

NO TAX ON OVERTIME

What employers need to know
about the new federal income tax
deduction for overtime premium



Key Policy Facts for Employers

- ◆ Employees can deduct up to \$12,500 (\$25,000 joint) of overtime premium income
- ◆ Deduction applies only to the 0.5x premium portion of FLSA overtime
- ◆ Employers continue normal withholding and payroll tax obligations
- ◆ New W-2 reporting requirements will be implemented to help employees claim this benefit
- ◆ Social Security and Medicare taxes still apply to all overtime income

What Changed

This new law allows employees to claim an above-the-line deduction for the “half” portion (the extra 0.5x over 40 hours/week) of FLSA defined overtime.



Who Qualifies?

Hourly, non-exempt workers covered under FLSA who work more than 40 hours per week.

Overtime Pay Deduction Limits



Single Filing

\$12,000



Joint Filing

\$25,000

Deduction Phase-Out Thresholds



Single Filing Income Over

\$150,000



Joint Filing Income Over

\$300,000

Non-Qualifying Overtime

Daily overtime, state or local overtime, and straight-time portion of overtime





EMPLOYER RESPONSIBILITIES

Continue Normal Operations

Keep withholding federal income tax on all overtime income. This deduction does not change your payroll tax obligations. Social Security and Medicare still applies and there are no changes to state or local taxes.

Report Qualified Earnings

There is no change to W-2 format for 2025, however, employers must use a “reasonable method” to report qualified overtime premiums separate from other withholdings.

RECOMMENDATIONS

- ◆ Verify the accuracy of payroll and timekeeping data
- ◆ Verify payroll and timekeeping systems are equipped to identify and report on overtime premiums by employee, by week
- ◆ Establish clear channels for sharing year-end summaries or periodic reports with employees

Determining Qualified Overtime Premium Amounts

Your normal overtime calculation and reporting may look different depending on your pay schedule(s), and any timekeeping system setup. The amount to be reported is not the total overtime pay, but specifically the premium portion (the “half” of time-and-a-half). For instance:

- Employee hourly rate = \$20.00
- Overtime hourly rate = \$30.00
- Overtime premium portion = \$10.00 per hour
- If employee worked 10 overtime hours
$$\$10.00 \times 10 \text{ hours} = \$100 \text{ premium to record in Box 14}$$

Special Considerations:

Semi-Monthly and Monthly Pay Schedules

Calculating overtime based on workweeks (as required by OBBBA) can be more complex for employers who pay semi-monthly or monthly.

Challenge: Semi-monthly and monthly pay periods often split workweeks or combine portions of multiple weeks, making it harder to directly match premium amounts to a single pay period.

Why it matters: The deduction is based on overtime worked over 40 hours per week, not per pay period.

Recommendation:

Use timekeeping reports to isolate the overtime premium by workweek, regardless of pay period.

Consider running weekly overtime premium summaries even if you pay less frequently.

For these pay frequencies, employers may need to reconcile overtime data outside of normal payroll reports to ensure accuracy.

For tax year 2025, the IRS is providing a Transition Relief period.



This means employers will not face penalties for failing to provide estimates or for providing incorrect estimates related to qualified overtime.

They also allow “any reasonable method” to report qualified OT premiums on W-2s or to provide to the employee.



How BBSI Can Help

BBSI provides guidance and support to help clients determine qualified OT premium amounts and process payroll batches to record qualified earnings on W-2s using specific pay codes.

We can also provide reports that provide estimated premiums, which can be shared with employees via a letter or statement.

RESOURCES

For more info, visit www.irs.gov.



FAQ - OBBBA's No Tax On OT

What is the Big Beautiful Bill?

A federal law allowing deductions for qualified tips and qualified overtime premiums for tax years 2025–2028.

When does the No Tax On OT deduction start?

Begins in the 2025 tax year and claimed when filing in early 2026.

How much can be deducted for overtime?

Up to \$12,500 per year (\$25,000 for joint filers), limited to the premium portion (extra 0.5×).

Who qualifies for No Tax On OT?

Non-exempt employees (hourly or salary) with FLSA overtime (> 40 hours/week).

What is the income cap for No Tax On OT?

The deduction phases out for those with a modified adjusted gross income (MAGI) above \$150,000 (\$300,000 for joint filers)

What should employers do for the 2025 tax year?

Use reasonable methods to share tip/OT premium information (e.g., summaries, Box 14).

Are there new forms for 2025?

No; 2025 is a transition year. 2026 forms are expected to update.



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