

## Are you ready for Cost Basis Reporting?



# Cost Basis

You've probably heard about the new rules regarding cost basis reporting. How will this affect you? What do you need to do to get ready?

### **First a quick summary:**

As part of the 2008 Emergency Economic Stabilization Act, custodians are required to report cost basis for securities sold on their 1099-Bs. There is a three year phase-in schedule depending upon the type of security.

**What is cost basis?** Cost basis or tax basis is the purchase price for an asset. For a security it is the purchase price, plus any commissions. Reinvested dividends are added to basis. Corporate actions and return of principal can also affect basis. When you sell the asset, the cost basis is deducted from the sale price and the proceeds are taxed.

**How is this different?** In the past, custodians reported cost basis, if available, on a supplemental form sent to you with Form 1099. This supplement was for your use, and not filed with the IRS. Custodians are now expected to verify and report cost basis on securities that were acquired and sold during the phase in period. For equities that is the 2011 tax year, mutual funds in 2012, fixed income and other types of securities in 2013. Eventually all cost basis will be reported.

Securities with required reporting are considered "covered" those without are "uncovered". Although the basis for holdings acquired before 2011 is not reportable by the custodian, you are still responsible for reporting basis on uncovered securities.

**What changes should you expect?** Upon the sale of a "covered" asset, you can choose a tax lot identification method. For instance, sell the first shares acquired (FIFO), the last shares acquired (LIFO), or those with the highest cost, which can minimize capital gains. There are several other methods available as well. If you make no choice the IRS mandates FIFO as the default.

If you prepare your own taxes, there are several changes. Your 1099 will look different. Although cost basis will now be reported on Form 1099-B, most custodians have elected to redesign the entire package which typically includes 1099-INT and 1099-DIV. Most have gone to a landscape format and are including other tax preference items such as fees and investment expenses. (over)

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The IRS has mandated has several new fields in the 1099-B:

Box 1b - Date security was acquired

Box 3 - Cost Basis

Box 5 - Wash Sale disallowed

Box 6 - If this box is checked, boxes 1b, 3, 5, 7, and 8 may be blank

Box 8 - Type of Gain or Loss, holding period (short or long)

Schedule D, Form 1040 will also receive a makeover. New this year is IRS Form 8949 - Sales and Other Dispositions of Capital Assets. This is a worksheet attachment to Schedule D to reconcile sale transactions you may be required to attach multiple forms separating sell transactions into short and long term gains, further divided into those with reported basis, those without and those with undetermined or un-reconciled basis.

***Be prepared to verify cost basis.*** Whether you prepare your taxes or have a professional prepare, make sure basis on the 1099-B match your records. If there is a discrepancy, use what the custodian reports, unless you can categorically prove your records are accurate. In this case, notify your custodian to correct. Missing basis is treated as zero so it is to your benefit to identify.

If you are a client of Schneider Downs Wealth Management Advisors, we are working to verify basis. We have historical records for every purchase made on your behalf. More importantly the accounting methods and tax lot identification method will have to synchronize. We are working directly with the custodians. As always we will collaborate with your tax preparer. For you, cost basis accounting will be seamless.

Contact your advisor or custodian with any questions.

Charles Schwab has put together an excellent eight-page booklet regarding these new rules. Follow the link below and choose "Guide to Tax Reporting Requirements."

<http://content.schwab.com/web/as/public/costbasis/index.html>

