

Insights

New Federal Tax Reporting Requirements for Overtime Compensation

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The IRS has announced that new tax-reporting rules are forthcoming for overtime compensation under recent federal tax legislation commonly known as the **“One Big Beautiful Bill”** (the “Bill”).¹ Although the Bill does not change how employers calculate or pay overtime it introduces new overtime reporting requirements for employers. These changes facilitate an income tax deduction for certain employee overtime compensation for tax years 2025 through 2028.

1. What Has Changed

The Bill created a new above-the-line income tax deduction (available regardless of whether an employee itemizes deductions) for eligible employees based on **qualified overtime compensation**, as defined by the statute and to be further clarified by IRS guidance. In general, qualified overtime compensation includes only overtime pay that is required by the Fair Labor Standards Act (“FLSA”). To administer this deduction, the statute requires employers to report deductible overtime so employees know the amount to claim on their individual tax returns. The reporting requirements are governed by federal tax law and administered by the Internal Revenue Service (IRS), not by the Fair Labor Standards Act (FLSA).

2. What Has Not Changed

Importantly, these reporting rules do not change employers’ overtime pay obligations under the FLSA. Employers must continue to calculate and pay overtime compensation in accordance with existing wage-and-hour law.

“Qualified” v. Not “Qualified” Overtime

The distinction between legally required overtime and premium pay provided by policy or agreement remains relevant for wage-and-hour compliance, but it does not control taxability. For federal tax purposes, overtime compensation remains taxable wages unless a specific exclusion applies, and the new deduction is expected to be claimed by employees on their individual tax returns rather than excluded from payroll wages.

Qualified overtime refers to overtime compensation that is required by the FLSA—generally pay at one and one-half times an employee’s regular rate for hours worked beyond the applicable statutory threshold during a defined work period. Overtime compensation required solely by state or local law, and not by the FLSA, may not qualify for the federal deduction, even if it is treated as overtime for wage-and-hour purposes.

Non-qualified overtime, by contrast, arises from an employer’s policies, state or local law, collective bargaining agreement, or other contractual arrangements rather than FLSA mandate. Examples include premium pay for holidays, weekends, or scheduled days off, or for exceeding internal scheduling thresholds that fall below the

legal overtime limit.

While both forms of compensation are generally treated as taxable wages, only qualified overtime satisfies statutory overtime obligations, and the two categories may require different treatment for payroll tracking and tax reporting purposes once IRS reporting requirements are finalized.

3. Employer Reporting Expectations

The statute envisions that employers will separately identify and report qualified overtime compensation on employee wage statements, such as Form W-2, to support employee eligibility for the deduction. For the 2025 tax year, the IRS has allowed “transitional relief,” meaning that the IRS will not penalize employers who do not separately report qualified overtime compensation while reporting mechanisms are being finalized.

In later tax years, employers should expect more formal reporting requirements once the IRS updates forms, instructions, and related guidance. Employers should begin evaluating now whether their payroll systems can distinguish among base wages, overtime premium amounts, and other forms of premium pay in anticipation of mandatory separate reporting.

Takeaways and Next Steps

New tax-reporting considerations for overtime compensation are emerging. Employers should:

- monitor IRS guidance,
- coordinate with payroll providers, and
- prepare systems to track overtime premium amounts separately in anticipation of future reporting requirements.

For guidance regarding these new developments in overtime reporting, contact **Marsha Jean-Baptiste, Kendall A. Schnurpel, Nancy Townsend** or any other member of Krieg Devault’s **Labor and Employment** and **Tax** Team.

¹ Public Law 119-21, H.R. 1, 139 Stat. 72 (signed July 4, 2025).

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