TaxBrief

Keeping you informed

One Big Beautiful Bill: What It Means for You

The legislation known as the One Big Beautiful Bill, enacted on July 4, 2025, introduces several significant updates to the federal tax system, affecting individuals and families in a range of situations. This landmark legislation brings significant changes to the tax laws. Below, we will break down these changes in simple terms and how they might affect you as a taxpayer.

No tax for qualified tips

For millions of Americans working in hospitality and other service industries, tips are a vital part of their income. Until now, tips were considered taxable income for federal tax purposes, and workers had to report them to the IRS and pay income tax.

What's changed?

The new law allows up to $25,000 per year in tip income to be deducted from your taxable income for tax years 2025 through 2028. The deduction is not an exclusion from gross income, but a deduction when you file your tax return. **This means you won't see any withholding changes to your paycheck.**

The deduction is **NOT** a full exclusion; tips still count toward Social Security and Medicare taxes. The deduction only applies to cash or card-based tips that you receive in qualifying jobs, but not to any service charges, regular wages or non-cash rewards.

Example: At a restaurant, Sarah's bill includes a 15% service charge automatically added because she is part of a large group. She pays the total with her credit card. Even though it looks like a tip on the receipt, it's a mandatory fee and not eligible for the tip income deduction. Her server is Jamal; therefore, Jamal cannot count the 15% service fee as a tip.

- The maximum deduction is $25,000 per year.
- Phaseout: The deduction is reduced by $100 for each $1,000 (or fraction thereof) by which the taxpayer's modified adjusted gross income MAGI exceeds $150,000 ($300,000 for joint filers).

The deduction is only allowed for tips that are:

- Included on a tax information reporting form such as Form W-2, Form 1099 or similar. These are usually tips the employer records or that the employee reports to their employer, or
- Reported by the taxpayer on Form 4137 (Social Security and Medicare tax on unreported tip income)

Qualifying occupations: The IRS will publish a list of occupations that customarily and regularly receive tips before the end of 2025. Examples likely include waiters, bartenders, hotel bellhops, casino dealers, hairdressers and other similar service roles.

Other requirements: The deduction is only available if the taxpayer includes their Social Security number on their tax return, and for married individuals, only if they file jointly.

Example: Maria is a waitress at the People's Pig, a BBQ joint, which is a qualifying occupation. In 2025, she receives $30,000 in cash and card tips, all of which she reports to her employer and includes on her Form W-2. Her total income for the year is $70,000 ($30,000 for tips and the rest is regular wages). She is a single taxpayer. Because her MAGI is less than $150,000, Maria can deduct $25,000 of the $30,000 of tips on her tax return, making her adjusted gross income (before other deductions) $45,0000 instead of $70,000.

No tax on overtime

Effective for 2025 through 2028, individuals who receive qualified overtime compensation may deduct the pay that exceeds their regular rate of pay, the "half" portion of "time-and-a-half" compensation, that is required by the *Fair Labor Standards Act* (FLSA). The maximum annual deduction is $12,500 (or $25,000 if filing jointly) of qualified overtime pay. To take the deduction, you will need a Social Security number.

As the same with the tips, this is **NOT** a total tax exemption; it's a deduction for federal income tax only. Payroll taxes (Social Security and Medicare) still apply. Just as with the tips explained above, the deduction begins to phase out at $150,000 (MAGI) for individuals, and $300,000 for married taxpayers who file jointly.

To qualify for this deduction an employer must report qualified overtime compensation separately on W-2s (the IRS will create a new box). Non-employees (e.g. contractors, but not self-employed individuals) must report the amount on Form 1099.

For tax year 2025 only, transitional rules allow employers to estimate this amount. We're waiting for additional guidance from the IRS as to the exact definition of overtime.

Example: Jane Doe is a single employee who earns $60,000 in regular wages and $10,000 in qualified overtime pay in 2025. Her total income is $70,000. Under this provision:

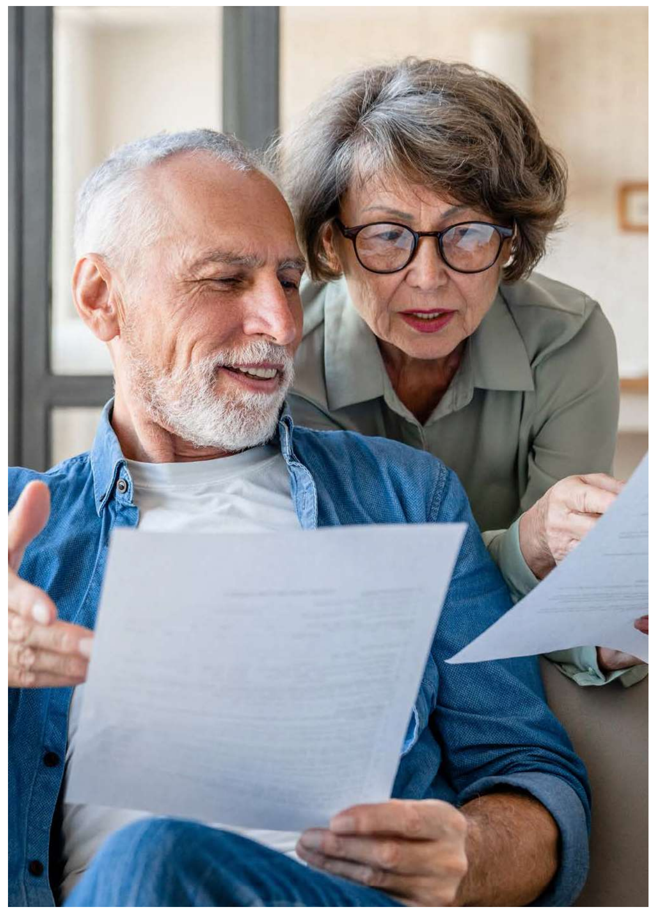
- Jane can deduct the full $10,000 of qualified overtime pay from her taxable income at the end of the year.
- Her taxable income for federal purposes would include $60,000 of regular wages plus $10,000 of overtime, totaling $70,000. However, since the $10,000 is qualified overtime, she can claim a $10,000 deduction on her tax return. [$60,000 (regular wages) + $10,000 (overtime) - $10,000 (deduction for overtime)].

New senior deduction

A new deduction is created only for seniors (65+), starting in tax year 2025 through 2028. Most personal exemptions are gone permanently, but seniors get a new temporary tax break.

Taxpayers age 65 or older (and their spouses if they are 65+ and filing jointly) can claim a $6,000 deduction per qualified individual. However, there are a few requirements.

- **Income limitation:** The $6,000 deduction is reduced by 6% of the amount the taxpayer's (MAGI) exceeds $75,000 ($150,000 for joint filers). MAGI include adjusted gross income plus certain excluded foreign income.
- **Social Security number requirement:** To claim the deduction, the taxpayer must include the qualified individual's Social Security number on the tax return.
    - Failing to include the correct Social Security number will be treated as a mathematical or clerical error by the IRS.



- **Joint return requirement:** Married couples must file jointly to claim the deduction for both spouses.

Example: John (68) and Mary (66) file jointly for 2025. Their MAGI is $140,000, and since they filed married filing jointly, they qualified for two senior deductions: $6,000 for John + $6,000 for Mary. Their income is under the $150,000 phaseout limit, so they get the full $12,000 deduction.

Tip: Several news outlets say Social Security benefits are NOT taxable, but this is not true. The One Big Beautiful Bill does not contain a provision that mentions this; however, the senior deduction could possibly lower your taxable income, which can REDUCE your total tax owed, even if your Social Security remains partially taxable.

Example: Penny (68) receives $20,000 in Social Security benefits and withdrew $30,000 from her IRA. She has no other income. Therefore, her AGI is $40.000. [$30,000 + ½ of Social Security ($10,000) = $40,000].

Since Penny's provisional income is $40,000, she is now in the highest tax bracket range and her Social Security benefit income becomes taxable at 85%. [85% of $20,000 = $17,000].

Now her AGI includes $30,000 (IRA) and $17,000 (taxable portion of Social Security), which equals $47,000.

Penny's new AGI becomes $47,000 [$30,000 IRA + $17,000 Social Security].

The current standard deduction for Penny in 2025 is $17,750 (including extra amount for age 65+ of $2,000). Additionally, with the new senior deduction of $6,000, Penny will now have a total deduction of $23,750 [$15,750 + $2,000 + $6,000]. Penny's new taxable income, instead of being $47,000, will be $23,250. As we can see, there are big savings for Penny in 2025.

Without the extra $6,000, Penny's taxable income would be $29,250 [$47,000 - $17,750].

Increased child tax credit

Families with children will see an increase in the child tax credit.

What changed?

- **Increased credit amount:** The child tax credit (CTC) is increased from $2,000 to $2,200 per qualifying child, effective for tax year 2025.

- **Permanent extensions:** The expanded CTC, which was previously set to expire after 2025, is now made permanent with no expiration date specified.

- **Social Security number requirement:** To claim the credit, the taxpayer (at least one parent on a joint return) and each qualifying child must have a valid SSN, which must be issued to a U.S. citizen or as specified under the *Social Security Act* and obtained before the tax return due date.

No tax on car loan interest

For tax years 2025 through 2028, interest on new car loans for personal vehicles can be deducted from your taxable income, even if you don't itemize your deductions.

- **Loan qualifications:** The loan must be a new loan (incurred after Dec. 31, 2024) and secured by a first lien on the qualifying vehicle, meaning it is a **brand-new vehicle that no one else has used or owned.** Refinanced loans can qualify, but only up to the amount of the original qualifying loan. Loans from related parties DO NOT qualify.
- **Dollar limit:** The maximum amount of interest that can be deducted per taxpayer per year is $10,000.

- **Income limitation:** The deduction is reduced by $200 for each $1,000 (or part thereof) by which the taxpayer's modified adjusted gross income (MAGI) exceeds:
  - $100,000 for single filers
  - $200,000 for joint filers
- **Income reporting requirement:** To claim the deduction, the taxpayer must report the vehicle identification number on their tax return.
  - **Vehicle qualifications:**
    - Brand new cars, minivans, trucks and motorcycles
    - The original use begins with the taxpayer (i.e., the buyer is the first user)
    - Vehicle must be assembled in the United States
    - Fleet vehicles, commercial vehicles, leased vehicles or salvage title vehicles do not qualify

Example: Katie buys a brand-new SUV in May 2025 for her own personal use. The SUV was assembled in the U.S., and Katie is the first owner. She takes out a $40,000 loan at 6% interest, secured by a first lien on the vehicle. In 2025, she pays $2,300 in interest on the loan. Her MAGI is $95,000.

Katie can deduct the full $2,300 of interest paid on her 2025 tax return, since the interest she paid is $2,300, which is less than $10,000, the annual cap.

Trump Account

A Trump Account is a type of savings account for kids under 18. It works similarly to a traditional individual retirement account (IRA), but with specific rules aimed at helping children build savings for the future. The account can be created by the government (the Secretary of the Treasury) or by a parent/guardian for a child under 18.

Who is eligible?

- Any child under age 18 with Social Security number can have a Trump Account.
- Only one Trump Account can be established per eligible child.

Contribution rules

- Annual contributions (other than certain exempt contributions) are limited to $5,000 per year, per child, before the year the child turns 18.
- No contributions are allowed until 12 months after the law's enactment; therefore, the date would be July 4, 2026.
- Certain types of contributions (like rollovers, government or employer contributions) do not count toward the $5,000 limit.
- No deduction is allowed for contributions made before the child turns 18.

Investment restrictions

- Until the child turns 18, the account can only be invested in low-fee, broad-based U.S. stock index funds or ETFs that track the S&P 500 or similar indexes.
- No leverage or high-fee funds are allowed.

Distribution rules

- No withdrawals are allowed before the year the child turns 18, except for specific rollovers or in the event of the child's death.
- If the child dies before age 18, the account is included in the estate or passed to beneficiaries, with special tax rules.
- If excess contributions are made, they must be withdrawn, and any earnings on excess are taxed at 100%.

Special rollovers

- At age 17, the entire Trump Account can be rolled over tax-free to an ABLE account (for individuals with disabilities) for the same beneficiary.
- Rollovers to a Trump Account for the same child is also allowed.

Employer and charitable contributions

- Employers can contribute up to $2,500 per year to an employee's child's Trump Account, tax-free to the employee.
- Charitable organizations and government entities can make "qualified general contributions" to groups of Trump Accounts (for example, all children in a state or birth year).

Government-funded pilot program

- For children born between Jan. 1, 2025, and Jan. 1, 2029, parents can elect to receive a $1,000 government contribution into their child's Trump Account.
- The payment is made as a refundable tax credit, paid directly into the account.
- Both the parent and the child must have Social Security numbers.

Tax treatment

- Trump Accounts are generally tax-deferred like traditional IRAs.
- Certain contributions (like government or charitable contributions) are excluded from gross income.
- Distributions after age 18 are taxed under normal IRA rules.

Trump Accounts are a new tax-advantaged savings vehicle for children under 18. With strict investment and contribution rules, this government-funded pilot program provides $1,000 to eligible newborns' accounts. The goal is to encourage early, long-term investments for children, with strong oversight and limited early access to funds.

Changes to miscellaneous itemized deductions

Starting with tax year 2026, taxpayers are permanently unable to claim miscellaneous itemized deductions that were previously suspended under the *Tax Cuts and Jobs Act* (TCJA). This means that deductions such as unreimbursed employee expenses, tax preparation fees and investment are permanently no longer available.

The law expands and clarifies the deduction for educator expenses, allowing teachers, instructors, counselors, principals, aides, and now interscholastic sports administrators and coaches to deduct certain out-of-pocket expenses related to their instructional activities.

If you are an educator, you may benefit from these expanded deductions. For all other taxpayers, miscellaneous itemized deductions will no longer be available after 2025.

Conclusion

As always, we're here to help you navigate these new rules and make the most of your tax situation. If you have questions or want to discuss your personal circumstances, please contact our office. We're committed to helping you thrive under the new law.