable security or (2) January 15 of the year following the calendar year during which the transfer occurred.

The new broker information statement is treated as a payee statement under section 6724(d)(2). Consequently, the penalties applicable to failures to furnish correct payee statements apply to failures to comply with the new information statement requirements.

Information reporting when issuer actions affect basis

The proposal imposes new reporting requirements when actions undertaken by issuers of applicable securities affect the basis of those securities.

Under regulations or forms prescribed by the Secretary, any issuer of an applicable security must file a return setting forth a description of any organizational action that affects the basis of the applicable security; the quantitative effect on the basis of the applicable security resulting from the action; and any other information prescribed by Treasury regulations. This return must be filed not later than the earlier of (1) 45 days after the date of the action or (2) January 15 of the year following the calendar year during which the action occurred.

Every issuer required to file a return for an organizational action that affects the basis of an applicable security also must furnish to each holder of that security a written statement showing the name, address, and phone number of the information contact of the issuer; the information required to be shown in the return; and any other information required by Treasury regulations. If an applicable security is held by a person as a nominee (for example, a broker), the written statement must be furnished to the nominee (rather than to the beneficial owner). The written statement must be furnished to the holder (including to a nominee) on or before January 31 of the year following the calendar year during which the organizational action occurred.

A person (such as a broker) who holds an applicable security as a nominee for another person must furnish to that other person, in the manner prescribed by the Secretary, the information required to be provided by the issuer to a holder (including to a nominee).

The proposal permits the Secretary to waive either or both of the return filing and information statement furnishing requirements if the issuer required to file a return for an organizational action makes certain required information publicly available in the form and manner as the Secretary determines necessary to carry out the purposes of the new reporting requirements. Under its authority, for example, the Secretary may provide, or sanction the use of, an electronic repository of information related to corporate actions that affect the basis of applicable securities.

The required issuer return is treated as an information return under section 6724(d)(1)(B), and the required information statement is treated as a payee statement under section 6724(d)(2). Consequently, the present-law penalties under sections 6721 and 6722, respectively, apply to failures to comply with the new reporting rules.

Basis computation rules

The proposal modifies the section 1012 basis computation rules (the first-in-first-out, specific identification, and average cost basis rules). Under the modification, the basis of any applicable security for which basis and holding period reporting is required is determined on an account by account method. For example, when a broker effects a sale for a customer of some or all of the customer's holding of an applicable security from an account with that broker, the customer's basis in the security is determined by reference only to the customer's holding of that security in the same account and not by reference to any shares of that security that the customer may hold in an account with another broker.

Effective Date

The proposal applies to securities acquired after the date that is 18 months after the date of enactment.