

INTERNAL REVENUE SERVICE

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January 23, 2001
CC:TE/GE:EOEG:ET1:STackney
COR-13786-00



Re: Form W-2 Reporting Requirement for Nonstatutory Stock Option Income

Dear [REDACTED]

This letter is in response to your [REDACTED] addressing Announcement 2000-97, 2000-48 I.R.B. 557. The announcement addressed an employer's obligation to report nonstatutory stock option income, i.e., the excess of the fair market value of the stock received upon exercise by an employee (or former employee) of a nonstatutory option over the amount paid for that stock. Employers are required to report that nonstatutory stock option income on Form W-2 in boxes 1, 3 (up to the social security wage base) and 5. As provided in that Announcement 2000-97, employers are also required to report nonstatutory stock option income in Box 12 of the Form W-2 using the new Code V. In response to employer concerns that the necessary changes to payroll and reporting systems would be difficult to institute in time for the 2001 Forms W-2, the Service made the Code V reporting requirement optional for 2001 Forms W-2, as stated in Announcement 2001-7, 2001-3 I.R.B. 1.

Authority for Form W-2 Reporting Requirements

Authority for the Services's requirement that nonstatutory stock option income be reported separately on a Form W-2 may be found in numerous places. Section 6051(a)(3) of the Internal Revenue Code (the Code), as well as section 31.6051-1(a)(1)(i)(c) of the Employment Tax Regulations, provide for the reporting of total amount of wages on the Form W-2. Because an employee's nonstatutory stock option income is included in the total amount of wages the employee receives for the taxable year, that income is reportable on the Form W-2.

Section 6011 of the Code also provides that where a taxpayer is required by regulation

to file a return or statement, the taxpayer must make the return or statement according to the forms and regulations prescribed by the Secretary, and must include any information required by the form or regulation. This section applies to Forms W-2, which are required by regulation to be filed. See Treas. Regs. § 31.6051-2 and § 301.6011-2(b). Therefore, taxpayers must include information as to nonstatutory stock option income that is required by the Form W-2.

Similarly, section 31.6051-1(a)(1)(i)(g) of the Employment Tax Regulations states that employers must provide “such information relating to coverage the employee has earned under the Federal Insurance Contributions Act as may be required by Form W-2 or its instructions.” An employee’s nonstatutory stock option income generally is included in the employee’s wages for purposes of the Federal Insurance Contributions Act (FICA). Therefore, information as to the employee’s nonstatutory stock option income relates to coverage the employee has earned under FICA and must be reported if required by the Form W-2.

Change in Stock Option Deduction Rules under section 83(h) of the Code

In your correspondence, you point out that the addition of reporting of nonstatutory stock option income to the Form W-2 will change the filing requirements that must be met to qualify for a deduction under Code section 83(h). Because section 1.83-6 of the Income Tax Regulations requires that the employer satisfy the Form W-2 reporting requirements with respect to the stock option income to qualify for the related deduction, satisfaction of the new Form W-2 reporting requirement will be a prerequisite to a proper deduction. However, neither section 1.83-6 nor the rule that it expresses have changed. Rather, because the deduction rule requires an employer to properly report information related to nonstatutory stock option income on the Form W-2 in order to qualify for the deduction, the deduction rule will necessarily reflect any change in the Form W-2 relating to nonstatutory stock option income.

Coordination with the Information Reporting Program Advisory Committee (IRPAC)

You have also expressed concern that the Information Reporting Program Advisory Committee (IRPAC) has not been consulted regarding the reporting requirement. Our records indicate that IRPAC was contacted at the time the Service initially considered the reporting requirement. Because the reporting requirement is now optional for 2001 Forms W-2, however, there will be an opportunity for IRPAC to revisit the Form W-2 Code V reporting requirement, should IRPAC choose to do so.

Usefulness of Information to Employees

You have stated that the reporting of the nonstatutory stock option income will not be useful to employees, because employers routinely provide such information to employees. It does not appear from your correspondence that this information is required to be given to the employees, but rather is provided as part of a typical payroll

system as a mention on the payroll stub. We look forward to discussing this with you further, including how the collection and reporting of this information in its current form will impact the burden of implementing the new reporting requirement.

Administrative Concerns

You have also expressed concern about the difficulty of instituting the payroll system changes necessary to administer the new reporting requirement. In response to your concerns, as well as those raised by other employer representatives, the Service has provided that the reporting of nonstatutory stock option income separately in Box 12, using Code V, is optional for 2001 Forms W-2. This will provide employers a full year to make any necessary changes.

Thank you for contacting the Service regarding your concerns. We welcome input from our customers so that we may more effectively and efficiently fulfill our mission. We hope that we have provided a useful response, and look forward to working with you in the future. If you have any questions about this letter, please contact Stephen Tackney at (202) 622-6040.

Sincerely,

Michael A. Swim
Branch Chief, Employment Tax 1
Office of the Associate Chief Counsel
(Tax Exempt and Government Entities)