



From Campaign Slogan to Current Law, Tips and Overtime Now Tax Free

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The President made the big promise on the campaign trail to remove taxes from tips and overtime. With the signing of the “One Big Beautiful Bill” in July, that promise became law. Tips and overtime now exist free from federal income taxes to a significant extent.

From tax year 2025 through 2028, tipped or hourly workers can deduct the amount they earn in tips or overtime, respectively, from their gross income.

However, with all the various versions and debating ideas of how to go about removing taxes from tips, what did the end result truly look like?

FOR TIPPED EMPLOYEES

Tipped workers will be able to deduct qualified tips from their gross income. This deduction is capped at \$25,000 for an individual filer or double for joint filers. Additionally, if the worker makes more than \$150,000 in adjusted gross income (including income beyond work income), the deduction will not apply to the worker.

FOR OVERTIME EMPLOYEES

Similar to tipped workers, employees who work overtime will be able to deduct overtime pay from their gross income. This only factors in the extra half-time pay from overtime, not the full-time and a half. The overtime deduction is capped at \$12,500 for an individual filer & unavailable for workers earning more than \$150,000.

FOR ALL EMPLOYEES CLAIMING THIS DEDUCTION OVERTIME EMPLOYEES

No tax on tips or overtime still provides coverage for FICA taxes (used later in life for Social Security and Medicare) as well as Unemployment compensation. Both of these tax deductions should not impact how your income is considered for loans.

No Tax on Tips Is in Full Effect

Detail	Current Law	NEW LAW – backdating to January 2025
Duration		Four Years (2025 – 2028)
Annual earnings	\$50,000 (\$40K tips, \$10K cash wages)	\$50,000 (\$40K in tips, \$10K in wages)
Income Subject to Federal Income Tax	\$50,000	\$25,000 (\$15K in taxable tips + \$10K in wages) <i>First \$25K is tax-free</i>
Effective Rate	11.3%	10%
Federal Income Tax Liability	\$4,016	\$1,040
Server Tax Savings		\$2,976 (\$4,016 - \$1,040)



I AM AN OPERATOR, AND I HAVE WORKERS THAT WORK OVERTIME OR EARN TIPS. WHAT DO I NEED TO DO?

Fortunately, very little (technically). The tax benefit for the worker comes from an above-the-line deduction, meaning that the adjustment to their taxes happens at the end of the year while filing for taxes starting in 2025. Tipped and overtime workers will be able to deduct their respective wage adjustments just the same as a taxpayer deducts student loan interest from their income. So long as the tipped workers are reporting their tips, and overtime is being recorded correctly, operators should not need to do any extra work to ensure their workers benefit from this tax deduction. You will need to file information returns with the IRS showing cash tips and the workers' occupation.

I AM A WORKER WHO MAKES TIPS/OVERTIME, HOW DO I CLAIM MY DEDUCTION?

Deductions for tips and overtime should be as simple as reporting those amounts to the IRS once it comes time to file taxes. Regardless of whether or not you itemize your deduction or take the standard deduction, you will be allowed to deduct \$25,000 of tips and/or \$12,500 in overtime pay. These will be deducted from your gross pay, basically changing what the IRS really considers your income. This deduction works the same as deductions for student loan interest or other income deductions.

Questions?

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