



The One Big Beautiful Bill Act

What it means for new overtime and tip tax deductions

On July 4, 2025, President Trump signed the “**One Big Beautiful Bill**” (OB BB) Act into law. The Act contains two key provisions in its nearly 900 pages that are likely to be very popular with employees—providing federal income tax deductions on both tips and qualified overtime compensation on tax years beginning on January 1, 2025, and ending on December 31, 2028.

The new federal deductions for overtime and tips give eligible employees new tax-saving opportunities, but they also require employers to track, report, and classify wages in new ways. With 2025 designated as a transition year by the IRS, now is the time to prepare your internal systems, payroll processes, and communication strategies for full compliance in 2026.

This whitepaper breaks down the law’s key provisions, deadlines, and reporting expectations to help you plan ahead with confidence.

What's already in effect- and what's next

2024



December 31, 2024

IRS rulemaking begins for tipped occupations

Treasury and the IRS will define eligible tipped occupations for tax years beginning after this date.

2025



January 1, 2025

Tax deduction eligibility begins

Qualified tip and overtime income earned from this date may be deductible for eligible workers. This applies to tax years beginning on or after January 1, 2025.



July 4, 2025

OBBB Act signed into law

The law became official on this date. Employers are expected to apply their provisions retroactively for 2025 and ensure accurate payroll tracking and reporting.



November 5, 2025

IRS designates 2025 as a transition year for new reporting requirements

The IRS issued [Notice 2025-62](#), granting penalty relief for employers that are unable to comply with new reporting rules for cash tips, employee occupation, and qualified overtime compensation. This relief applies only to tax year 2025. Employers should use this year to prepare internal systems for full compliance in 2026. No changes will be made to the 2025 Form W-2 or other reporting forms.

2028



December 31, 2028

Deductions set to expire

Unless extended, the tax benefits under the OBBB Act will expire after the 2028 tax year.

No federal tax on overtime and tips

In order to be eligible, **individuals must earn \$150,000 or less;** for **couples, it's \$300,000 or less.** These amounts may be adjusted according to inflation.



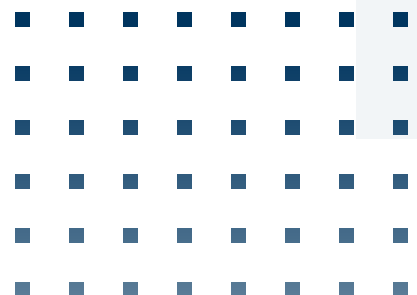
The deduction decreases for employees who earn more than \$150,000—the allowable deduction is reduced by \$100 for each \$1,000 (10%) by which an employee's gross income exceeds \$150,000 (or \$300,000 in the case of a joint return). **These deductions are temporary and are set to expire after the 2028 tax year.**

Tip deductions

Employees must work in occupations in which receiving tips is customary, like servers, bartenders, hotel staff, and hairstylists. The Internal Revenue Service (IRS) **published a proposed rule** that includes a list of covered occupations, with changes to be applied for taxable years beginning after December 31, 2024.

New tip reporting rules and expanded FICA credit for employers

- ▶ Employers must report both cash and non-cash tips, along with employees' occupation, on each employee's Form W-2.
- ▶ Businesses must separately report tip amounts and recipient occupations on Forms 1099 for tipped independent contractors.
- ▶ Social Security and Medicare taxes still apply to all reported tips. Employers should continue withholding and paying these taxes as usual.
- ▶ The IRS is required to revise tax forms and withholding procedures to reflect the new tip deduction and reporting rules, but no guidance has been issued yet.
- ▶ Employers in beauty and personal care industries, such as salons and spas, may now claim the Federal Insurance Contributions Act (FICA) tip credit if tipping is customary.
- ▶ The structure of the FICA tip credit remains the same for existing qualifying businesses (e.g., food service), but eligibility has broadened.
- ▶ Tipped workers may deduct up to \$25,000 of qualified tips earned.
- ▶ To be considered a "qualified tip," the amount must be paid voluntarily without any consequence in the event of nonpayment, must not be the subject of negotiation, and must be determined by the payor. Therefore, earnings from mandatory service charges assessed automatically to customers aren't deductible. Tips received under tip-sharing arrangements count as qualified tips.





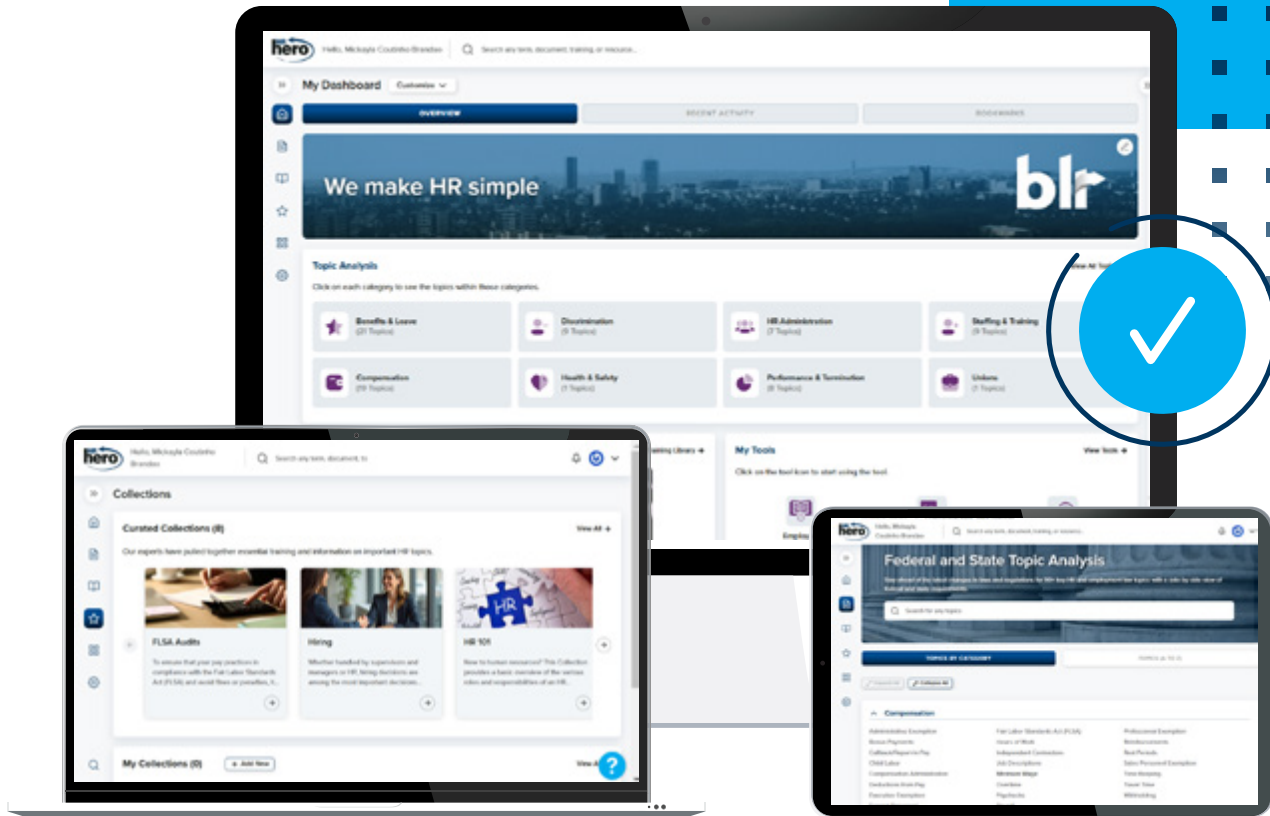
No tax on overtime

This applies to “**qualified overtime**,” which is overtime pay required under the Fair Labor Standards Act (FLSA), meaning hours worked beyond 40 in a workweek that must be paid at a premium rate. The deduction only applies to the premium portion of overtime pay, and the maximum deduction is \$12,500 per year for single individuals and \$25,000 per year for married individuals filing jointly.

The deduction doesn’t apply to overtime premiums paid solely under state laws or collective bargaining agreements. Like the tip deduction, it doesn’t affect Social Security or Medicare taxes, which must still be withheld and paid on the full amount of wages.

Employer reporting and compliance duties for overtime tax deduction

- ▶ This deduction is available in addition to the standard deduction, so employees don’t need to itemize to benefit.
- ▶ This deduction only reduces federal income tax. Social Security and Medicare taxes still apply to the full amount of overtime pay.
- ▶ Employers must report the total amount of qualified overtime pay on employees’ Forms W-2.
- ▶ Tax benefits are capped at \$12,500 for overtime.
- ▶ For independent contractors, businesses must report the amount of qualified overtime compensation on the relevant Forms 1099 even though, under the statute, “qualified overtime compensation” specifically refers to payments made to individuals under the FLSA.
- ▶ Because the law is retroactive to January 1, 2025, employers must account for qualified overtime already paid this year. Estimation methods should be clearly documented.
- ▶ The IRS is directed to revise withholding procedures and tax forms to accommodate the new deduction.
- ▶ For tax year 2025, employers are not required to separately report qualified overtime compensation due to transition-year relief from the IRS. However, the law directs the Secretary of the Treasury to establish a method for determining and reporting these amounts in future years.
- ▶ It’s recommended that employers review employee classifications to ensure exempt and nonexempt employees are properly designated. Employers should also keep detailed records of overtime hours and confirm that all hours are accurately tracked to prepare for full compliance in 2026.



BLR gives you expert clarity on complex employment law changes

As employers work through the new federal deductions for overtime and tips, having clear guidance and reliable tools becomes essential. BLR's HR Hero® offers thoughtful analyses of core topics such as FLSA, minimum wage, paid and unpaid leave, FMLA, discrimination, and unions, helping you make sense of changes like the OBBB Act with confidence.

Learn how we can help