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Part III

Administrative, Procedural, and Miscellaneous

26 CFR 1.199A-2: Determination of W-2 Wages
(Also: § 199A)

Rev. Proc. 2019-11

SECTION 1. PURPOSE

This revenue procedure provides methods for calculating W-2 wages, as defined in section 199A(b)(4) and § 1.199A-2 of the Income Tax Regulations, (1) for purposes of section 199A(b)(2) of the Internal Revenue Code (Code) which, for certain taxpayers, provides a limitation based on W-2 wages to the amount of the deduction for qualified business income (QBI); and (2) for purposes of section 199A(b)(7), which, for certain specified agricultural and horticultural cooperative patrons, provides a reduction to the section 199A deduction based on W-2 wages.

SECTION 2. BACKGROUND

For taxpayers above a certain amount of taxable income, section 199A(b)(2)

limits the amount of a taxpayer's section 199A deduction for each qualified trade or business to the lesser of (1) 20 percent of the taxpayer's QBI with respect to the qualified trade or business, or (2) the greater of (A) 50 percent of the W-2 wages with respect to the qualified trade or business, or (B) the sum of 25 percent of the W-2 wages with respect to the qualified trade or business plus 2.5 percent of the unadjusted basis immediately after acquisition of all qualified property. Section 199A(b)(7) provides that in the case of any qualified trade or business of a patron of a specified agricultural or horticultural cooperative, the amount determined under section 199A(b)(2) with respect to such trade or business shall be reduced by the lesser of (A) 9 percent of so much of the qualified business income with respect to such trade or business as is properly allocable to qualified payments received from such cooperative, or (B) 50 percent of so much of the W-2 wages with respect to such trade or business as are so allocable.

Section 199A(b)(4)(A) defines the term "W-2 wages" to mean, with respect to any person for any taxable year of such person, the amounts described in section 6051(a)(3) and (8) paid by such person with respect to employment of employees by such person during the calendar year ending during such taxable year. Section 199A(b)(4)(B) provides that W-2 wages does not include any amount which is not properly allocable to qualified business income for purposes of section 199A(c)(1). Section 199A(b)(4)(C) provides that W-2 wages shall not include any amount that is not properly included in a return filed with the Social Security Administration (SSA) on or before the 60th day after the due date (including extensions) for such return.

Section 1.199A-2(b)(2)(iv)(A) of the regulations provides the Internal Revenue Service with authority to issue guidance providing the methods that may be used to calculate W-2 wages.

This revenue procedure provides three methods for calculating W-2 wages, as defined in section 199A(b)(4) and § 1.199A-2, for purposes of section 199A(b) and the regulations thereunder. The first method (the unmodified Box method) allows for a simplified calculation while the second and third methods (the modified Box 1 method and the tracking wages method) provide greater accuracy.

W-2 wages calculated under this revenue procedure are not necessarily the W-2 wages that are properly allocable to QBI and eligible for use in computing the section 199A limitations. As mentioned above, only W-2 wages that are properly allocable to QBI may be taken into account in computing the section 199A(b)(2) W-2 wage limitations. Thus, after computing W-2 wages under this revenue procedure, under § 1.199A-2(b)(3), the taxpayer must determine the extent to which the W-2 wages are properly allocable to QBI. Then, the properly allocable W-2 wages amount is used in determining the W-2 wages limitation under section 199A(b)(2) for that trade or business as well as any reduction for income received from cooperatives under section 199A(b)(7).

SECTION 3. RULES FOR APPLICATION

.01 *In general.* In calculating W-2 wages for a taxable year under the methods described in this revenue procedure, include only wages properly reported on Forms W-2 that meet the applicable rules of § 1.199A-2(b). Specifically, § 1.199A-2(b)(2)(i)

provides that, except as provided in § 1.199A-2(b)(2)(iv)(C)(2) (concerning short taxable years that do not include December 31) and § 1.199A-2(b)(2)(iv)(D) (concerning remuneration for services performed in the Commonwealth of Puerto Rico), the Forms W-2, “Wage and Tax Statement,” or any subsequent form or document used in determining the amount of W-2 wages are those that are issued for the calendar year ending during the person’s taxable year for wages paid to employees (or former employees) of the person for employment by the person. Section 1.199A-2(b)(2)(i) also provides that, for purposes of § 1.199A-2, employees of the person are limited to employees of the person as defined in section 3121(d)(1) and (2) (that is, officers of a corporation and employees of the person under the common law rules). Therefore, Forms W-2 provided to statutory employees described in section 3121(d)(3) (that is, Forms W-2 in which the “Statutory Employee” box in Box 13 is checked) should not be included in calculating W-2 wages under any of the methods described in this revenue procedure.

.02 No application in determining whether amounts are wages for employment tax purposes. The discussions of “wages” in this revenue procedure and in the regulations under section 199A are for purposes of section 199A only and have no application in determining whether amounts are wages under section 3121(a) for purposes of the Federal Insurance Contributions Act, under section 3306(b) for purposes of the Federal Unemployment Tax Act, or under section 3401(a) for purposes of the Collection of Income Tax at Source on Wages (federal income tax withholding), or any other wage-related determination. See § 1.199A-2 of the regulations.

SECTION 4. DEFINITION OF W-2 WAGES AND CORRELATION WITH BOXES ON FORM W-2

.01 *Definition of W-2 wages.* Section 199A(b)(4)(A) provides that W-2 wages means, with respect to any person for any taxable year of such person, the sum of the amounts described in section 6051(a)(3) and (8) paid by such person with respect to employment of employees by such person during the calendar year ending during such taxable year. Thus, W-2 wages include: (i) the total amount of wages as defined in section 3401(a); (ii) the total amount of elective deferrals (within the meaning of section 402(g)(3)); (iii) the compensation deferred under section 457; and (iv) the amount of designated Roth contributions (as defined in section 402A).

.02 *Correlation with Form W-2.* Under the 2018 Forms W-2, the elective deferrals under section 402(g)(3) and the amounts deferred under section 457 directly correlate to coded items reported in Box 12 on Form W-2. Box 12, Code D is for elective deferrals to a section 401(k) cash or deferred arrangement plan (including a SIMPLE 401(k) arrangement); Box 12, Code E is for elective deferrals under a section 403(b) salary reduction agreement; Box 12, Code F is for elective deferrals under a section 408(k)(6) salary reduction Simplified Employee Pension (SEP); Box 12, Code G is for elective deferrals and employer contributions (including nonelective deferrals) to any governmental or nongovernmental section 457(b) deferred compensation plan; Box 12, Code S is for employee salary reduction contributions under a section 408(p) SIMPLE (simple retirement account); Box 12, Code AA is for designated Roth contributions (as defined in section 402A) under a section 401(k) plan; and Box 12, Code BB is for

designated Roth contributions (as defined in section 402A) under a section 403(b) salary reduction agreement. However, designated Roth contributions are also reported in Box 1, Wages, tips, other compensation and are subject to income tax withholding.

SECTION 5. METHODS FOR CALCULATING W-2 WAGES

For any taxable year, a taxpayer must calculate W-2 wages for purposes of section 199A(b)(2) using one of the three methods described in sections 5.01, 5.02, and 5.03 of this revenue procedure. For a taxpayer with a short taxable year, see section 6 of this revenue procedure. In calculating W-2 wages for a taxable year under the methods below, the taxpayer includes only those Forms W-2 that are for the calendar year ending with or within the taxable year of the taxpayer and that meet the rules of application described in section 3 of this revenue procedure.

.01 Unmodified box method. Under the unmodified box method, W-2 wages are calculated by taking, without modification, the lesser of—

- (A) The total entries in Box 1 of all Forms W-2 filed with SSA by the taxpayer with respect to employees of the taxpayer for employment by the taxpayer; or
- (B) The total entries in Box 5 of all Forms W-2 filed with SSA by the taxpayer with respect to employees of the taxpayer for employment by the taxpayer.

.02 Modified Box 1 method. Under the Modified Box 1 method, the taxpayer makes modifications to the total entries in Box 1 of Forms W-2 filed with respect to employees of the taxpayer. W-2 wages under this method are calculated as follows—

- (A) Total the amounts in Box 1 of all Forms W-2 filed with SSA by the taxpayer with respect to employees of the taxpayer for employment by the

taxpayer;

(B) Subtract from the total in paragraph .02(A) of this section amounts included in Box 1 of Forms W-2 that are not wages for Federal income tax withholding purposes, including amounts that are treated as wages for purposes of income tax withholding under section 3402(o) (for example, supplemental unemployment compensation benefits within the meaning of Rev. Rul. 90-72); and

(C) Add to the amount obtained after paragraph .02(B) of this section the total of the amounts that are reported in Box 12 of Forms W-2 with respect to employees of the taxpayer for employment by the taxpayer and that are properly coded D, E, F, G, and S.

.03 Tracking wages method. Under the tracking wages method, the taxpayer actually tracks total wages subject to federal income tax withholding and makes appropriate modifications. W-2 wages under this method are calculated as follows—

(A) Total the amounts of wages subject to federal income tax withholding that are paid to employees of the taxpayer for employment by the taxpayer and that are reported on Forms W-2 filed with SSA by the taxpayer for the calendar year; plus

(B) The total of the amounts that are reported in Box 12 of Forms W-2 with respect to employees of the taxpayer for employment by the taxpayer and

that are properly coded D, E, F, G, and S.

SECTION 6. APPLICATION IN CASE OF SHORT TAXABLE YEAR

.01 *Special rule for taxpayers with a short taxable year.* In the case of a taxpayer with a short taxable year, subject to the rules of application described in section 3 of this revenue procedure, the W-2 wages of the taxpayer for the short taxable year shall include only those wages paid during the short taxable year to employees of the taxpayer, only those elective deferrals (within the meaning of section 402(g)(3)) made during the short taxable year by employees of the taxpayer, and only compensation actually deferred under section 457 during the short taxable year with respect to employees of the taxpayer. See § 1.199A-2(b)(2)(iv)(C) of the regulations.

.02 *Method required for a short taxable year and modifications required in application of method.* The W-2 wages of a taxpayer with a short taxable year shall be determined under the tracking wages method described in section 5.03 of this revenue procedure. In applying the tracking wages method in the case of a short taxable year, the taxpayer must apply the method as follows—

(A) For purposes of section 5.03(A), the total amount of wages subject to federal income tax withholding and reported on Form W-2 must include only those wages subject to federal income tax withholding that are actually or constructively paid to employees during the short taxable year and reported on Form W-2 for the calendar year ending with or within that short taxable year (or, for a short taxable year that does not contain a calendar year ending with or within such short taxable year, wages subject to federal

income tax withholding that are actually or constructively paid to employees during the short taxable year and reported on Form W-2 for the calendar year containing such short taxable year); and

(B) For purposes of section 5.03(B), only the portion of the total amounts reported in Box 12, Codes D, E, F, G, and S on Forms W-2, that are actually deferred or contributed during the short taxable year are included in W-2 wages.

SECTION 7. EFFECTIVE DATE

This revenue procedure applies to taxable years ending after December 31, 2017.

SECTION 8. DRAFTING INFORMATION

The principal authors of this revenue procedure are Andrew Holubeck and Mikhail Zhidkov of the Office of Associate Chief Counsel (Employee Benefits, Exempt Organizations, and Employment Taxes) and Margaret Burow and Frank J. Fisher of the Office of Associate Chief Counsel (Passthroughs & Special Industries). However, other personnel from the Treasury Department and the IRS participated in its development. For further information regarding this revenue procedure contact Andrew Holubeck or Mikhail Zhidkov at (202) 317-4774, or Margaret Burow or Frank J. Fisher at (202) 317-6850 (not toll free calls).