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Basis Reporting by Securities Brokers & Basis Determination for Stock

Comment On: IRS-2009-0037-0001

Basis Reporting by Securities Brokers and Basis Determination for Stock

Document: IRS-2009-0037-0018

Comment on FR Doc # E9-29855

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General Comment

Please see the attached comment letter from Cameron M. Routh, SVP Strategic Products, Scivantage, Inc. regarding the proposed Basis Reporting by Securities Brokers and Basis Determination for Stock (Document ID IRS-2009-0037-0001).

Best Regards.

Attachments**IRS-2009-0037-0018.1:** Comment on FR Doc # E9-29855



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CC:PA:LPD:PR (REG-101896-09)
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Internal Revenue Service
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Re: FR Doc. 2009-29855 Filed 12/16/2009

Dear Mr. Schaeffer,

Scivantage, Inc. appreciates this opportunity to provide comments on the Basis Reporting regulations being finalized by the Internal Revenue Service (IRS). These regulations will have a profound impact on the financial services industry, altering not only the tax reporting process, but almost every aspect of the investment experience, including new accounts, operations, customer support, online access and trading and financial planning.

The current draft of regulations which have been promulgated by the IRS can be separated into two distinct groups: those which are inconvenient or challenging and those which are logistically problematic. Inconvenient or challenging issues can generally be resolved through determination and ingenuity. Those which have logistic issues may be impossible to resolve or possess an impractical cost-benefit. Given the limited time to finalized regulations and the small window which will be left for firms to implement compliant systems, we recommend focusing on several specific issues which we believe will cause the most difficulty for the industry.

Foreign securities: Tracking cost basis on non-ADR foreign securities has two unique requirements: bifurcating capital gains from currency exchange gains and properly accounting for corporate action events. The currency issues can be solved with technology, although this will necessitate adding another layer to the already complex transfer process, which already poses several issues. The requirement for supporting foreign corporate actions is more problematic and cannot be resolved easily. Data on foreign corporate action events is far less organized and more opaque than data on U.S. events. Given that foreign issuers have no obligation to adhere to these basis regulations, nor U.S. tax principles for that matter, it is certain that attempting to meet





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this standard will be expensive, distract from addressing other critical regulations and, ultimately most firms will likely fall far short of satisfying this requirement, regardless of effort. It is our recommendation that reporting on non-ADR foreign securities be delayed until 2013 or until a better system for collecting and distributing accurate, reliable corporate action data can be implemented.

Asset Classification: For purposes of determining the applicable date for basis reporting, the proposed regulations state that any security classified by an issuer as stock should be treated as such. However, if no classification has been made the regulations only allows a security to be treated as stock if, "the broker knows, or has reason to know, that the security is reasonably classified as stock under general tax principles." This may result in further complications to the transfer process. One broker may believe a security, which has not been classified by the issuer, is a debt instrument which is not covered in 2011; while another broker may have reason to classify the same security as stock, which is covered in 2011. In the transfer process, this would result in the failed expectation of basis being provided in the transfer statement. As a result, the delivering broker may be subject to penalties and the receiving broker will be forced to treat as noncovered the same security that it otherwise treats as covered in the same account. Aside from the confusion this will cause in the transfer process, the receiving broker may have two lots for the same security with post-legislation acquisition dates the must receive different treatment in the same account. It is our recommendation that all issuers be required to determine, without exception, the asset classification of its securities for purposes of determining applicable date for basis reporting.

Reporting options impact on stock basis: the proposed regulations allow a broker to report noncovered securities voluntarily. They do not, however, address reporting the impact of noncovered securities on covered securities. Brokers that already possess the ability to properly carry option premiums to the basis of underlying securities in the event of assignment or exercise may find it preferable to report the stock basis fully adjusted for the option activity. We believe it is consistent with reporting noncovered securities in general to permit brokers to report options-adjusted stock basis voluntarily.

Wash sale reporting on high volume accounts: the regulations specifically noted that comments requesting exemptions from calculating wash sales on high frequency accounts would not be adopted, even in the case of a taxpayer who has been approved for professional status and the use of mark-to-market accounting. We strongly recommend that this issue be reconsidered by Treasury. The cost of properly calculating wash sales on high volume accounts can be significant and may not benefit either Treasury or the investor. While there is no exact correlation between the frequency of





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trading and the prevalence of wash sales, it is not unrealistic for a single account, trading a single security, to trade 10,000 times in a single tax year and generate millions of wash sale adjustments. The cost of calculating and storing this data can be significant. The effort to generate reports with this data adds greater costs and has practical limitations. This high cost and effort is significantly disproportionate to any value gained. The wash sale rule is designed to prevent investors from taking artificial losses. The strategy of high frequency traders is to capitalize on small price fluctuations which occur during a single market session. The notion of harvesting losses, even taking the time to determine the availability of potential losses, is contrary to the behavior of high frequency traders. It is our recommendation that an exception be created to exempt reporting wash sales on accounts which either are entitled to use mark-to-market accounting under Section 475, or trade more than 10,000 times in a single tax year.

Accepting basis in transfer: the proposed regulations provide that basis “must be furnished to the receiving broker not later than fifteen days after the transfer of the covered security.” The receiving broker is obligated to notify the delivering party once, after which the security may be classified as noncovered if no response is received prior to the security being sold or transferred. This open-ended timeframe puts undue responsibility on the receiving broker to accept basis potentially years after receiving the transfer and perform all the reprocessing which may be required. This could include reprocessing corporate actions against the security, recalculating wash sales and reissuing 1099-Bs. Our recommendation is to impose a limit of thirty days from transfer that a receiving broker must accept basis from another party, after which the receiving broker may permanently classify the security as noncovered.

We appreciate this opportunity to present Treasury with our opinions on some of the key issues facing brokers as they work to comply with the regulations. We hope that our recommendations will help produce the intended goals of providing reporting basis to the IRS and the taxpayer without placing undue challenges on the investment community.

Respectfully submitted,

Cameron Routh
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Scivantage, Inc.

