IRPAC Preliminary Comments as of March 2, 2009
Notice 2009-17 - IRS Request for Comments on Reporting Customer's Basis in Securities Transactions

Applicability of Reporting Requirements		
Issue From IRS		**Response**
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	• "Middleman" required to report basis information must be defined the same as under existing rules for determining who is the reporting broker for 1099-B purposes, including adopting the "multiple broker" rule [i] and the "cash on delivery account" [ii] reporting deferral. It will be important that basis information be reported by the same broker that has contractual responsibility for reporting the sale proceeds. • The party required to provide the transfer reporting statement needs to be defined broader than the IRC §6045 reporting broker. Moreover, components of basis information may come from different parties. Basis information can be housed in many different locations including with investment advisors, transfer agents and employers (regarding stock purchase plans and options) who are not considered brokers under IRC §6045. • If the goal to is to track cost basis through to the ultimate sale of the security, then any party that effects purchases or holds securities in some fashion must be responsible to track cost basis so as to be able to forward that information to a broker or to IRS if a sale occurs. • Today, many different service providers can be involved in warehousing and developing information necessary for basis calculations. Debt maintenance outsourced to one provider, OID and other income related basis adjustments maintained by another service, equities to another, reorganization information in yet another, customer statements to another, etc. In addition, data needed to produce the combined product can actually be owned by different parties. Regulations should contemplate this possible diverse processing environment and be as flexible as possible in allowances for many different means of accountabilities. • To facilitate that task of allocating reporting responsibilities among various industry participants, IRPAC offers to develop a glossary of terms and underlying principles and suggest that the IRS consider adding such a

		glossary to the regulations to avoid reader confusion of the final regulations. (Glossaries are in both the existing backup withholding regulations and the 1441 regulations.)
2	Who, in addition to brokers, should be treated as "applicable persons" subject to the transfer reporting requirements	• Regulations need to address whether a party can be required to provide the transfer reporting statement and not be a §6045 reporting broker. Brokers should be able to use the best basis information available regardless of its source. • "Applicable persons" should include: transfer agents [iii] ; investment advisers [iv]; stock plan administrators and employers regarding equity based compensation such as restricted stock, employee stock purchase plans, qualified and non-qualified stock option exercises, etc. ; issuers' shareholder services; bank trust departments; accounting trustees for non tradable securities; CPA firms who do K-1 reporting for master limited partnerships; trustees for Grantor Trust or WHFIT entities or other alternative investments; IRA custodians for distributions of stock at fair market value for 1099-R reporting; foreign brokers holding for U.S. clients; to name a few. • Third party services also track this information under contract to the client, the investment advisor, the broker, or even to the client's tax service. Their historical data can be better than data the reporting broker holds in its records and it should be allowed as a reliable reporting source. Recognizing other viable sources of basis information will be important to encourage compliance particularly from small or midsize brokers and financial services who do not own their operating systems. • In addition, the client should be allowed to provide historical data from their tax records. It is important to remember that the client has elected a method of accounting for existing securities to which they may want to increase their positions and may have separate tax records to support their basis. This is particularly the case where securities may be transferred to a broker from a transfer agent. • Rules need to be flexible enough to allow a broker to acquire the best data

		available from whatever source, but strong enough to produce basis information where the transferring broker has it to deliver and there is no other source. • In addition, the new rules need to outline what is acceptable evidence of basis information if coming from other than an "applicable person."
3	Whether the issuer's classification of an instrument (e.g., as stock or debt) should determine which effective date applies	• Brokers generally rely on their own existing security master files and systems to classify securities. Not all master file classifications are the same from one broker to another. Brokers can and do disagree with each other and sometimes even with the issuer on classification matters. • Looking to an issuer's classification of an instrument to determine the effective date is deceptively too simple a strategy, however, and begs the broader question whether and how the broker can obtain the issuer's classification where it is missing or where there is conflict between brokers in the classification. • In practice, the real concern arises where the issuer is not clear on the tax classification of the instrument. It is the more complex securities that pose the difficulties, such as certain exchange-traded funds (ETFs) that may be partnerships or mutual funds or WHFITs, or products that combine attributes of several instruments, for example, stock with an option or stock with a forward contract, or that masquerade as other products such as units that trade like preferred stock but are actually debt instruments. • Issuers do not always tax-classify the more complex securities. Instead, the prospectus or red herring poses long and detailed descriptions of what it could be. For decades, the lack of a clear tax classification requirement for new issues has caused variances from one broker to another on how a security has been classified. These problems will carry over into the tax basis reporting tasks. • Unless there are teeth to require the issuer to publish a binding tax classification, extending the effective date determination to the issuer's classification will only add to the difficulties already present when a

		security's classification is unknown. It is important to note that issuers are not required to tax-classify instruments under securities laws for the instrument to trade in the market place, only to disclose the tax risks. It is these more difficult instruments that a broker has trouble identifying and will have trouble determining the effective date just like they presently have trouble in classifying related income. By the way, taxpayers also have trouble determining basis for much the same reasons. • For basis reporting to be successful, it is important that the regulations establish a course of action in resolving conflicts in classifications of covered securities. Defaulting to an issuer who fails to step up and resolve the matter will not solve the problem. Without some formal requirements, if a broker were to ask an issuer to clarify, it is not likely the issuer will address or respond beyond what is in the prospectus. • The best solution has been recommended by IRPAC in the past in the context of many different tax reporting issues, which is for the IRS to establish some clearing facility, like Pub. 1212 for OID that lists and classifies securities that pose these types of concerns. See the recent IRPAC notes on WHFITs. A solution would be to target issuers of the more complex products on Wall Street, such as WHFITs, and to require them to file a classification report with the IRS that would publish it. Brokers will not be able to solve this classification problem without IRS help to bridge the gap with issuers.
Basis Method Elections		
Issue From IRS		**Response**
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	• A reasonable method for all stakeholders would be to include such information in account-opening documents, which could allow taxpayers to select one of the basis determination methods that a Broker supports. The IRS should also permit Brokers to communicate this information electronically.
5	How to facilitate customer elections of	• It should be stressed that maximizing customer flexibility and minimizing

	acceptable basis determination methods, including average cost basis, for an account to maximize customer flexibility and minimize broker burden	broker burden are, at times, diametrically opposed objectives. What may be needed is a simplification of the alternative ways to calculate cost basis. For example, instead of two average cost methods perhaps, one might suffice for 1099 reporting purposes; while taxpayers who want to use a different average cost method should be allowed to do so on their Form 1040. • It would be very helpful for the IRS to develop a booklet that explains the different elections for basis calculation that ties to the broker reporting requirements. Currently the information is imbedded in many different publications. See Pub. 551, *Basis of Assets*; Pub. 550, *Investment Income and Expenses*, and Pub. 564, *Mutual Fund Distributions*. It would also benefit taxpayers if the IRS updated these publications to reflect the new basis reporting rules for Brokers. • It is important to note that not all Brokers will be able to offer all methods and elections for calculating basis. Existing GLAS systems were developed looking to the process that the majority of clients would elect to follow. Costs will be very prohibitive to make major modifications to these systems to accommodate a small number of clients. For example, few GLAS systems allow for an election to recognize market discount over the life of a taxable bond. Taxpayers may still need to make adjustments to basis amounts reported on Form 1099. It will be important to allow for the most flexibility possible in writing these requirements. • Consideration needs to be given to calculation variances between brokers on transferred accounts particularly involving mutual funds where for example, one broker uses the single category method and the new broker offers only 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	• Changes to cost basis calculation methods must be minimized to assure the integrity of the process. The IRS will need to specify terms for the rare events where elections to change would be authorized, such as transfer to another broker who does not have the support capabilities for the method in current use. • Where allowed, a new account could be set up under the other method of

		accounting and taxpayers would then transfer chosen assets to that account if they wish to change methods. Where this requires basis adjustments, clients will need to provide that information to the broker in some formalized process. • Keep in mind that where average cost basis is utilized, a limited amount of specific tax lot information will be kept (perhaps 18 months) as storing data is very expensive and keeping two accounting systems for the same account is not reasonable. • In the alternative, the client could elect to have basis tracked and reported by an independent third party that can maintain the new method.
7	What it means to apply the basis determination conventions on an "account-by-account" basis	• Regulations need to define "account" and take into consideration industry variances in meaning: – There is conflict in the definition of "account" between securities brokers and mutual funds. A securities broker's account can hold many CUSIPs and each CUSIP position is broken out by tax lots based on purchase dates. Mutual funds hold the same fund shares in an account. Care needs to be taken in how the term is used. – Many securities brokers allow customers to break an account into several subaccounts reducing the need to acquire several sets of new account customer documentation and allowing for customer special needs to segregate assets. Although they are called subaccounts, they are actually separately maintained, including with separate tax lots. IRS should consider whether a subaccount should be respected as a separate "account" for purposes of this legislation. – Many brokers also allow customers to combine accounts for statement purposes to reduce paper and mailing costs as well as for the convenience of the customer. We think it important that an account be respected as a separate "account" for purposes of this legislation even if consolidated for statement purposes. – Applying basis determinations on an account-by-account basis also means that Brokers should not be required to link events that occur in one account to a taxpayer's assets in another account. For example, assume a taxpayer maintains two accounts with the same Broker. If it

		sells securities in one account in which it realizes a loss, and then purchases identical securities in the other account within the wash sale period so as to cause the loss in the first account to be deferred, the Broker ought not be required to link the purchase in the second account with the sale in the first account. The wash sale rules ought to be applied on an account-by-account basis, rather that on a taxpayer-by-taxpayer basis.
Dividend Reinvestment Plans		
Issue From IRS		**Response**
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")	• Many Brokers offer a dividend reinvestment plan (DRIP) where the Broker enters into the market place and actually buys the stock to supply the purchases from dividend income. Such plans are offered for many different stock issues. It will be important that the final rules address whether these Broker-furnished plans qualify as DRIPs. Rules need to be written very broadly. • Reinvestment plans can vary widely. We suggest that the final rules broadly allow for plans where any income from the shares can be reinvested, not just dividends; to plans that are more restrictive limiting income to be reinvested or where income can be divided and only a portion reinvested; as well as plans that allow clients to contribute fixed amounts periodically for reinvestment.
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	• Security master file or CUSIP numbers are used by Brokers to identify securities for related processing. Most Brokers will not be able to distinguish general purchases from DRIP purchases without significant manual efforts since both positions are maintained under the same identifying CUSIP or security master file number. • Generally in a GLAS system, the chosen tax accounting method is applied to the all the positions in the account with the same CUSIP.

		• To break general purchases out from DRIP purchases to grant separate basis calculations will be an expensive process and for the present manually intensive process for many. • Going forward it will mean some radical programming changes that will take time to implement or the maintenance of the DRIP positions in a separate account. • The better strategy would allow all identical issues of stock held in the same account to fall under the same accounting treatment for the life of the account. • A protocol is needed to work through effective date variances: general stock purchases in 2011are subject to basis reporting in 2011 whereas DRIP purchases are not subject until 2012. Taxpayers will be very confused with basis information provided for some shares and not others. • We recommend that general purchases where the taxpayer elects DRIP application be treated as part of a DRIP and basis reporting not required until 2012.
10	Whether and to what extent the average cost basis method applies to subsequent additions to dividend reinvestment plan accounts by purchase or transfer	• See #9 above.
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	• If the data for pre-effective shares is weak or unclear, Brokers should not treat the pre and post-effective date shares as maintained in a single account.

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Reconciliation with Customer Reporting		
Issue From IRS		**Response**
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	• Brokers should be permitted (not required) to report basis information for uncovered shares. Brokers that elect to report basis information for uncovered shares should be permitted to indicate on the 1099-B that the reporting is with respect to uncovered shares. • IRS should seek input from the public as to the design of the 1099-B. The 941X testing program was very successful and it should stand as a model for the 1099-B draft. SIFMA (Securities Industry and Financial Markets Association) and ICI (Investment Company Institute) could be asked to supply team members from different segments of their industry to review and comment similar to the request made to the APA (American Payroll Association) on the 941X. • Where stock is sold in one trade that covers several tax lots, currently a single 1099-B is produced with the same trade date, etc. Where basis information is available for some and not all of the tax lots, if the single, 1099-B were to be still required, some indicator would be needed to let the client and the IRS know the basis information is incomplete. • Issuing multiple 1099-Bs for a single sale may be impractical for brokers who use trade confirmations as the source of the 1099-B amounts. These Brokers would be required to generate a separate ticket (sale) that would drive a different trade confirmation. Brokers would need to retain staff on this and eservice brokers would have to reprogram their online ticket process. The IRS should recognize that the costs incurred to issue multiple 1099-Bs for a single sale might outweigh the potential benefits that the additional information brings. • Interestingly, in GLAS systems today, the gross proceeds used to calculate realized gains and losses does not originate from the trade tickets, but instead from the statement process after settlement. It is rare, but they can be different numbers.

		• Experience and wisdom tell us that it is important that the 1099-B gross proceeds continue to come from the trade confirmation process as it forces a reconciliation process against the broker's books and records.
13	How to ensure consistency between customers making specific identification of securities sold or transferred and broker reporting	• Comments are still in development and will be relayed shortly.
14	How to ensure that reconciliation is possible if broker reporting should differ from customer reporting	• Details on variances between Broker-reported basis and actual basis should be reported by taxpayers on Schedule D (Form 1040). • Taxpayers (not Brokers) should be responsible for reconciling differences between Broker-furnished basis and actual basis. • If Broker-furnished reporting is incorrect, taxpayers should notify their Broker for a correction. However, Brokers should not be required to amend 1099s and Basis Transfer Statements if a taxpayer elects to change its basis calculation methods, or when additional information is made available after a reasonable period of time.
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	• Flexibility is important to allow for corrections. Many times there is miscommunication between the client and the broker that needs to be repaired and sometimes the client just plain changes their mind. At other times, during fast falling markets for example, it is important that orders be placed without any delay. If the IRS believes that specific identification of tax lots cannot be later changed after the sale (the current rule in place), then the better answer is no corrections and leave it to the 1040 process for the client to adjust and disclose.

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Special Rules and Mechanical Issues		
Issue From IRS		**Response**
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	• See #7 above. • Comments are still in development and will be relayed shortly.
17	How to apply the rules for basis reporting of options	• Comments are still in development and will be relayed shortly. There is some urgency to flushing out these rules as it will take time to develop supporting systems.
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	• Because cash changes hands when the short sale is entered, new rules are needed to address backup withholding responsibilities which currently follow the earlier cash flow where reporting is no longer required.[v]
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	• Consideration needs to be given to protocols for retroactively adjusting basis on securities after they have been transferred to a new broker. Such basis adjustments may become impossible to accomplish once they have moved from one broker to another. • Since these adjustments can come in after the 1099 has been provided to the client for the year (sometimes several years after), consideration needs to be give to establishing reasonable de minimis thresholds to waive corrections. • File transfer layouts will need to be determined that contemplate yearend and later corrections of transmitted data. • Industry groups should be engaged to discuss methodology as some may have instituted programming successfully and can advise. Trying to address all issues simultaneously will result in a suboptimum return on investment and less impact reducing tax gap.

		• Most brokers' retail systems are not set up to handle mark-to-market accounting for clients. Terms, time frames, and abilities will need to be considered by many before final rules that are workable can be established. • It will also be important to remember that debt instrument basis adjustments are fairly sophisticated and not all elections may be readily supportable across the board. For the present, many brokers do not provide basis information on debt instruments apart from initial cost. Those that do provide basis information reach out to third parties to calculate and the cost is pricey. Some brokers may not have the bandwidth or funds to track this information. • Similar issues arise in the context of equity reorganizations.
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	• Current IRC §6045 rules allow for recognition of IRC §988 hedges where security proceeds and currency conversion values are integrated into one 1099-B reportable value. See Reg. §1.6045-1(d)(6). Basis information should be similarly treated to simplify tracking in U.S. dollars and the reporting result. Otherwise, the movement of the currency becomes a separate forward contract subject to its own reporting concerns. Most brokers operate U.S. dollar systems and an integrated approach would be the easiest. • Where IRC §988 hedges are not available, the present reporting requirements for foreign currency are outdated and need to be brought up to date to consider current trading practices. [vi]

Transfer Reporting		
Issue From IRS		**Response**
21	What information about the transferring person, the customer, the security transferred, and the underlying lots should be required on the transfer reporting statements	• Establishing the details necessary for transfer reports needs to be given priority and instructions need to fit the capabilities of the present ACAT/CBRS inter-broker transfer systems. • There currently exist uniform broker-to-broker information transfer standards (ACATs) and a system to accomplish the transfers. The system is Cost Basis Reporting System (CBRS) maintained by DTCC (Depository Trust & Clearing Corporation). • The fact that different classes of securities have varied effective dates only means important decisions need to be made so file layouts for the transmission of this information can encompass all the necessary elements. • Transmitting basis information on paper is often not a realistic option; electronic communication is preferable in most instances. • Information about the customer should not be required on the transfer file, but the file should contain information necessary to associate the basis information to an account at the transferee organization.
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	• The quicker the better, but allowances for the resubmission are necessary to correct previously transmitted errors. Assets must be on a Broker's books in order for a Broker to effect a basis adjustment; once the assets have moved off the Broker's books (e.g., transferred in the ACATs process), a Broker should no longer be responsible for calculating cost basis. • Currently brokers who are part of the CBRS system transmit cost basis information to the new broker (if on CBRS) within 3 days of the assets moving. • Retroactive basis adjustments can become known at anytime (sometimes years after an event has occurred), and unless there are protocols to handle these hindsight adjustments on transferred securities, there will be gaps in reporting. • We strongly suggest a working task force between the IRS and SIFMA and ICI be developed to explore workable industry options.

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 whether multiple lots should be transferred on a pro-rata basis. • Typically a system set to default to FIFO will transfer securities on that basis as well. If customers are allowed to transfer specifically identified securities as opposed to tax lots, brokers will likely have to reprogram their systems or will have to manually adjust records. • Generally when an account transfers, the entire account transfers to another broker. More frequently brokers would get requests for transfer of certain tax lots to satisfy for example, a gift to family members or to a charity. • Many basis calculation elections may not be supportable by all brokers, such as an election to recognize market discount over the life of the debt instrument. Protocols are needed to address when certain basis information is transferred that will require special treatment that may or may not be processable by the acquiring broker.
24	Whether electronic transfer reporting may be appropriate and, if so, whether a common format should apply	• Yes and Yes. Information received on paper is less likely to be processed correctly as it is easily lost and, at times, illegible. Automated systems currently exist and must be expanded upon. It is possible that another electronic system(s) may need to be developed. • Brokers who are members of DTCC may also be part of the CBRS, but non-DTCC members cannot avail themselves of this system, relegating those transfers to paper and human input errors. This gap needs to be closed to facilitate the reporting process, but it will not happen overnight. • We strongly suggest a working task force between the IRS, SIFMA, ICI and other identified transferring parties be developed to explore workable industry options.
25	Whether brokers and transferring parties may utilize reporting services of third-party intermediaries to meet their transfer reporting requirements	• Outsourcing and division of services: Today's securities processing can be divided among many different service providers. Debt outsourced to one provider, equities to another, customer statements to another, etc. In addition, data needed to produce the combined product can actually be owned by different parties. • Regulations should contemplate this possible diverse processing environment. Are powers of attorney needed to allocate responsibility as

		is currently done with Forms 8655 and 2678?
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	• Probably yes. If a Broker does not know why a transfer statement fails to arrive, it may earmark an item for follow-up making extra work when none is required. • Even more importantly, all information should be transferred that is available to avoid a costly research foray into old records. Even if not "covered" the broker will still more than likely be asked by the client at some point to provide the historical data.
Issuer Reporting		
Issue From IRS		**Response**
27	What information about the issuer and organizational action should be required on the issuer returns and reporting statements	• The parties to any corporate action should provide clear and definitive examples of how the corporate action will affect cost basis. • With clear pre-merger examples, most brokers could effect adjustments after obtaining any fair market value information required from the marketplace. • Particularly if one of the components of the transaction or securities released is not tradable, then unless the value is provided it will go unaccounted for.
28	How to maximize the timeliness of issuer returns and statements and promote public reporting by issuers in lieu of return filing	• Corporate actions are often unique and major transactions that involve legal and accounting teams versed in such matters. Since corporate issuers are the ones who plan and execute the corporate actions, it should be the issuer's expense to have a tax opinion rendered as to the proper way to account for cost basis adjustments. It is unreasonable that the expense of researching the matter fall to thousands of securities firms, who individually could come to different results. See #3 above. The issuer's opinion should be published in advance of a shareholder vote in a shareholder offering document for consideration by shareholders and should be published on the issuer's website. • In cases where fair market valuation (FMV) of a security is needed to calculate a cost basis adjustment, the issuer should post the FMV on its website as soon as possible, but not later than 45 days after the corporate

		action. Owners of securities involved in corporate actions usually desire to have their basis adjusted quickly. • In addition, the IRS may wish to consider alternative notification mechanisms in the case of certain small issuers for which these requirements may not be feasible.
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	• Comments are still in development and will be relayed shortly.
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	• There currently exist uniform broker-to-broker information transfer standards (ACATs) and a system to accomplish it. The system is Cost Basis Reporting System (CBRS) maintained by DTCC. Typically once an account transfer is approved the assets are moved and the cost basis information must follow within 3 days. Usually this is next business day. This means the fifteen day IRS standard and the 45 day corporate standard are not in sync with the more rigorous current state of the art industry standard, but are needed to accommodate those transferring securities outside the ACATs program and where there are processing inconsistencies that need to be researched. By enforcing a more rigorous standard on issuers to provide information more timely, there will be fewer instances of unadjusted basis due to corporate actions flowing between Brokers. Meanwhile, protocols are needed to address corrections and to make retroactive basis adjustments as discussed in #19 and #23 above.
Broker Practices and Procedures		
Issue From IRS		**Response**
31	To what extent a broker should verify the reasonableness of basis information and what document retention requirements should apply	• Brokers should be under no obligation to verify information provided to them. Taxpayers should be responsible for ensuring information transferred to their new account agrees with information from their old account. Document retention rules that currently exist to support 1099

		reporting should also apply to cost basis information included in the 1099 report. Retention requirements should not be extended. Data storage for tax lot accounting usually are the largest databases brokers maintain and extending retention would be burdensome from a cost standpoint.
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	• Some brokers currently hold basis information in their GLAS and would use it for reporting purposes if the IRS sanctions the use without penalty. • The IRS needs to outline curative actions on part of customer (burden of proof) where transferring broker refuses or can't pass information or passes unreliable information that allow the broker to rely on customer provided information. • Acceptable processes and alternative sources of basis information need to be sanctioned to allow for use of data from other sources apart from the upstream broker who may have unreliable information.
33	What procedures a transferee broker should follow if the broker does not receive a transfer reporting statement	• See #32 above for curative suggestions. • A basis record should be passed for all assets, covered and uncovered that are transferred and there needs to be a protocol for requesting and receiving missing records.
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	• Procedures should support acceptance of all data received. The broker may maintain that information on their GLAS and may later transfer that information if the position is later transferred to another broker. • The industry may be divided on whether Brokers should include this information on the 1099B, but firms who wish to include it should not be penalized in so doing if it turns out to be wrong. • An entity that takes possession of a security on behalf of an investor or issuer should be required to both receive and send cost basis upon the transfer of securities even if technically not a §6045 broker. See #1-3 above. • However, if a broker receives securities without information there should be no responsibility to go get it. The security should simply be reported based on the information received or generated by transactions that occur on the broker's systems. • The client has and must remain ultimately responsible for reporting on

		their Schedule D. • See #32-33 above on need for curative provisions.
35	What procedures a broker should follow with respect to basis adjustments if an issuer report on a corporate action is insufficient or untimely	• Actually, the question should be what procedures IRS should follow when a report is insufficient or untimely. Brokers are not in a position to influence issuers, but the IRS is. If an issuer has an insufficient report then there is simply no responsibility for the broker to do an adjustment unless IRS provides rules. If the report is untimely then the broker will no doubt want to do a 'best efforts' adjustment for positions that remain on the book for tax reporting purposes. See #23-33 above on need for curative provisions.
36	Under what circumstances penalties may apply to brokers or other reporting entities and when relief from penalties should be available	• Provisions should be made for lenient application of penalties in first few years as: – System development will take several years; – Due to the economy down turn that has hit the financial community hard, funds for system development are bare to none; – Developmental issues are fairly complex even on matters so simple as to who owns needed data, and it will take time to work through the processes; and – Financial servicers are traditionally not tax return preparers. This is a new venture that will require a substantial learning curve even for those with gain/loss analysis systems (GLAS) already on line. Their tax reporting systems are fundamentally drop-in numbers from existing processes and are not built to support actual tax calculations. Staffs are not tax return preparers trained in tax preparation work. Reporting tax basis information requires a new business culture that involves owning what traditionally has been a client's purview. • Penalties are such an easy subject to bring up but should not be a consideration. It is premature to consider such a question until we are years into the process. There is a tremendous financial cost for building these additional systems and corresponding increase in staff which many erroneously think will just be passed on to the consumer. Let's expend

		our energies focused on the job at hand and through experience we will gather such knowledge necessary to discuss penalties when good and bad behavior is understood.

[i] Multiple broker rule: If a broker is instructed to initiate a sale by a securities or commodities dealer, a bank or a futures commission merchant (that is, an introducing broker), no return of information is required with respect to the sale by that broker. In redemption of stock or retirement of securities, only the broker responsible for paying the holder redeemed or retired, or crediting the gross proceeds on the sale to that holder's account, is required to report the sale. [Reg. §1.6045-1(c)(3)(iii)] From an industry standpoint, the multiple broker rule results in only the clearing broker, that is, the broker who is responsible for paying the holder or crediting the gross proceeds on the sale to that holder's account, reporting the sale on Form 1099-B.

It will be important that basis information be reported by the same broker that has contractual responsibility for reporting the sale proceeds. Splitting the basis reporting requirement from the gross proceeds reporting requirement could potentially cause duplicate reporting. It is strongly recommended that the multiple broker rule be adopted for all 1099-B purposes including basis reporting. Multiple reporting of sales proceeds is a rare occurrence in the industry today since the multiple broker rule has been standardized into industry practice. There may be some concerns with adopting this rule for all purposes, since some GLAS systems that reconcile gains and losses are owned by the introducing broker or an investment advisor. The clearing broker may not own either the GLAS data or the GLAS system. This would need to be worked out between the brokers and advisors contractually.

[ii] Cash on delivery transactions (also known in the industry as the RVP/DVP exception): In the case of a sale of securities through a cash on delivery account, a delivery versus payment account, or other similar account or transaction, only the broker that receives the gross proceeds from the sale against delivery of the securities sold is required to report the sale. If, however, the broker's customer is another broker (second-party broker) that is an exempt recipient, then only the second-party broker is required to report the sale. [Reg. §1.6045-1(c)(3)(iv)] Like the multiple broker rule, this rule is actually a deferral rule that requires the final broker in the chain who is responsible for paying the holder or crediting the gross proceeds on the sale to that holder's account to report the sale on Form 1099-B.
Also like the multiple broker rule, it will be important that basis information be reported by the same broker that has contractual responsibility for reporting the sale proceeds. Splitting the basis reporting requirement from the gross proceeds reporting requirement could potentially cause duplicate reporting. It is strongly recommended that the cash on delivery rule be adopted for all 1099-B purposes including basis reporting. Multiple reporting of sales proceeds is a rare occurrence in the industry today also because this rule has been standardized into industry practice. There may be some concerns with adopting this rule for all purposes, since some GLAS systems that reconcile gains and losses are owned by the investment advisor. The receiving broker may not own either the GLAS data or the GLAS system even though it knows the gross proceeds. This would need to be worked out between the brokers and advisors contractually.

[iii] Under existing regulations, the term *broker* means any person, U.S. or foreign, that, in the ordinary course of a trade or business during the calendar year, stands ready to effect sales to be made by others. [Reg. §1.6045-1(a)(1)] Also under existing regulations, a transfer agent for a corporation that records transfers of securities is a broker only if the nature of the activities of the agent is such that the agent ordinarily would know the gross proceeds from sales. [Reg. §1.6045-1(b)(iv)] Transfer agents do not ordinarily buy and sell securities and take the position that they are not brokers since they would ordinarily not know the gross proceeds from sales. When securities are held directly with an issuer, they are maintained on the books of the transfer agent in the name of the beneficial owner. When a security is to be sold, the owner may instruct the transfer agent to ship the security to a broker to effect the sale. For the present, since transfer agents are not brokers, many do not see they are accountable to tell the broker under these new provisions what the basis was when transferred. Transfer agents do carry original purchase, gift and inheritance information which will be lost if not required to be transferred to the selling broker.

[iv] Many investment advisors have historical basis information for securities they recommend and track gains and losses in these securities for their clients as part of their services. If an investment advisor moves an account from one broker to another broker, the investment advisor should be allowed to supply the basis information to the new broker where available and the new broker should be allowed to rely on it even if the old broker transfers basis data to the new broker in the course of the transfer.

[v] Present regulations read as follows: Reg. §31.3406(b)(3)-2(b)(4): (i) *Amount subject to backup withholding*. --The amount subject to withholding under §3406 with respect to a short sale of securities is the gross proceeds (as defined in §1.6045-1(d)(5)) of the short sale. At the option of the broker, however, the amount subject to withholding may be the gain upon the closing of the short sale (if any); consequently, the obligation to withhold under §3406 would be deferred until the closing transaction. A broker may use this alternative method of determining the amount subject to withholding under §3406 with respect to a short sale only if at the time the short sale is initiated, the broker expects that the amount of gain realized upon the closing of the short sale will be determinable from the broker's records. If, due to events unforeseen at the time the short sale was initiated, the broker is unable to determine the basis of the property used to close the short sale, the property must be assumed for this purpose to have a basis of zero. (ii) *Time of backup withholding*. --The determination of whether a short seller is subject to withholding under §3406 must be made on the date of the initiation or closing, as the case may be, or on the date that the initiation or closing, as the case may be, is entered on the broker's books and records.

[vi] Regs. §1.6045-1(c)(5)(ii) clarifies that §1256(g) defined foreign currency contracts are reportable under the rules for regulated futures contracts. Brokers must report these foreign currency contracts in accordance with the rules for reporting regulated futures contracts. Under Regs. §1.6045-5(c)(ii) regarding determinations of profits or losses from foreign currency contracts, realized profit (or loss) from a reportable contract is to be determined in the case of making or taking delivery by comparing the contract price, *i.e.*, the "strike price," to the "spot price," *i.e*., the contract's market price at the time and place specified in the contract. In the case of a closing by entry into an offsetting contract, the profit (or loss) is determined by comparing the contract price to the price of the offsetting contract. Unrealized profit is determined by comparing the contract price to the broker's price for similar contracts at the close of business of the reporting year.