

Understanding the difference between “covered” and “noncovered” securities

Federal Cost Basis Reporting Regulations (“Regulations”) are taking effect over a three-year phase-in period that began in 2011. During this period, different types of securities have and will become “covered” and subject to new 1099-B cost basis reporting to the IRS. The phase-in of the various types of securities is as follows:

- Equities (including foreign securities and ADRs) – January 1, 2011
- Mutual Funds – January 1, 2012
- Fixed Income, Options and Structured Notes – January 1, 2013

Brokerage firms are required to report gross proceeds from sales and dispositions for cash for “covered” and “noncovered” securities. For “covered” securities, brokerage firms are also required to report the following information on Form 1099-B:

- Adjusted basis of the tax lots sold
- Acquisition date of the tax lots sold
- Classification of any gain or loss as short-term or long-term

For the 2011 tax year, the IRS has introduced the new Form 8949 that you must complete and attach to Schedule D when filing your tax return.

“Covered” Securities

A “covered” security refers to a security you have purchased on or after the effective date (above) or to a security that has been transferred to your account from an account in which the security was already “covered.” **As required by the Regulations, when you sell covered securities we will report to the IRS not only the gross proceeds from the sale, but also the cost basis, the date of acquisition and whether any gain or loss with respect to such securities is long-term or short-term.**

Example of a “Covered” Transaction

John Q Customer purchased ABC Inc. stock on 04/21/11 and subsequently sold the position on 05/25/11. Since ABC Inc. stock is an equity purchased on or after January 1, 2011, it is “covered” under the new cost basis legislation. As a result, the cost basis for ABC Inc. stock is IRS-reportable and is listed in the “Covered Transactions” section of the Tax Reporting

Are Not FDIC Insured	Are Not Bank Guaranteed	May Lose Value
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Statement, as indicated below. You will use information provided in this section of the Tax Reporting statement to complete Part I of Form 8949. Specifically for “covered” securities with basis reported to the IRS, you will check box (A) and list the transaction details in the appropriate columns of the Form 8949. (See the section “Completing Form 8949.”)

1099-B		2011 PROCEEDS FROM BROKER AND BARTER EXCHANGE TRANSACTIONS (OMB 1545-0715)						
Quantity	Transaction Description	Date Acquired Cover of Short	Date Liquidated Short Sale	Amount	Cost Basis	Adjustments	Gain or (Loss)	Remarks
SHORT TERM CAPITAL GAINS AND LOSSES								
COVERED TRANSACTIONS								
ABC Inc. 100.0000	Sale	CUSIP Number 04/21/11	037833100 05/25/11	35,500.22	35,008.95	0.00	491.27	
ABC Materials Inc. 10.2673	Sale	CUSIP Number 02/02/11	038222105 02/02/11	2,356.40	0.00	0.00	2,356.40	
10.7613	Sale	06/29/11	06/29/11	3,546.80	0.00	0.00	3,546.80	
	Security Subtotal			5,903.20	0.00	0.00	5,903.20	
Covered Short Term Capital Gains and Losses Subtotal				41,403.42	35,008.95	0.00	6,394.47	

“Noncovered” Securities

Securities purchased prior to the effective date (above) are considered “noncovered,” for which we will report only the gross proceeds to the IRS. Equities purchased prior to January 1, 2011, mutual funds purchased prior to January 1, 2012, and other securities—i.e., fixed income, options and structured notes—purchased prior to January 1, 2013 are and will be considered “noncovered.” **Any sale of a security that is not considered “covered” will still be included on the tax reporting statement with its adjusted cost basis but the cost basis amount will not be transmitted to the IRS.**

Example of a “Noncovered” Transaction

John Q Customer purchased XYZ Inc. stock on 12/19/10 and subsequently sold the position on 11/03/11. Since XYZ Inc. stock was acquired prior to the effective date of January 1, 2011, the cost basis will not be reportable to the IRS and is listed in the “Noncovered Transactions” section of the Tax Reporting Statement, as indicated below. You will use details provided in this section of the Tax Reporting statement to complete Part I of Form 8949. Specifically for “noncovered” securities in which basis is not reported to the IRS, you will check box (B) and list the transaction details in the appropriate columns of the Form 8949. (See the section “Completing Form 8949.”)

1099-B		2011 PROCEEDS FROM BROKER AND BARTER EXCHANGE TRANSACTIONS (OMB 1545-0715)						
Quantity	Transaction Description	Date Acquired Cover of Short	Date Liquidated Short Sale	Amount	Cost Basis	Adjustments	Gain or (Loss)	Remarks
NONCOVERED TRANSACTIONS								
XYZ Inc. 10.0000	Sale	CUSIP Number 12/19/10	456789123 11/03/11	408.20	500.22	0.00	(92.02)	
XYZ CITY SER D FULLY RFD REF OID PRF 04 MAR 93 06.000% 10000.0000	Redemption	CUSIP Number 12/24/10	64966BA78 04/01/11	5,075.00	5,300.00	0.00	(225.00)	

New Form 8949 and changes to Schedule D for the 2011 tax year

For tax year 2011, the IRS has created the new Form 8949 that must be completed and attached to Schedule D. In addition, Merrill Lynch has made changes to the Proceeds from Broker and Barter Exchange Transactions sections of the Tax Reporting statement. It now includes a consolidated gross proceeds and gain/loss section that segregates short-term gains and long-term gains as either “covered” or “noncovered” transactions. The information in this new section will provide you with the necessary information to complete Form 8949. You should complete Form 8949 before completing Schedule D.

The IRS has also made major revisions to Schedule D, which now acts as a summary of all capital gain and loss transactions. You are required to list the individual sale transactions on Form 8949. If the gain or loss is short-term, the gain or loss should be included on Part I of Form 8949. If the gain or loss is long-term, the gain or loss should be reported on Part II of Form 8949. You may need to attach multiple copies of Form 8949 to Schedule D to reflect different transaction types during the 2011 tax year. A separate Form 8949 is required for gains and losses if you:

- Have the basis reported on the Form 1099-B you received
- Do not have the basis reported on Form 1099-B
- Did not receive a Form 1099-B

Completing Form 8949

Part I of Form 8949 is broken out into columns (a) through (g). The illustration below shows where you can obtain the required information needed to complete this form. For “covered” securities, the information may all be obtained from Form 1099-B. You can indicate which category your gains and losses fall under by checking either box (A), (B) or (C) on Form 8949. You will need to include on each Form 8949 only those transactions described in the text for the box you check; i.e., either (A), (B) or (C). If you have more than one type of transaction and otherwise would have checked multiple boxes, a separate Form 8949 is required for each type. For example, if you check box (A) in Part I of the Form 8949, you will need to include only short-term gains and losses from “covered” transactions. If you check box (B) in Part I of the Form 8949, you will need to include only short-term gains and losses from “noncovered” transactions.

Form 8949 Department of the Treasury Internal Revenue Service (99)	Sales and Other Dispositions of Capital Assets ▶ See Instructions for Schedule D (Form 1040). ▶ For more information about Form 8949, see www.irs.gov/form8949 ▶ Attach to Schedule D to list your transactions for lines 1, 2, 3, 8, 9, and 10.	OMB No. 1545-0074 <div style="font-size: 2em; font-weight: bold; text-align: center;">2011</div> Attachment Sequence No. 12A
Name(s) shown on return Example A. Employee		Your social security number 123 45 6789

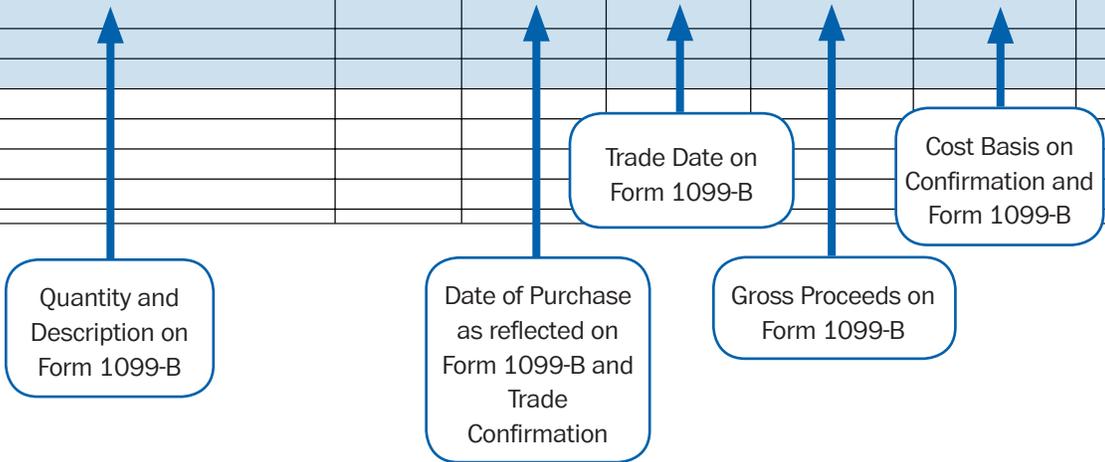
Part I Short-Term Capital Gains and Losses—Assets Held One Year or Less

Note: You must check **one** of the boxes below. Complete a *separate* Form 8949, page 1, for **each** box that is checked.

***Caution.** Do not complete column (b) or (g) until you have read the instructions for those columns (see the Instructions for Schedule D (Form 1040)). Columns (b) and (g) do not apply for most transactions and should generally be left blank.

(A) Short-term transactions reported on Form 1099-B with basis reported to the IRS
 (B) Short-term transactions reported on Form 1099-B but basis not reported to the IRS
 (C) Short-term transactions for which you cannot check box A or B

	(a) Description of property (Example: 100 sh. XYZ Co.)	(b) Code, if any, for column (g)*	(c) Date acquired (Mo., day, yr.)	(d) Date sold (Mo., day, yr.)	(e) Sales price (see instructions)	(f) Cost or other basis (see instructions)	(g) Adjustments to gain or loss, if any*
1	20.0000 shares ABC Co.		04-05-11	04-25-11	940.97	991.00	



Form 8949 is used to list all of your capital gain and loss transactions; the subtotals from this form are then carried over to Schedule D (Form 1040), where gain or loss is calculated in the aggregate.

Completing Your Schedule D

Schedule D has been revised for tax year 2011, and is now a summation of short- and long-term capital gains and losses from Form(s) 8949. You will need to complete Form 8949 first, and then carry over the subtotals from Form(s) 8949 column (e) Sales Price and column (f) Cost or Other Basis to Schedule D column (e) and (f). You may then calculate column (h) of Schedule D by combining columns (e), (f) and (g).

SCHEDULE D (Form 1040)		Capital Gains and Losses			OMB No. 1545-0074 2011 Attachment Sequence No. 12
Department of the Treasury Internal Revenue Service (99)		▶ Attach to Form 1040 or Form 1040NR. ▶ See Instructions for Schedule D (Form 1040). ▶ Use Form 8949 to list your transactions for lines 1, 2, 3, 8, 9, and 10.			
Name(s) shown on return Example A. Employee					Your social security number 123 45 6789
Part I Short-Term Capital Gains and Losses—Assets Held One Year or Less					
Complete Form 8949 before completing line 1, 2, or 3. This form may be easier to complete if you round off cents to whole dollars.		(e) Sales price from Form(s) 8949, line 2, column (e)	(f) Cost or other basis from Form(s) 8949, line 2, column (f)	(g) Adjustments to gain or loss from Form(s) 8949, line 2, column (g)	(h) Gain or (loss) Combine columns (e), (f), and (g)
1 Short-term totals from all Forms 8949 with box A checked in Part I		940.97	(991.00)		(50.03)
2 Short-term totals from all Forms 8949 with box B checked in Part I			()		
3 Short-term totals from all Forms 8949 with box C checked in Part I			()		(50.03)
4 Short-term gain from Form 6252 and short-term gain or (loss) from Forms 4684, 6781, and 8824				4	
5 Net short-term gain or (loss) from partnerships, S corporations, estates, and trusts from Schedule(s) K-1				5	
6 Short-term capital loss carryover. Enter the amount, if any, from line 8 of your Capital Loss Carryover Worksheet in the instructions				6	()
7 Net short-term capital gain or (loss). Combine lines 1 through 6 in column (h). If you have any long-term capital gains or losses, go to Part II below. Otherwise, go to Part III on the back				7	
Part II Long-Term Capital Gains and Losses—Assets Held More Than One Year					
Complete Form 8949 before completing line 8, 9, or 10. This form may be easier to complete if you round off cents to whole dollars.		(e) Sales price from Form(s) 8949, line 4, column (e)	(f) Cost or other basis from Form(s) 8949, line 4, column (f)	(g) Adjustments to gain or loss from Form(s) 8949, line 4, column (g)	(h) Gain or (loss) Combine columns (e), (f), and (g)
8 Long-term totals from all Forms 8949 with box A checked in Part II			()		
9 Long-term totals from all Forms 8949 with box B checked in Part II			()		
10 Long-term totals from all Forms 8949 with box C checked in Part II			()		
11 Gain from Form 4797, Part I; long-term gain from Forms 2439 and 6252; and long-term gain or (loss) from Forms 4684, 6781, and 8824				11	
12 Net long-term gain or (loss) from partnerships, S corporations, estates, and trusts from Schedule(s) K-1				12	
13 Capital gain distributions. See the instructions				13	
14 Long-term capital loss carryover. Enter the amount, if any, from line 13 of your Capital Loss Carryover Worksheet in the instructions				14	()
15 Net long-term capital gain or (loss). Combine lines 8 through 14 in column (h). Then go to Part III on the back				15	

For additional questions, please contact your Financial Advisor.

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