

NEWSLETTER, Federal Tax Weekly, NO. 7, FEBRUARY 12, 2009, IRS Begins Developing Guidance On New Broker Basis Reporting Rules

IRS Begins Developing Guidance On New Broker Basis Reporting Rules

By Brant Goldwyn, JD

Notice 2009-17

The IRS recently asked for comments on developing proposed guidance on broker reporting of a customer's basis in securities. Brokers will also have to determine whether the resulting gain or loss is long-term or short-term. The guidance reflects mandatory broker reporting under the *Emergency Economic Stabilization Act of 2008 (EESA)*.

CCH Take Away. Stevie Conlon, tax director for GainsKeeper, a division of Wolters Kluwer Financial Services, commented that "The notice is a great first step. It shows the IRS is serious about issuing guidance." The notice has 36 detailed questions, Conlon pointed out. "Anyone who's in this area should read the notice. The notice is well thought out, [but] it indicates how much work there is to do." Brokers "can't write software overnight. They may need a year or two on some key issues, [so they] need the guidance right away to get their work done." Conlon noted that people are unsure whether to wait for the IRS guidance. Her advice is that brokers start revamping their systems.

Covered security

Reporting is required for a sale of a "covered security" acquired on or after the date the law takes effect (the "applicable date"). Covered securities include corporate stock; mutual fund shares; any note, bond, debenture, or other evidence of debt; and any commodity, contract, derivative or financial instrument for which the IRS decides to require reporting. Reporting is required when a short sale is closed and when an option lapses or is exercised.

For corporate stock, the applicable date is January 1, 2011. For mutual funds and dividend reinvestments, the applicable date is January 1, 2012. For any other security, the applicable date is January 1, 2013, unless the IRS decides to apply a later date. For an option grant, the applicable date also is January 1, 2013.

Basis reporting

Generally, the *EESA* requires that stock basis be reported using the first-in, first-out (FIFO) method, unless the customer specifically identifies the stock and notifies the broker at the time of the sale or transfer. The basis of stock and mutual fund shares acquired through a dividend reinvestment plan must be determined using the broker's default method under Code Sec. 1012, which includes FIFO, specific identification, and average basis.

Comment:

A mutual fund may elect, on an individual stockholder basis, to use the average basis method and apply it to all shares held, including shares acquired before the applicable date of January 1, 2012.

IRS topics

The IRS asked for comments on a range of issues raised by the new requirements:

- Applicability of the reporting rules -- who is a broker or a middleman?;
- Basis method elections by a customer;
- Dividend reinvestment plans, including additions by purchase or transfer;
- Reconciliation of broker and customer reporting;
- Special rules, for example, wash sales, short sales and options; and mechanical adjustments, such as premiums and discounts;
- Transfer reporting for transactions between brokers or other parties;
- Issuer reporting, for example, corporation actions such as a stock split; and
- Broker practices and procedures, including document retention and penalties.

Comment:

The range of topics and questions raised by the IRS foreshadows the likely length and complexity of the reporting required in any upcoming IRS guidance.

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