

Insights

ONE BIG BEAUTIFUL BILL ACT: EMPLOYER REPORTING OBLIGATIONS FOR “QUALIFIED OVERTIME COMPENSATION”

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The One Big Beautiful Bill Act (“OBBA”) enacted in 2025 created a temporary federal income tax deduction for “qualified overtime compensation” paid to an employee. Although the deduction is claimed by employees on their tax returns (up to \$12,500), OBBA imposes new reporting obligations on employers that will require payroll and tax departments to modify systems to track and identify the amount of “qualified overtime compensation” paid to an employee during the year.

Employers’ full tracking and reporting obligations are fully effective beginning in 2026. Given the heightened attention that the deduction is likely to receive as we head to the mid-term elections and as employees complete their returns, employers should prepare their systems now to track and report the compensation eligible for the deduction and to answer questions from employees concerning their overtime (or eligibility for overtime).

WHAT IS QUALIFIED OVERTIME COMPENSATION?

OBBA defines qualified overtime compensation by reference to the overtime requirements of the Fair Labor Standards Act (“FLSA”). Accordingly, *only the 0.5X portion of the 1.5X overtime wages* required by the FLSA is included.

Additional compensation, such as the “straight-time” portion of overtime wages, premium pay required by state law overtime rules, overtime premiums required solely by collective bargaining agreements, shift differentials, and other voluntary premium or bonus payments are excluded.

Example:

Component	Amount
Regular rate of pay	\$20/hour
Overtime rate of pay (1.5x)	\$30/hour
Qualified Overtime Compensation	\$10/hour (premium portion of the overtime rate of pay)

WHAT ARE AN EMPLOYER'S REPORTING REQUIREMENTS?

Employers must separately identify and report the aggregate annual amount of qualified overtime compensation paid to each individual on an applicable Form W-2 (most common), Form 1099-NEC, or 1099-MISC filed with the IRS and furnished to the employee. Under the 2026 Form W-2 instructions, this information would be reported using Code TT in Box 12.

WHAT ARE AN EMPLOYER'S WITHHOLDING REQUIREMENTS?

OBBA does not change an employer's obligation to withhold income or payroll taxes from overtime compensation.

OBBA, however, directs the Department of the Treasury to update withholding procedures under Internal Revenue Code § 3402 to account for the new deduction. Employees may adjust their withholding through Form W-4 to reflect anticipated their qualified overtime compensation deduction. Employers are not responsible for verifying employees' eligibility for the deduction but must provide accurate wage information pursuant to the employee's Form W-4.

WHEN ARE THE QUALIFIED OVERTIME COMPENSATION REQUIREMENTS EFFECTIVE?

The qualified overtime compensation deduction is effective for 2025 through 2028. For 2025, the IRS issued transition guidance providing that employers would not be penalized for failing to report 2025 qualified overtime compensation.

WHAT ELSE SHOULD EMPLOYERS BE CONSIDERING?

The new deduction (a.k.a. "no tax on overtime") is likely to receive greater attention as employees complete their tax returns and the mid-term elections approach. In addition to preparing for reporting in 2026 and beyond, employers should anticipate questions from employees regarding the amount of their qualified overtime compensation or their eligibility for overtime generally. In connection with this, employers may consider reviewing certain employee classifications under the FLSA, as the heightened attention to overtime could bring additional focus from employees.

WHAT ARE THE KEY TAKEAWAYS FOR EMPLOYERS?

- OBBA allows *employees* to deduct qualified overtime compensation their federal taxable income.
- *Employers* must track and report the amount of qualified overtime compensation paid to each employee during the year.
- Employers will generally report the qualified overtime compensation on Form W-2.

- The 2025 tax year was treated as a transition year, with penalty relief for incomplete reporting. Full compliance will be expected beginning with 2026 wage reporting.
- Additional focus from employees on their overtime compensation may bring questions around the total amounts of overtime paid and reported or overtime eligibility generally.
- The IRS published helpful Q&A guidance for the deduction.

If you have questions about the OBBBA's qualified overtime compensation requirements, please contact us or your trusted BCLP counsel.

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