OBBBA Eliminates Taxes on Qualified Tips and Overtime Compensation

On July 4, 2025, President Donald Trump signed a tax and spending bill, commonly referred to as the One Big Beautiful Bill Act (OBBBA), into law. Among other provisions, the OBBBA would allow certain workers an above-the-line deduction for “qualified tips” and “qualified overtime compensation” for taxable years beginning after Dec. 31, 2024, and ending for taxable years beginning after Dec. 31, 2028.

Tip Deductions

Section 70201 of the OBBBA creates a new above-the-line tax deduction for qualified tips. Individuals must earn $150,000 or less ($300,000 if married filing jointly) in 2025 to be eligible for the tip deduction. The maximum deduction for tip income is capped at $25,000 per year, and the deduction only applies to cash tips, which include tips that are charged and tips received under a tip-sharing agreement. To be considered a **qualified tip**, the tip must be paid voluntarily without any consequence in the event of nonpayment, not be subject to negotiation, and be determined by the payor.

To qualify for the tip deduction, individuals must work in occupations where receiving tips is customary (e.g., servers, bartenders, hotel staff, hairstylists) on or before Dec. 31, 2024. The Treasury Department will publish a list of qualifying occupations within 90 days of the OBBBA’s enactment. Qualified tips must be reported on statements furnished to the individual as required under the Internal Revenue Code (e.g., Form W-2) or on Form 4137. The OBBBA does not change the requirement that employees and employers report all tips to the IRS. Individuals must include their Social Security number (and, if married and filing jointly, their spouse’s Social Security number) on their tax return to receive the deduction.

Overtime Deductions

Section 70202 of the OBBBA establishes a new above-the-line tax deduction for **qualified overtime compensation**. The OBBBA defines “qualified overtime compensation” as overtime compensation paid to an individual required under Section 7 of the Fair Labor Standards Act (FLSA) that is in excess of the regular rate at which the individual is paid. The maximum deduction for overtime income is capped at $12,500 per year ($25,000 per year if married filing jointly). The deduction decreases for those earning over $150,000 per year. Employers must include the total amount of qualified overtime compensation as a separate line item on employees’ Form W-2. Qualified tips cannot be claimed as qualified overtime compensation. Similar to qualified tips, individuals must include their Social Security number (and, if married and filing jointly, their spouse’s Social Security number) on their tax return to receive the deduction.

Next Steps for Employers

Employers may need to adjust their payroll systems to accurately track and report qualifying tips and overtime compensation on employees’ Forms W-2.

Provided by National Insurance Services