

CRS Report for Congress

Tax Gap: Proposals in the 110th Congress to Require Brokers to Report Basis on Publicly Traded Securities

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Summary

Recent and projected large deficits and the need for revenue to offset spending or tax reduction proposals generated congressional and executive branch interest in reducing the tax gap. Proposals in the 110th Congress to require brokers to report adjusted basis on publicly traded securities sold by individuals are examined in this report because this is a source of revenue. Basis is the amount a taxpayer uses to determine the cost of acquiring an asset, which is used to determine the asset's capital gain or loss. In order to calculate the appropriate "adjusted basis" for tax calculations the original cost may have to be altered.

Proposals to report basis were included in the President's FY2008 Budget and FY2009 Budget and are initially discussed in this report. Then the Senate Finance Committee's draft proposal to report basis on publicly traded securities, which was released on May 25, 2007, is examined. On June 29, 2007, the committee held a hearing on this proposal. Written comments of representatives of private financial associations are examined and legislative implications presented. Lastly, relevant legislation in the 110th Congress is described, including P.L. 110-343.

The President's FY2009 Budget proposes that information reporting to the IRS be expanded to include requiring basis reporting on security sales. The Senate Finance Committee drafted a proposal similar to the proposal in the President's Budget that brokers be required to report basis to the IRS and customers for publicly traded securities. Witnesses at a committee hearing on reporting basis included representatives from five financial associations. The written comments of these witnesses provide useful insights. Numerous implications for drafting legislation to report basis may be derived from their testimony.

Two bills had been introduced in the 110th Congress that would require broker reporting of a customer's adjusted basis in securities transactions. These bills, H.R. 878 and S. 601, have almost the exact same wording and the same title, the *Simplification Through Additional Reporting Tax Act of 2007*. Nine other bills have been introduced in the 110th Congress that include a section to raise revenue by requiring broker reporting of customers' basis to the Internal Revenue Service on the sale of publicly traded securities. These bills are H.R. 2147 (*Healthy Kids Act of 2007*), H.R. 3395 (*Responsible Fatherhood and Healthy Families Act of 2007*), H.R. 3970 (*Tax Reduction and Reform Act of 2007*), H.R. 5720 (*Housing Assistance Tax Act of 2008*), S. 1111 (*Fair Flat Tax Act of 2007*), S. 1626 (*Responsible Fatherhood and Healthy Families Act of 2007*), S. 2362 (*Property Tax Fairness Act of 2007*), S. 3335 (*The Jobs, Energy, Families, and Disaster Relief Act of 2008*), and HR. 1424 (*Emergency Economic Stabilization Act of 2008*). On October 3, 2008, President George W. Bush signed H.R. 1424 into law (P.L. 110-343), which included Section 403, "Broker Reporting of Customer's Basis in Securities Transactions."

This report will not be updated.

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Introduction

Recent and projected large deficits and the need for revenue to offset spending or tax reduction proposals generated congressional and executive branch interest in different proposals to reduce the tax gap; and consequently, raise additional revenue.¹ Proposals in the 110th Congress to require brokers to report adjusted basis on publicly traded securities sold by individuals are examined in this report. Basis reporting can help clarify the actual amount of capital gains and thus the tax revenue from such gains may rise if capital gains have been under reported. Basis is “the amount a taxpayer uses to determine the cost of acquiring an asset, which is used to determine the asset’s capital gain or loss.”² The original cost may have to be altered in order to calculate the appropriate “adjusted basis” for tax calculations. For example, the original cost of a purchase of stock would be adjusted upwards to account for brokerage fees.

The Internal Revenue Service (IRS) defines the tax gap “as the aggregate amount of true tax liability imposed by law for a given tax year that is not paid voluntarily and timely.”³ The IRS defines the true tax liability for any given taxpayer as “the amount of tax that would be determined for the tax year in question if all relevant aspects of the tax law were correctly applied to all of the relevant facts of that taxpayer’s situation.”⁴ For the 2001 tax year, IRS estimated that the gross tax gap was approximately \$345 billion.⁵ After enforcement efforts and late payments, this gross tax gap was reduced over several years by an estimated \$55 billion to equal a net tax gap of \$290 billion as reported in 2007.⁶

¹ The last section of this report describes the passage of P.L. 110-343 (*Emergency Economic Stabilization Act of 2008*), which included Section 403 requiring brokers to report customers’ adjusted gross basis for their securities transactions.

² *The Encyclopedia of Taxation and Tax Policy*, edited by Joseph J. Cordes, Robert D. Ebel, and Jane G. Gravelle (Washington, DC: The Urban Institute Press, 1999), pp. 22-23.

³ Internal Revenue Service, *Reducing the Federal Tax Gap, A Report on Improving Voluntary Compliance*, Washington, Aug. 2, 2007, p. 6.

⁴ Ibid.

⁵ Ibid., p. 8.

⁶ Ibid.

Current law requires brokers to report annually the name, address, and gross proceeds of each sale by a taxpayer to the IRS. Brokers are also required to report this information to each customer.⁷ The term broker includes “a dealer, a barter exchange, and any other person who (for a consideration) regularly acts as a middleman with respect to property or services.”⁸ An individual taxpayer’s gain or loss is the difference between the amount realized on the sale of property and the adjusted basis. Because brokers are currently not required to report adjusted basis to the IRS, there is no third-party reporting of adjusted basis; consequently, the ability of the IRS to verify the amount of capital gains and losses reported by individuals is limited. Brokers would incur significant costs in reporting adjusted basis, but taxpayers would be relieved of the often substantial costs of calculating adjusted basis to determine capital gains and losses from the sale of securities. According to the IRS, third-party reporting increases voluntary tax compliance.⁹

For tax year 2001, the Government Accountability Office (GAO) found that an estimated 8.4 million out of an estimated 21.9 million taxpayers (or 38%) with securities transactions misreported their securities gains and losses.¹⁰ GAO calculated that the most frequent reason for this misreporting of securities gains and losses was the inaccurate reporting of basis of securities sold.¹¹

The issue of reporting basis is complicated by the following current 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”). 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. 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.¹²

A proposal to report basis was included in the President’s FY2008 Budget and is discussed in this report. The Senate Finance Committee’s draft proposal to report basis on publicly traded securities, which was released on May 25, 2007, is also

⁷ U.S. Code, Title 26, Section 6045 (a) and (b).

⁸ U.S. Code, Title 26, Section 6045 (c).

⁹ For an overview of tax gap and tax enforcement issues, see CRS Report RL33882, *Tax Gap and Tax Enforcement*, by James M. Bickley.

¹⁰ U.S. Government Accountability Office, *Capital Gains Tax Gap: Requiring Brokers to Report Securities Cost Basis Would Improve Compliance if Related Challenges Are Addressed*, GAO-06-603 (Washington: June 2006), p. 10.

¹¹ *Ibid.*, p. 14.

¹² Senate Committee on Finance, *Proposal to Impose Basis Reporting Requirements for Publicly-Traded Securities*, June 29, 2007, p. 1.

examined. On June 29, 2007, the committee held a hearing on this proposal. Written comments of representatives of private financial associations are examined and legislative implications presented. Lastly, relevant legislation in the 110th Congress is described.

President's FY2008 Budget Proposal

The President's FY2008 Budget proposed that information reporting to the IRS be expanded to include basis reporting on security sales.¹³ The U.S. Treasury described this proposal as follows:

Certain brokers (including brokerage houses, mutual funds, asset managers and fiduciaries) would be required to report information regarding adjusted basis in connection with the sale of certain publicly traded securities. The IRS and Treasury Department would be granted regulatory authority to promulgate specific rules, including exceptions, to implement this mandate. Brokers also would be required to report acquisition or disposition dates for securities to determine short-term or long-term gain or loss for taxpayers. To facilitate accurate basis reporting if a customer transfers securities from an account with one broker to an account with another, the transferor broker would be required to provide the relevant information to the transferee. Under regulations, a broker would be exempt from reporting items of information that the broker is unable to obtain with reasonable efforts. Regulations may establish a regime under which customers provide information to their brokers about customer transactions that produce adjustments to basis and about the customers' initial basis in securities when the broker has no other way of knowing this information. Information about basis adjustments that are applicable to all holders of securities of a particular class would be available to brokers either directly from the relevant issuer or indirectly from the issuer through a central repository of information.¹⁴

This reporting proposal would apply to securities acquired after December 31, 2008; consequently, revenue estimates in the first year are not on a fiscal year basis. The Treasury estimates that this reporting proposal would yield revenue of \$1.035 billion for the period of January 1, 2009, through September 30, 2012, and \$6.709 billion for the period of January 1, 2009, through September 30, 2017.¹⁵

¹³ U.S. Executive Office of the President, Office of Management and Budget, *Analytical Perspectives, Budget of the United States Government Fiscal Year 2008* (Washington: GPO, 2007), p. 262.

¹⁴ U.S. Treasury, *General Explanations of the Administration's Fiscal Year 2008 Revenue Proposals*, Washington, Feb. 2007, p. 64. This document is available at [<http://www.treas.gov/offices/tax-policy/library/bluebk07.pdf>].

¹⁵ Ibid.

President's FY2009 Budget Proposal

The President's FY2009 Budget also proposed that information reporting to the IRS be expanded to include basis reporting on security sales.¹⁶ The Treasury's description of this proposal was the same as the same proposal in the President's FY2008 Budget with only a few changes in wording. The U.S. Treasury described this FY2009 Budget proposal as follows:

Certain brokers (including brokerage houses, mutual funds, asset managers and fiduciaries) would be required to report information regarding adjusted basis in connection with the sale of certain securities. The IRS and Treasury Department would be granted regulatory authority to promulgate specific rules, including exceptions, to implement this mandate. Brokers also would be required to report acquisition or disposition dates for securities to determine short-term or long-term gain or loss for taxpayers. To facilitate accurate basis reporting if a customer transfers securities from an account with one broker to an account with another, the transferor broker would be required to provide the relevant information to the transferee. Under regulations, a broker would not be penalized for failure accurately to report items of information that the broker is unable to obtain with reasonable efforts. Regulations may establish a regime under which customers provide information to their brokers about customer transactions that produce adjustments to basis and about the customers' initial basis in securities when the broker has no other way of knowing this information. Information about basis adjustments that are applicable to all holders of securities of a particular class would be available to brokers either directly from the relevant issuer or indirectly from the issuer through a central repository of information.¹⁷

This reporting proposal would apply to securities acquired after December 31, 2009.¹⁸ The Treasury estimated that this reporting proposal would yield revenue of \$1.203 billion for the period of January 1, 2010, through September 30, 2013, and \$7.480 for the period of January 1, 2010, through September 30, 2018.¹⁹

The Joint Tax Committee (JTC) indicated that this proposal "is based on findings that third-party reporting increases compliance."²⁰ Currently, brokers did not report information to the IRS that allows the IRS to calculate gains or losses from securities sales. JTC found that this proposal would reduce compliance costs of

¹⁶ U.S. Executive Office of the President, Office of Management and Budget, *Analytical Perspectives, Budget of the United States Government, Fiscal Year 2009* (Washington: GPO, 2008), p. 259.

¹⁷ U.S. Treasury, *General Explanations of the Administration's Fiscal Year 2009 Revenue Proposals*, Washington, Feb. 2008, p. 64. This document is available at [<http://www.treas.gov/offices/tax-policy/library/bluebk08.pdf>].

¹⁸ *Ibid.*, p. 64.

¹⁹ *Ibid.*

²⁰ Joint Committee on Taxation, *Description of Revenue Provisions Contained in the President's Fiscal Year 2009 Budget Proposal*, committee print, 110th Cong., 2nd sess., JCS-1-08 (Washington: GPO, March 2008), p. 144.

some taxpayers, raise compliance costs of some brokers, and impose significant costs on the Internal Revenue Service.²¹

“Under present law taxpayers must determine the effects of certain actions undertaken by issuers of securities — spin-offs, recapitalization, mergers, and return of capital distributions, for example — on the taxpayers’ basis in those securities.”²² The proposal would relieve some taxpayers from making these calculations concerning basis because brokers would be required to provide this information to customers when securities are sold.²³

Some brokers, particularly brokers with large portfolios, currently provide information about adjusted basis to customers. Other brokers provide partial information or no information concerning basis to their customers. Some brokers may incur additional expenses in meeting the proposal’s reporting requirements.²⁴ The IRS would incur significant costs from altering or creating new forms, processing data including matching data, and storing data.²⁵

Because the proposal would only apply to publicly traded securities, if the cost of compliance is passed onto taxpayers, some taxpayers may shift part of their assets from publicly traded securities to other securities and assets. Some taxpayers may prefer to acquire assets not subject to the requirement that brokers must report basis information to the IRS.²⁶ “The proposal provides few details about which taxpayers and securities would be subject to reporting requirements.”²⁷

Senate Finance Committee’s Proposal

The Senate Finance Committee drafted a proposal, which is almost the same as the proposal in the President’s budget that brokers be required to report basis to the IRS and customers for publicly traded securities. One of the advantages of analyzing this draft proposal is the availability of extensive testimony and background documents provided by witnesses at the committee’s hearing on the proposal.

²¹ As discussed later in this report, the JCT estimated that a provision in H.R. 3970 requiring basis reporting by brokers would yield \$4.27 billion over a 10-year period beginning with stock acquired after Jan. 1, 2009.

²² Joint Committee on Taxation, *Description of Revenue Provisions Contained in the President’s Fiscal Year 2009 Budget Proposal*, p. 144.

²³ *Ibid.*

²⁴ *Ibid.*

²⁵ *Ibid.*, p. 145.

²⁶ *Ibid.*

²⁷ *Ibid.*

Description

The Senate Finance Committee description of its draft proposal included the following excerpts:

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.²⁸

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 proposal imposes new reporting requirements when actions undertaken by issuers of applicable securities affect the basis of those securities.²⁹

The proposal applies to securities acquired after the date that is 18 months after the date of enactment.³⁰

Legislative Implications of Witnesses' Testimony

Numerous implications for drafting legislation to report basis could be derived from the testimony of witnesses from finance associations at the Senate Finance Committee hearing.³¹ Some issues were raised by more than one witness.

First, several witnesses stated that sufficient time should be allowed for brokers to implement the requirements necessary to report adjusted basis. This time period may be approximately two years after Treasury regulations have been written. Witnesses emphasized that some financial intermediaries would have to develop new systems to report basis and other intermediaries would have to reprogram existing

²⁸ Senate Committee on Finance, *Proposal to Impose Basis Reporting Requirements for Publicly-Traded Securities*, June 29, 2007, p. 3.

²⁹ *Ibid.*, p. 4.

³⁰ *Ibid.*, p. 5.

³¹ Views of selective witnesses before the Senate Finance Committee's hearing are presented in the **Appendix**.

systems. From Treasury's perspective, additional time to implement the reporting of basis would result in lost tax revenue.

Second, two witnesses maintained that the flexibility in the methods of reporting basis should be maintained. Currently, a taxpayer may use the "first-in-first-out rule" or the specific identification rule. A taxpayer who owns shares in a mutual fund may use either of these rules or one of two average-cost-basis methods. Many mutual funds report basis to their customers using an average cost method. From the IRS perspective, requiring the use of one standard rule such as "first-in-first-out" would expedite the use of cost basis data for IRS matching purposes.

Third, two witnesses believed that filing requirements should be prospective, based on the date of purchase, or brokers should not be held accountable for errors in data on current and prior reports of adjusted basis. Many brokers do not have records concerning basis and must rely on customers or third parties for information.

Fourth, two witnesses expressed opposition to extending gross proceeds reporting (and thus adjusted basis reporting) to corporate customers because the Secretary of the Treasury already has the authority to extend gross proceeds reporting to corporations, without legislative action if corporations are a significant source of noncompliance.

Fifth, one witness stated that the volume of transfers of securities would preclude a paper transfer system providing brokers with data to calculate adjusted basis; hence, an electronic system would be necessary. Another witness maintained that electronic transmission of transfer data should be allowed as an option.

Sixth, two witnesses argued that the Treasury should have broad authority to implement legislation requiring the reporting of basis. These witnesses maintained that the legislative language in the Senate Finance Committee's draft proposal did not address many issues such as the reporting of gifted and inherited securities and the reporting of options transactions. Congress could specify many of these issues in legislative language, which would result in congressional preference being implemented and a reduced need for Treasury discretion in writing rules.

Seventh, two witnesses maintained that the deadline for filing 1099 statements should be delayed by two weeks, which is addressed by S. 636, the Reduce Wasteful Tax Forms Act of 2007. These witnesses argue that the Senate Finance Committee's proposal would cause such an enormous increase in the year-end processing costs for brokers and custodians that the two week delay would be necessary.

Proposed Legislation in the 110th Congress

Two bills were introduced in the 110th Congress that focused on requiring broker reporting of a customer's adjusted basis in securities transactions. These bills, H.R. 878 and S. 601, had almost the exact same wording and the same title. A third bill, H.R. 3970, included a section requiring the broker reporting of customers' adjusted basis in securities transactions.

On February 7, 2007, Representative Rahm Emanuel introduced H.R. 878, Simplification Through Additional Reporting Tax Act of 2007, which would require broker reporting of customers' adjusted basis in securities transactions. The Secretary of the Treasury would issue regulations in cases in which brokers do not have sufficient information to report basis. These regulations could require other information relating to basis to be reported and could exempt some brokers from any reporting.

On February 14, 2007, Senator Evan Bayh introduced S. 601, Simplification Through Additional Reporting Tax Act of 2007, which would require broker reporting of customers' adjusted basis in securities transactions to the IRS. The contents of S. 601 are almost the same as H.R. 878.

On October 25, 2007, Representative Charles B. Rangel, Chairman of the House Committee on Ways and Means, introduced H.R. 3970, Tax Reduction and Reform Act of 2007. This comprehensive bill is revenue neutral and proposes to eliminate the individual alternative minimum tax.³² This bill includes Section 1221 titled "Broker Reporting of Customer's Basis in Securities Transactions." The House Ways and Means Committee describes this section as follows:

The bill creates mandatory cost basis reporting by brokers for transactions involving publicly traded securities. Covered securities are generally stock, debt, commodities, derivatives and other items as specified by the Treasury Secretary, which are acquired in the account or transferred to the account managed by the broker. The provision applies to stock acquired after January 1, 2009, and after January 1, 2011, for all other instruments. *This proposal is estimated to raise \$4.27 billion over 10 years.*³³

In addition to the current requirement that brokers report the gross proceeds from the sale of a covered security, brokers would be required to report the customer's adjusted basis and whether any gain or loss is long-term or short-term. Long-term capital gains are taxed at a higher rate than short-term capital gains. Every broker that transfers to another broker a covered security would be required to furnish to the transferee broker a written statement that allows the transferee broker to satisfy the proposal's basis and holding period requirements. The bill would change to February 15, from the present-law January 31, the deadline for furnishing certain information statements to customers including statements showing gross proceeds.³⁴

Nine other bills were introduced in the 110th Congress that included a section to raise revenue by requiring broker reporting of customers' basis to the Internal

³² For an overview of the contents of this bill, see CRS Report RL34249, *The Tax Reduction and Reform Act of 2007: An Overview*, Jane G. Gravelle.

³³ U.S. Congress, House Ways and Means Committee, *H.R. 3970, Tax Reduction and Reform Act of 2007*, Description of Provisions, Oct. 29, 2007, available at [<http://waysandmeans.house.gov/>].

³⁴ U.S. Congress, Joint Committee on Taxation, *Description of the Chairman's Amendment in the Nature of a Substitute of H.R. 3996, The Temporary Tax Relief Act of 2007*, Nov. 1, 2007, (JCX-106-07), pp. 123-125. Available at [<http://www.house.gov/jct/>].

Revenue Service on the sale of publicly traded securities. These bills are H.R. 2147 (*Healthy Kids Act of 2007*), H.R. 3395 (*Responsible Fatherhood and Healthy Families Act of 2007*), H.R. 5720 (*Housing Assistance Tax Act of 2008*), S. 1111 (*Fair Flat Tax Act of 2007*), S. 1626 (*Responsible Fatherhood and Healthy Families Act of 2007*), S. 2362 (*Property Tax Fairness Act of 2007*), S. 3335 (*The Jobs, Energy, Families, and Disaster Relief Act of 2008*), and H.R. 1424 (*Emergency Economic Stabilization Act of 2008*).

Emergency Economic Stabilization Act of 2008

On October 3, 2008, President George W. Bush signed H.R. 1424, *Emergency Economic Stabilization Act of 2008*, into law (P.L. 110-343). This act included Section 403, “Broker Reporting of Customer’s Basis in Securities Transactions,” which required brokers to report to the IRS customers’ adjusted gross basis and whether any capital gain or loss is long-term or short-term for customers’ sales of stock, debt, commodities, derivatives, and any other assets specified by the Treasury. The Joint Committee on Taxation estimated that this reporting provision would raise \$6.67 billion in revenue through September 30, 2018.³⁵ January 1, 2011, is the initial applicable date of the reporting provision to customers’ sales of corporate stock.

³⁵ Joint Committee on Taxation, *Estimated Budget Effects of the Tax Provisions Contained in An Amendment in the Nature of a Substitute to H.R. 1424, Scheduled for Consideration on the Senate Floor on October 1, 2008*, JCX-78-08, Oct. 1, 2008.

Appendix. Views of Selective Witnesses on Senate Finance Committee's Proposal

Witnesses at the Senate Finance Committee's hearing on June 28, 2007, included representatives from five financial associations. The written comments of these witnesses provide useful insights. The reader may want to refer to the actual written testimony for details. Numerous implications for drafting legislation to report basis may be derived from their testimony.

Investment Company Institute.³⁶ The Investment Company Institute (ICI) emphasized three points concerning reporting of basis:

First, a mandatory basis-reporting regime will be costly, and the cost ultimately will be borne by fund investors. Second, sufficient time must be provided to ensure that necessary programming and systems challenges are addressed effectively. Finally, the flexibility the current law provides to mutual funds and their shareholders to compute cost basis under any available method (first-in, first-out ("FIFO"), specific identification, and average cost, in the case of fund shareholders) must be maintained. We recognize that allowing this flexibility will limit the use of cost basis information for Internal Revenue Service ("IRS") matching purposes.³⁷

The ICI indicated that many mutual funds currently provide average cost basis information to a substantial portion of their shareholders, but some funds (particularly smaller funds) do not provide any cost basis information.³⁸ No mutual fund provides cost basis information to all of its shareholders because the fund managers do not have or cannot have access to the necessary information or are not confident that the information is accurate.³⁹ The ICI maintains that mutual funds would "need sufficient lead time to program their systems to provide cost basis information to all of their shareholders in all circumstances."⁴⁰ The date applicable to basis reporting should be the later of "December 31 of the calendar year that ends more than 18 months after the date of enactment or December 31 of the first calendar year that ends at least twelve months after the issuance of final regulations by the

³⁶ The ICI is the national association of American mutual funds. As of July 1, 2007, the ICI's members included 8,766 open-ended investment companies (mutual funds), 670 closed-end investment companies, 440 exchange-traded funds, and four sponsors of unit investment trusts. Mutual fund members of the ICI have total assets of approximately \$11.242 trillion (representing 98% of all assets of U.S. mutual funds; these funds serve approximately 93.9 million shareholders in more than 53.8 million households. Source: ICI's website at [http://www.ici.org/about_ici.html].

³⁷ Senate Finance Committee, Investment Company Institute Comments at hearing on Proposed Legislation Requiring Basis Reporting Requirement for Publicly Traded Securities, 110th Cong., 1st sess., June 28, 2007, p. 2.

³⁸ Ibid.

³⁹ Ibid., pp. 2-3.

⁴⁰ Ibid., p. 5.

Secretary.”⁴¹ The ICI maintained that filing requirements should be prospective based on the date of purchase if the fund has not reported cost basis data. If a fund wishes to try and reconstruct basis using “good faith efforts” then the mutual fund would have reasonable cause for any errors.⁴² The internal transfer of shares in mutual funds results in complex recording issues.⁴³ The ICI recommends that the written statement requirement for data on the transfer of stock may also be met using electronic transmittal.⁴⁴

Securities Industry and Financial Markets Association. The Securities Industry and Financial Markets Association (SIFMA) represents the interests of more than 650 securities firms, banks, and asset managers.⁴⁵ SIFMA made five major recommendations.

(1) SIFMA strongly opposes the proposal to extend gross proceeds reporting (and thus adjusted basis reporting) to corporate customers and recommends this proposal be dropped. The Secretary of the Treasury already has the authority to extend gross proceeds reporting to corporations and can exercise this authority without legislative action if corporations are a significant source of noncompliance.

(2) The Secretary of the Treasury should be granted broad regulatory authority to implement the new reporting requirements and to provide safe harbors, uniform adjusted basis calculation rules, simplifying assumptions, and limited exceptions if justified.

(3) The new reporting regulations should be effective for securities acquired 18 months after Treasury regulations are finalized (rather than 18 months after date of enactment). Brokers cannot develop or modify their basis reporting systems if they do not know the rules they must follow.

(4) The definition of “applicable security” should be clarified.

(5) S. 636, the Reduce Wasteful Tax Forms Act of 2007 ... should be incorporated into the proposal.⁴⁶ The new reporting requirements will greatly increase year-end processing for brokers and custodians, thus increasing the number of corrected 1099 and cost basis statements that will have to be issued

⁴¹ Ibid., p. 6.

⁴² Ibid., p. 9.

⁴³ Ibid., pp. 9-11.

⁴⁴ Ibid., p. 17.

⁴⁵ Securities Industry and Financial Markets Association, *Comments to Senate Finance Committee on Proposed Legislation Requiring Basis Reporting Requirement for Publicly Traded Securities*, July 17, 2007, p. 1.

⁴⁶ S. 636, Reduce Wasteful Tax Forms Act of 2007, was introduced by Senator Schumer and referred to the Senate Committee on Finance on Feb. 15, 2007.

to taxpayers and the IRS. S. 636 would delay the filing deadline for 1099 statements by two weeks, from January 31 to February 15.⁴⁷

The Clearing House. The Clearing House Association L.L.C. (The Clearing House), an association of major commercial banks, presented its concerns about the Senate Finance Committee's Basis Reporting Proposal.⁴⁸

The Clearing House states that "the Proposal requires financial institutions to report gross proceeds with respect to securities sold by corporate customers."⁴⁹ The Clearing House states that corporate customers of brokers and financial institutions have generally been exempt from gross proceeds reporting requirements. The reason is that timing and accounting differences would result in mismatches in gross figures being reported to corporate customers and the IRS.⁵⁰ Hence, the Clearing House states that "the cost to implement gross proceeds and basis reporting on payments to corporations will ... be prohibitive with no foreseeable benefit to the Internal Revenue Service or the corporate customers."⁵¹ The Clearing House maintains that financial institutions and brokers would be unable to report adjusted basis and holding period information for certain securities such as foreign securities and securities purchased as part of a dividend reinvestment program.⁵² The Clearing House argues that the proposal's requirement that persons transferring securities to a broker provide that broker with a written statement which includes data to calculate adjusted basis "is inefficient, burdensome, unmanageable and susceptible to error."⁵³ The Clearing House believes that the volume of transfers of securities would preclude a paper transfer system and necessitate an electronic system.⁵⁴

The Clearing House represents large banks that do not collect and send basis or holding period data to their customers; hence, these large banks would have to develop necessary information systems, which would be time consuming. In addition, large banks are currently integrating multiple information reporting systems. Consequently, the Clearing House advocates an effective date for compliance with the proposal of either three years after the date of the passage of the law or two years after the finalization of relevant Treasury regulations.⁵⁵

⁴⁷ Securities Industry and Financial Markets Association, *Comments to Senate Finance Committee on Proposed Legislation Requiring Basis Reporting Requirement for Publicly Traded Securities*, June 28, 2007, pp. 1-3.

⁴⁸ The Clearing House Association L.L.C., *Comments to Senate Finance Committee on Proposed Legislation Requiring Basis Reporting Requirements for Publicly Traded Securities*, June 29, 2007, p. 1.

⁴⁹ *Ibid.*

⁵⁰ *Ibid.*

⁵¹ *Ibid.*, p. 2.

⁵² *Ibid.*

⁵³ *Ibid.*

⁵⁴ *Ibid.*

⁵⁵ *Ibid.*, p. 3.

American Bankers Association. A representative of the American Bankers Association (ABA) provided written comments that stated that the Finance Committee’s proposal raised significant issues among its members. The ABA indicated that while banks serving in fiduciary and related capacities were required to meet Section 6045 filing requirements, they may not be directly involved in either the purchase or sale of securities; hence, they do not have direct access to the necessary information concerning basis or have access only through third-party reporting.⁵⁶ The ABA maintains that the proposal should require that banks receive information from the party that files Form 1099-B, and banks should be able to rely on the accuracy of information from third parties, particularly clients, without penalty.⁵⁷ The ABA argues that the proposal should be effective prospectively and allow sufficient time to implement after regulations have been established.⁵⁸ The ABA maintains that taxpayers should be allowed to continue to select the method of accounting for gains and losses on securities sold.⁵⁹ Finally, the ABA states that the IRS should be provided with broad authority to provide exceptions or safe harbors where determining adjusted basis is difficult or impossible.⁶⁰

National Association of Real Estate Investment Trusts. The National Association of Real Estate Investment Trusts (NAREIT) represents U.S. real estate investment trusts (REITs) and publicly traded real estate companies worldwide.⁶¹ The NAREIT made only one specific comment: “that brokers and mutual funds be provided with an additional two weeks — until February 15th — to report dividend income to taxpayers on IRS Form 1099-DIV.”⁶²

⁵⁶ American Bankers Association, *Comments to Senate Finance Committee on Proposed Legislation Requiring Basis Reporting Requirement for Publicly Traded Securities*, June 29, 2007, p. 2.

⁵⁷ Ibid.

⁵⁸ Ibid., p. 3.

⁵⁹ Ibid., pp. 3-4.

⁶⁰ Ibid.

⁶¹ National Association of Real Estate Investment Trusts, *Comments to Senate Finance Committee on Proposed Legislation Requiring Basis Reporting Requirement for Publicly Traded Securities*, p. 1.

⁶² Ibid.