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No Tax on Overtime Bill Guidance

The **no tax on overtime bill** was included in the recently enacted legislation that President Trump signed into law in July 2025. This new law creates a tax exemption for certain overtime pay effective beginning in tax year 2025. That means you'll first claim it when you file your tax return in early 2026. Under the current law, this new deduction is scheduled to remain in place through the end of 2028. It *doesn't make all overtime completely tax-free*, but it *reduces how much federal income tax you owe on qualified overtime pay*.

Key Details for Employees

- **It is a tax deduction, not an exemption at the time of payment.** Employers must continue to withhold federal income, Social Security, and Medicare taxes from all overtime wages as usual. The tax relief comes in the form of a deduction when you file your federal tax return (Form 1040). You can potentially adjust your W-4 form to lower your tax withholding throughout the year if you expect to claim this deduction.
- **Only the "premium" portion qualifies for the deduction.** The deduction applies only to the "half" portion of "time-and-a-half" pay for hours worked over 40 in a workweek, as defined by the Fair Labor Standards Act (FLSA).
    - **Example:** If your regular rate is $20/hour and your overtime rate is $30/hour, only the $10/hour premium is eligible for the deduction, not the full $30 overtime pay.
    - **If you earn straight-time bonuses, tips, or hazard pay, those don't qualify for the overtime deduction.**
- **Maximum Deduction Limits:** You can deduct up to **$12,500** annually (or **$25,000** if married filing jointly) on qualified overtime compensation.
- **Income Phase-Outs:** The deduction begins to phase out for taxpayers with a modified adjusted gross income (MAGI) over **$150,000** (or **$300,000** for joint filers).
- **Documentation:** For the 2025 tax year, employers are not required to separately report the qualified overtime amount on Form W-2. You should use information from your pay stubs or earning statements to calculate your deduction. For the 2026 tax year, employers will likely use a new code on Form W-2 (Code TT in Box 12) to report this amount.

Who Is Eligible?

To qualify for the deduction:

- You must be an **employee paid overtime under the federal Fair Labor Standards Act (FLSA)** (non-exempt workers).
- Independent contractors and most gig workers generally **do not qualify**.
- If overtime is paid because of a **collective bargaining agreement or state law** (e.g., California daily overtime), it might *not* count as "qualified overtime" for this deduction.
- Married taxpayers generally must file a **joint return** to claim the full married deduction.

How You Claim It

- You must **claim the deduction on your federal tax return**.
- Employers will now be required (with transitional relief) to report the amount of qualified overtime on Forms W-2 or other statements so you can calculate the deduction.

Summary

- **What the law does:**
  - Let's workers deduct *part* of their overtime pay from their federal taxable income (the extra premium portion under FLSA).
  - Reduces federal income tax owed, potentially lowering your overall tax bill.
- **What it *doesn't* do:**
  - It doesn't make *all* overtime totally tax-free.
  - Social Security/Medicare taxes still apply.
  - It's temporary (expires end of 2028 unless extended)

For additional information see the IRS website. https://www.irs.gov/newsroom/one-big-beautiful-bill-provisions