

No Tax on Overtime

FAQs for Government Employees



Disclaimer

On November 5, 2025, the IRS granted relief to employers from providing employees with separate statements accounting for qualified overtime compensation for the purposes of the no tax on overtime deduction.

In further guidance published on November 21, 2025, the IRS outlines several ways that employees can calculate their qualified overtime eligible to be deducted this year.

The following FAQs are not advice, but an explanation of what the IRS guidance says and how federal law treats overtime compensation. Specific questions about your overtime compensation should be directed to your employer.

What is No Tax on Overtime?

H.R. 1 established “no tax on overtime” as an above-the-line deduction, meaning that when you file your personal taxes for the year, you can subtract up to \$12,500 of qualified overtime from your gross income (up to \$25,000 for joint filers). This deduction is limited to employees making less than \$150,000 in modified adjusted gross income per year (\$300,000 in the case of joint filers) and is retroactive to tax year 2025.

I am not seeing more money in my paycheck for overtime. Why is that?

“No tax on overtime” is not a withholding, meaning that taxes will not be withheld from overtime pay throughout the year.

Who qualifies for the no tax on overtime?

All **FLSA-covered** employees who are **non-exempt from overtime** may deduct qualified overtime compensation from their federally taxable income.

Certain employees that **are exempt from FLSA** overtime requirements may still receive overtime compensation based on state law, collective bargaining, or employer policy. This overtime is not eligible to be deducted.

Employees of governmental entities are covered by the FLSA and must receive minimum wage and overtime compensation unless otherwise exempt. ***If you have questions about your status under FLSA, please contact your payroll administrator.***

What is qualified overtime?

H.R. 1 defines qualified overtime as the overtime compensation that is in excess of your regular rate. In other words, this means that only the “half” portion of the base time and a half pay rate required by the FLSA for non-exempt employees. This half portion of time-and-a-half pay is also known as the “overtime premium.” This means that only some of the overtime you earned will be eligible to be deducted.

For example: Employee A has a regular rate of \$30/hour. This means they earn \$45 in time-and-a-half pay for any hours worked beyond the FLSA maximum in a week. The overtime premium is therefore \$15, and the employee may deduct \$15 as qualified overtime compensation.

If you are an exempt employee earning overtime pay or compensatory time off, it is not FLSA-covered and therefore is not eligible to be deducted.

Is qualified overtime different than the overtime compensation I see on my paystubs?

It could be if your employer does not differentiate between FLSA and non FLSA overtime and does not list the overtime premium (the amount beyond your regular rate) separately. The IRS provided guidance to employees on how to calculate their qualified overtime compensation based on what information is available to them. ***See pages 22–25 of the IRS guidance, GFOA’s FAQs or talk to your payroll administrator.***

Is my regular rate the same as my hourly rate?

No. Under the FLSA, overtime compensation is based on an employee’s regular rate for the work week. The regular rate is the week’s total compensation (with certain exclusions) divided by the total hours worked that week.

Total compensation in the workweek (except for statutory exclusions) ÷ Total hours worked in the workweek = Regular Rate for the workweek

Most information needed to calculate your regular rate should be available on your pay stub. If it’s not, talk to your payroll administrator for the necessary information.

How is overtime earned under the FLSA?

Under FLSA, overtime is earned at least at a time-and-a-half rate for all hours worked over the employee's maximum allowable hours during a week or an FLSA-covered work period. The maximum allowable hours under the FLSA are traditionally 40 hours per week, however there are variations in maximum allowable hours for different public sector roles. For example, public safety employees and hospital workers earn overtime based on different work periods. See GFOA FAQ #2 for additional information. ***If you have questions about your maximum allowable hours, speak with your payroll administrator.***

I've heard that if I take paid time off (holiday, sick leave, compensatory time, etc.) my overtime that week isn't eligible for deduction. Is this true?

It depends. The FLSA does not consider paid time off as "hours worked" even if you are being compensated for that time. If you take paid time off during the week, overtime compensation would only be eligible if your hours actually worked more than 40 hours that week (or another FLSA-covered allowable maximum hour threshold). ***See GFOA FAQs for more information or talk with your payroll administrator.***

I am non-exempt but earn overtime at a rate beyond time-and-a-half pay. How do I figure out what is deductible?

This means that only some of the overtime you earned will be eligible to be deducted if you are a non-exempt employee. Certain non-exempt employees may also receive overtime that is more generous than the FLSA definition (such as overtime based on state law, collective bargaining, or employer policy). Only the half portion of FLSA overtime time-and-a-half pay is eligible to be deducted. Reasonable Methods C and D found on pages 23 of the IRS guidance instructs non-exempt employees how to calculate their overtime premium eligible to be deducted. ***See GFOA FAQ #9 for additional information or talk to your payroll administrator for assistance.***

If you do receive different types of overtime (i.e. FLSA versus collective bargaining agreement overtime) you should begin to see that broken out in your W-2 beginning in tax year 2026.

I earn overtime after working 37.5 hours in a week and/or receive daily overtime. Is that eligible?

No. For the purposes of the deduction, only the premium portion of overtime earned for working more than 40 hours or another FLSA-covered allowable maximum per week is eligible to be deducted. If you are an FLSA non-exempt employee, you may need to separately calculate your qualified overtime based on a 40 hour work week.

For Example: Employee A is a FLSA-covered and non-exempt and works for a county in a non-public safety position and earns overtime at the time-and-a-half rate of \$15 for hours worked over 37.5 hours each week. They work 45 hours in a week.

The premium overtime for hours 38, 39 and 40 is not qualified overtime compensation eligible to be deducted. The premium overtime portion of hours 41–45 worked is qualified overtime compensation. Employee A may deduct \$25 of their total overtime compensation.

Do I have to calculate qualified overtime on a week-by-week basis?

If you have a more generous overtime compensation than what FLSA requires (i.e. you earn overtime for hours worked under 40 per week and/or receive overtime compensation at a rate higher than time-and-a-half) **and** your employer does not separate out the overtime premium from total overtime compensation, then you may have to calculate qualified overtime compensation on a weekly basis using your paystubs or other pay statements. ***Talk to your payroll administrator if you need assistance determining your regular rate.***

You should begin to see your FLSA overtime premium broken out in your W-2 beginning in tax year 2026. Employees claiming the deduction should complete and submit a new Schedule 1-A form.

Is the compensatory time I have accrued this year considered qualified overtime?

Governmental employees who earn compensatory time in lieu of cash payments for overtime hours worked are allowed to incorporate it into their qualified overtime once the compensatory time has been paid out as wages. Further, wages paid for only the premium portion of compensatory time (in this case the additional half hour earned) is eligible to be included in the deduction.

Your compensatory time is not counted towards overtime when it is used and you are paid for time off, and compensatory time off is not considered “hours worked” for the purposes of earning overtime.



GFOA FLSA FAQs



IRS GUIDANCE



SCHEDULE 1-A
DRAFT FORM

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