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“No Tax on Overtime” Provision (One Big Beautiful Bill Act)

Employee FAQ’s

Effective for Overtime Earned in 2025–2028

The federal government has introduced a new provision under the *One Big Beautiful Bill Act* that changes how certain overtime pay is treated for federal income tax purposes. Below are answers to commonly asked questions.

1. What is the “no tax on overtime” rule?

This rule does **not** make all overtime completely tax-free. Instead, it allows employees to **deduct the overtime premium portion** of their overtime pay from their federal taxable income.

- The **overtime premium** is the extra *half-time* paid when you work more than 40 hours in a week.
 - Your regular hourly wages (including for hours over 40) continue to be taxable.
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2. Who qualifies for this deduction?

You may qualify if you:

- Are a **non-exempt, hourly employee** eligible for overtime under federal law.
- Earn overtime that meets the definition of “qualified overtime compensation.”
- Have income below federal limits (generally under **\$150,000** single / **\$300,000** married filing jointly).

Employees who are salaried and exempt from overtime, or employees whose overtime is paid under special agreements or state rules, may not qualify.

3. When does this start?

The provision applies to overtime earned **starting January 1, 2025**, and remains in effect through **December 31, 2028**, unless extended by Congress.

Employees will claim the deduction when they file their federal tax return for that year.

4. Does this affect my paycheck now?

Not immediately.

This deduction is applied when you file your **annual federal tax return**, not during each paycheck. Your paychecks will continue to reflect normal federal tax withholding unless you choose to update your withholding elections.

5. What part of my overtime is deductible?

Only the **overtime premium portion**—the extra 0.5x paid above your regular rate—is eligible for the deduction.

Examples:

- If your regular rate is \$20/hour, your time-and-a-half overtime rate is \$30/hour.
 - **Regular pay for OT hours (\$20)** = taxable
 - **Premium portion (\$10)** = potentially deductible
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6. Will this affect my Social Security or Medicare taxes?

No.

Overtime wages are still subject to **FICA taxes** (Social Security and Medicare). The provision only affects **federal income tax**.

7. Will the deduction affect my state taxes?

Maybe, but not necessarily.

State and local tax laws vary. Some may follow the federal rule; others may not. You may want to consult a tax professional for state-specific guidance.

8. How will this be shown on my W-2?

The IRS is expected to provide a specific Box for W-2s starting in 2026. For calendar year 2025, W-2s from South Texas College will include Box 14, H.R. 1, to report the eligible amount to employees.

9. How much income is tax-free:

Income eligible for the deduction is capped at \$12,500 (Single) / \$25,000 (Married Filing Jointly).

10. What does the employer do to comply?

Our payroll system will:

- Track the overtime premium separately from regular wages.
 - Report qualified overtime properly on your year-end tax documents.
 - Follow guidance issued by the IRS for reporting during the transition period.
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11. Do I need to do anything now?

No action is needed at this time.

You may want to:

- Review your pay slips to understand your overtime breakdown.
 - Consult a tax professional if you have questions about how this affects your tax situation.
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12. Who can I contact with questions?

If you have any questions, please contact the South Texas College Payroll Office at 872-4641, 872-4629, or 872-4606, or email us at Payroll@southtexascollege.edu.

Thank you.