

Tips and Overtime on Your 2026 W-2

A year-end kit to get your 2026 W-2s right the first time, including the overtime calculation most payroll systems get wrong. For employers with tipped or hourly staff.

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The real deadline is your last pay run of 2026. After it, the year's totals are final and every fix becomes a manual correction before W-2s go out on February 1, 2027.

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SECTION 1

What changed on the W-2

The new federal deductions for qualified tips and qualified overtime belong to your employees. For wages paid in 2026, the reporting belongs to you, on the W-2, in three new places.

W-2 ENTRY	WHAT GOES THERE	BUILT FROM
Box 12, code TP	Total cash tips reported to the employer	Employee tip reports and point-of-sale data, all year
Box 12, code TT	Total qualified overtime compensation	The FLSA overtime premium, every pay period
Box 14b	Treasury Tipped Occupation Code, up to two per employee	Your mapping of each tipped role to Treasury's list

Dates and rules to know. 2026 W-2s are due to employees and the Social Security Administration by **February 1, 2027**, because January 31 falls on a Sunday. The transition relief that covered 2025 does not carry forward. Box 14b is required whenever code TP reports tips. What used to be box 14 is now box 14a.

Only the premium counts

Qualified overtime is not the employee's overtime pay. It is only the premium portion that section 7 of the Fair Labor Standards Act requires: the extra half in time and a half. An employee earning \$24 an hour who works 10 overtime hours at \$36 receives \$360 of overtime pay, and has **\$120** of qualified overtime.

\$360 overtime pay · 10 hours at \$36

\$240 regular rate (\$24 × 10 hrs)	\$120 premium
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Ordinary wages, not deductible

QUALIFIED OVERTIME · W-2 BOX 12, CODE TT

- **Exempt employees do not qualify**, even if you pay them extra for long weeks.
- **Double time counts only up to time and a half.** The extra beyond that is ordinary wages.
- **Overtime beyond what the FLSA requires does not count**, including overtime paid by policy or contract.
- **Texas adds no overtime rules of its own**, so the federal calculation is the whole calculation.

SECTION 2

The regular-rate trap

The premium is half the employee's **regular rate** for each overtime hour. The regular rate is not always the hourly rate. Non-discretionary bonuses, production and attendance bonuses, shift differentials, and commissions generally go into it.

Example: \$20 an hour, 50 hours in the week, \$100 production bonus.

WHAT MANY SYSTEMS DO	WHAT THE FLSA REQUIRES
40 hrs × \$20 = \$800	50 hrs × \$20 + \$100 bonus = \$1,100
10 hrs × \$30 = \$300	\$1,100 ÷ 50 hrs = \$22 regular rate
Bonus = \$100	10 hrs × \$11 premium = \$110
Total \$1,200 · premium \$100	Total \$1,210 · premium \$110

The system that paid \$1,200 underpaid the employee \$10 under federal wage law, and its code TT figure would be \$100 instead of \$110. When a non-discretionary bonus covers a quarter or a year, it has to be allocated back over the weeks it was earned and the premium recalculated for those weeks. That adjustment changes qualified overtime too.

THE 30-SECOND CHECK

Compare total overtime paid this year with total code TT. At time and a half, the premium is one third of overtime pay, so code TT should be **roughly one third of total overtime pay or less**. If the two numbers are equal, the system is reporting overtime pay instead of the premium, and every W-2 with overtime will be wrong.

SECTION 3

Tips: what counts and what does not

COUNTS AS A QUALIFIED TIP	DOES NOT COUNT
Voluntary amounts the customer decides on, in cash or charged to a card, debit card, gift card, or similar cash-denominated method	Mandatory service charges, large-party charges, and automatic gratuities, unless the customer can remove or change them without consequence
Tips received in one of 68 occupations on Treasury's list, each with a three-digit Treasury Tipped Occupation Code	Tips received by someone who owns 5% or more of the business paying them

SECTION 4

Year-end setup checklist

Work through these with whoever runs your payroll. Most employers can finish in an afternoon. The point is to find problems in October or November, not in the week W-2s are due.

STEP	WHAT TO CHECK	DONE
☐ 1. Separate the earnings	Regular wages, overtime straight-time, FLSA overtime premium, overtime not required by the FLSA, reported cash tips, and service charges each need to be distinguishable at year-end.	
☐ 2. Get the regular rate right	The most common error. Confirm the premium is calculated on the FLSA regular rate, including non-discretionary bonuses and shift differentials, and that period bonuses are allocated back.	
☐ 3. Confirm who is exempt	Check every employee's FLSA status in the system. Nothing paid to exempt staff belongs in code TT.	
☐ 4. Map tipped roles to occupation codes	Assign a Treasury Tipped Occupation Code to each tipped role. Employees who work two tipped roles can carry two codes. Flag roles that do not fit the list.	
☐ 5. Keep service charges out of tips	Check the point-of-sale setup. Automatic gratuities and mandatory fees are wages, not code TP.	
☐ 6. Flag owners	Tips received by anyone who owns 5% or more of the business are not qualified tips.	
☐ 7. Verify names and SSNs	A valid Social Security number is required for the deduction. Use the SSA's free verification service before W-2s are generated.	
☐ 8. Test five employees	A tipped employee, a nonexempt employee with overtime, one with a bonus, one in two roles, and one exempt. Calculate TP, TT, and 14b by hand and compare.	
☐ 9. Reconcile before W-2s go out	Tie year-to-date wages to Forms 941, tie code TP to tip records, and run the 30-second check on code TT.	

Quick reference for employee questions

	TIPS	OVERTIME
Maximum deduction	\$25,000 per year, 2025 through 2028	\$12,500 single, \$25,000 joint, 2025 through 2028
What counts	Voluntary cash and charged tips in a listed occupation	Only the FLSA-required premium
Phase-out begins	\$150,000 MAGI single, \$300,000 joint	\$150,000 MAGI single, \$300,000 joint
Keep in mind	Valid SSN required. Married couples must file jointly. Social Security and Medicare still apply to tips and overtime.	

SECTION 5

Six questions for your payroll provider

If you use an outside payroll service, these answers tell you quickly whether you are covered. The first one matters most: anything other than "only the premium" means the rest needs a closer look.

1. Will box 12, code TT show only the FLSA overtime premium, or total overtime pay?

2. Is the premium calculated on the FLSA regular rate, including non-discretionary bonuses and shift differentials?

3. How does the system handle a bonus paid for a prior period?

4. Where do I enter Treasury Tipped Occupation Codes, and can an employee carry two?

5. How are service charges and automatic gratuities kept out of code TP?

6. Can I see a preview of box 12 and box 14b for my employees before year-end?

If part of 2026 was recorded the wrong way

It is usually fixable, and the earlier the better. Work through it in this order:

- A** Export payroll registers and time records by workweek for every 2026 pay period so far.
- B** Isolate overtime hours: hours over 40 in each workweek, for nonexempt employees only.
- C** Find weeks with non-discretionary bonuses, shift differentials, or commissions. Recalculate the regular rate for those weeks and allocate period bonuses back to the weeks they cover.
- D** Rebuild tips by employee from point-of-sale and tip reports, with service charges removed.
- E** Write the method down on one page and keep it with payroll records.
- F** Load corrected year-to-date totals before your last pay run of 2026, then reconcile.

If the recalculation shows overtime was underpaid, the difference is owed to the employee as wages, so involve your advisor in how it is paid. Errors found after W-2s are issued are corrected with Form W-2c.

[COMPANY NAME]

About the new tips and overtime tax deductions

Starting with 2025, eligible employees may be able to deduct **qualified tips**, up to \$25,000, and **qualified overtime**, up to \$12,500, or \$25,000 for married couples filing jointly, on their federal income tax return.

These are income tax deductions only. Social Security and Medicare taxes still apply to tips and overtime, and your paycheck withholding does not change automatically.

For overtime, only the extra "half" of time-and-a-half pay required by federal law counts, not the full overtime paycheck. For example, if you earn \$24 an hour and work 10 overtime hours at \$36, \$120 of that counts.

Starting with your 2026 Form W-2, you will see:

- Your reported cash tips in **box 12 with code TP**
- Your qualified overtime in **box 12 with code TT**
- If you work in a tipped role, an occupation code in **box 14b**

Your tax preparer will use these amounts. The deductions phase out at higher incomes, require a valid Social Security number, and require married couples to file jointly. Please talk with your own tax preparer about how they apply to you.

Questions about the amounts on your W-2? Contact [PAYROLL CONTACT NAME] at [PHONE OR EMAIL].

Want a second set of eyes before your last pay run?

We will review your payroll setup against this kit, including the regular-rate calculation and the occupation code mapping, so your 2026 W-2s go out right the first time.

CONTACT

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READ MORE

No Tax on Tips and Overtime: What Employers Actually Have to Do

secondmilecpa.com/insights/tips-overtime-deduction-employer-guide/

Payroll Setup for Tips and Overtime: A Checklist Before Your 2026 W-2s

secondmilecpa.com/insights/payroll-w2-tips-overtime-setup/

This kit is general information, not individualized tax or legal advice. FLSA classification and regular-rate questions can have legal consequences. Rules and thresholds can change; verify current IRS guidance and discuss your specific situation with a qualified professional before acting.
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