

Abstract: Taxpayers who received tips or overtime pay in 2025 may be eligible for a new deduction when they file their income tax return. Last year's One Big Beautiful Bill Act (OBBBA) created both deductions, which can be claimed whether or not the taxpayer itemizes deductions. But various rules and limits apply. This article provides an overview of the deductions, rules and limits.

Can you claim a tax deduction for tips or overtime income?

If you received tips or overtime pay in 2025, you may be eligible for a new deduction when you file your income tax return. Last year's One Big Beautiful Bill Act (OBBBA) created both deductions, which can be claimed whether or not you itemize deductions. But various rules and limits apply. Also be aware that such income may still be fully taxable for state and local income tax purposes. And federal *payroll* taxes still apply to tips and overtime income you deduct for federal *income* tax purposes.

Deducting tips

Eligible taxpayers can deduct up to \$25,000 of annual qualified tips income. The deduction begins to phase out when modified adjusted gross income (MAGI) exceeds \$150,000 (\$300,000 for married couples filing jointly). It's completely phased out when MAGI reaches \$400,000 (\$550,000 for joint filers).

Qualified tips can be paid by customers in cash or with credit cards or given to workers through tip-sharing arrangements. The tips deduction is available if you receive qualified tips in an occupation that's designated by the IRS as one where tips are customary. Some examples of eligible occupation categories are beverage and food service, hospitality and guest services, personal appearance and wellness, and transportation and delivery.

The tips deduction is allowed for both employees and self-employed individuals. However, those who work in certain trades or businesses — such as health, law, accounting, financial services, investment management — are ineligible.

Deducting overtime

Eligible taxpayers can deduct up to \$12,500 of qualified overtime income (\$25,000 for joint filers). The deduction begins to phase out when MAGI exceeds \$150,000 (\$300,000 for joint filers). It's completely phased out when MAGI reaches \$275,000 (\$550,000 for joint filers).

Qualified overtime income is overtime compensation mandated under Section 7 of the Fair Labor Standards Act. It requires time-and-a-half overtime pay except for certain exempt workers. Only the extra "half" constitutes qualified overtime income and thus is deductible.

Qualified overtime income doesn't include overtime premiums that aren't required by Sec. 7, such as those required under state laws or pursuant to union-negotiated collective bargaining agreements.

Reporting requirements

Under the OBBBA, qualified tips income must be reported on Form W-2, Form 1099-NEC or

another specified information return or statement furnished to both the worker and the IRS. And qualified overtime income must be reported to workers on Form W-2 or another specified information return or statement furnished to both the worker and the IRS.

However, the IRS announced that for the 2025 tax year, there will be no OBBBA-related changes to federal information returns such as Form W-2, Forms 1099 and Form 941. The IRS is providing transition relief for the 2025 tax year and will update forms for the 2026 tax year.

We can help you determine your eligibility for one or both of these deductions. We'd also be pleased to answer any other questions you may have about the impact of the OBBBA on your 2025 return and 2026 tax planning.

© 2025