

Federal Overtime Tax Deduction Guidance FOR UNION EMPLOYERS AND MEMBERS



The One Big Beautiful Bill Act (OBBA) created a federal income tax deduction for certain overtime compensation for tax years **2025–2028**.

Not all overtime qualifies, and this change **does not affect paychecks, union contracts, or payroll withholding**. This memo explains how the deduction works in union environments, particularly where collective bargaining agreements (CBAs) require overtime under rules that differ from federal law.

WHAT OVERTIME QUALIFIES FOR THE DEDUCTION

Only overtime pay that meets **all** of the following criteria may qualify:

- ✓ Overtime is **required under federal law** (the Fair Labor Standards Act, or FLSA)
- ✓ The employee works **more than 40 hours in a workweek**
- ✓ Only the **premium portion** of pay (the additional half-time) is eligible

Federal law requires overtime only after **40 hours in a workweek**.

WHAT OVERTIME DOES NOT QUALIFY FOR THE DEDUCTION

Overtime pay does **not** qualify for the federal deduction when it is paid solely because of:

- ✗ Daily overtime rules (for example, overtime after 8 hours in a day)
- ✗ Collective bargaining agreement (CBA) provisions not tied to hours worked over 40 in a week
- ✗ Double time, weekend premiums, or shift differentials beyond federal overtime rules

CBAs may require overtime pay earlier or under broader circumstances, but the tax deduction applies only to overtime required by the FLSA.

EXAMPLE

Daily Overtime Under a CBA vs. Weekly Overtime Under Federal Law

An IBEW member earns **\$52 per hour** under a collective bargaining agreement. The CBA requires overtime pay at time-and-a-half for hours worked over **8 hours in a day**, even if the employee does not exceed 40 hours for the week.

SCENARIO 1 | Daily Overtime Only

- Employee works 9 hours on Monday
- Total hours worked for the week: **38**

Although overtime pay is required under the CBA, the employee did not exceed 40 hours for the week. Because the overtime was not required under federal law, **no portion of the overtime qualifies** for the federal overtime deduction.

SCENARIO 2 | Daily Overtime & Weekly Overtime

- Employee works 9 hours per day for 5 days
- Total hours worked for the week: **45**

In this case:

- Overtime paid solely because of daily thresholds earlier in the week **does not qualify**
- Overtime paid for the **five hours over 40 does qualify**
- Only the **premium portion** of pay for those five hours (the additional half-time) may be considered for the deduction

PAYROLL VS. PERSONAL TAX RETURNS

This change **does not affect payroll processing**:

- Overtime pay is still **taxed as usual when it is paid**, and payroll withholding **does not change**
- Social Security, Medicare, and applicable state taxes still apply

The deduction is claimed later on the employee's **personal federal income tax return**.

Beginning in **2026**, employers are expected to separately track qualified and non-qualified overtime on pay stubs and Forms W-2. For **2025**, that separate reporting is not required.

TAXPAYER RESPONSIBILITY FOR 2025

For tax year 2025, employees are responsible for:

- Calculating any eligible overtime deduction
- Claiming the deduction on their personal tax return

Additional 2025 Considerations

- Employers are **not required** to provide a total amount of qualified overtime pay for 2025.
- If a separate overtime summary is not provided, employees may use a **reasonable method** to calculate eligible overtime pay, such as reviewing pay stubs.
- Because only the premium portion of overtime pay is deductible, the deductible amount generally equals **one-third of total overtime pay** related to qualifying hours.

INCOME LIMITS

The overtime deduction is subject to limits and phaseouts:

Maximum Deduction

- **\$12,500** for single filers
- **\$25,000** for married filing jointly

The deduction phases out for higher-income taxpayers when modified adjusted gross income exceeds:

- **\$150,000** for single filers
- **\$300,000** for married filing jointly

NEXT STEPS

- Employers should continue to process payroll as usual
- Employees should continue reporting hours as normal and keep pay stubs
- Employees should consult with their own tax preparer to determine eligibility



This memorandum is based on the One Big Beautiful Bill Act, the Fair Labor Standards Act, and current IRS guidance. It is intended for general informational purposes only, and individual tax situations may vary.