

# Mutual Funds and Cost Basis Reporting

## Background

- Gain or loss on sales of securities generally equals the difference between the amount realized and the taxpayer's adjusted cost basis in those securities.
  - Mutual fund shareholders may elect to compute cost basis using the "average cost" method. Under this method, a shareholder divides their total investment in a fund by their total number of fund shares.
- Current law does not require cost basis information to be reported to investors or the IRS.
- Vanguard, like many other mutual fund sponsors, has voluntarily provided average cost basis information to shareholders since the early 1990's.
- Recent legislative proposals ("Proposals") would require mutual funds (and other financial intermediaries) to track and report cost basis information to investors and the IRS when securities are sold.
  - One such proposal also would require the reporting of information sufficient to determine the investor's holding period for securities.
- Vanguard supports these efforts. Further, Vanguard believes there are workable approaches for implementing a mandatory cost basis reporting regime.
  - If, however, a new cost basis reporting regime is enacted without sufficient clarity and implementation time, it could negatively impact millions of investors.
    - For example, Vanguard alone currently provides average cost basis information to approximately 5.6 million non-retirement accounts.

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## Key Areas of Concern

- Proposals should clarify the treatment of existing shareholder accounts currently receiving average cost basis information.
  - For example, proposals would require cost basis reporting for securities *acquired after* a stated effective date.
    - Proposals should address how average cost basis would be calculated where an existing shareholder in a fund makes additional share purchases in that fund.
    - Proposals should address how cost basis would be calculated for existing shareholders currently excluded from any cost basis reporting service because cost basis information is unavailable (for example, due to the transfer of shares from another financial institution).
    - Proposals should provide penalty relief for post-effective date cost basis information calculated using existing shareholder cost basis information.
- Proposals should clarify that mutual fund sponsors may continue to provide average cost basis information to investors.
- Proposals should avoid creating potential for investors to receive significant numbers of amended Forms 1099.
  - For example, Proposals should modify underlying substantive rules for calculating cost basis (such as for wash sales or returns of capital) and/or otherwise directly modify existing 1/31 delivery deadline for original delivery of Forms 1099 such that all required cost basis adjustments can be reflected in those forms.
- Proposals should provide sufficiently detailed rules to permit industry-wide development of new data transfer protocols and automated mechanisms for transferring large volumes of cost basis reporting information across distribution channels (such as fund sponsor to fund sponsor, brokerage firm to brokerage firm, brokerage firm to fund sponsor, fund sponsor to brokerage firm).
  - Without sufficient detail, implementation of systems to transfer cost basis reporting information will necessarily be delayed.