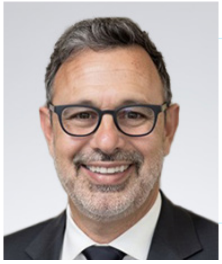
Payroll Insights

Employment tax news to guide you now and for the future

July 2026



John's *fresh take*: Decoding OBBBA W-2 guidance and overtime calculations

It is hard to believe it has already been a year since the payroll world was upended by the One Big Beautiful Bill Act (OBBBA). Since its enactment on July 4, 2025, *Payroll Insights* has provided continuous coverage to help payroll professionals decode the legislation and adapt to its changes.

To support you through this transition, our Washington National Tax practice has meticulously analyzed every facet of the OBBBA and its business impact (read the full breakdown: KPMG reports: Tax subtitle for "One Big Beautiful Bill Act"). We even have podcast episodes dedicated to OBBBA. (You can listen here!)

Much of our recent reporting has focused on the deductions for qualified overtime compensation and qualified tips. While the initial grace period spared employers from immediate reporting changes, the lack of early guidance left many brainstorming compliance stopgaps.

Fortunately, the Internal Revenue Service (IRS) has since issued definitive guidance for 2026 Form W-2 reporting:

- Box 12, Code TP: Use to report total cash tips reported to the employer.
- Box 12, Code TT: Use to report qualified overtime premiums.

Despite having clear Form W-2 guidance, one of the biggest ongoing struggles we see clients facing is the actual calculation of qualified overtime premiums for Box 12, Code TT.

There are two major hurdles to reaching an accurate total:

- **Regulatory alignment:** Calculating overtime premiums strictly in accordance with the Fair Labor Standards Act (FLSA), rather than relying on state or union requirements
- **Isolating the premium:** Accurately separating the premium portion from regular overtime compensation.

Precision here is critical. Incorrectly reporting this information on Form W-2 can result in costly information reporting penalties for the employer. Downstream, it can also cause employees to overpay or underpay their personal income taxes by claiming the wrong deduction amount, creating an administrative and employee-relations nightmare.

While auditing your OBBBA compliance might not be your first choice for a summer activity, taking the time to review your processes now will save you from major headaches come year-end.

Additionally, other provisions, such as entity aggregation rules for the section 45S Paid Family and Medical Leave Act credit and the Section 162(m) deduction limitation, came into effect for tax years after December 31, 2025. Consider taking another look through our OBBBA analysis referenced above to make sure you're considering all the ways the law affects your tax compliance.

Federal updates

JCT releases Bluebook explaining recent federal tax law

The Joint Committee on Taxation (JCT) released its *General Explanation of the Tax Provisions of Public Law 119-21* (the Bluebook), providing insight into recently enacted federal tax legislation. The JCT is a nonpartisan, bicameral congressional committee staffed by experienced economists, attorneys, and accountants. Their primary role is to assist both the House and Senate with tax legislation. The Bluebook provides the JCT's explanations and interpretations of various statutory provisions for taxpayers and may guide future Treasury and IRS interpretations.

Notably, the report includes discussion of provisions affecting tips and overtime compensation and also identifies areas that may benefit from technical corrections. The JCT's explanations of the OBBBA's provisions include, but aren't limited to, the following:

No tax on tips

- Qualified tips should be reported on Form W-2, 1099-K, or 1099-NEC, or reported by the taxpayer themselves on Form 4137.
- The qualified tip deduction is permitted in addition to the standard deduction, if the taxpayer does not itemize their deductions.
- The taxpayer must report a Social Security Number to be eligible for the credit.

No tax on overtime

- Qualified overtime compensation must be reported by the employer separately on Form W-2. Note that alternative reporting may be available for workers who are treated as employees for FLSA purposes under the "economic reality test" but not for tax purposes.
- Qualified overtime compensation does not include qualified tips (i.e., not double counted).
- The qualified overtime compensation deduction is permitted in addition to the standard deduction, if the taxpayer does not itemize their deductions.
- The taxpayer must report a Social Security Number to be eligible for the credit.

Trump accounts

- Employers may contribute to the Trump account of an employee or an employee's dependent.
- These contributions are not includable in taxable wages.
- The employer must have a separate, written plan that is for the exclusive benefit of the employees.
- The employer's plan must meet requirements similar to those of a dependent care assistance program under Internal Revenue Code (IRC) Section 129 and comply with nondiscrimination, eligibility, and notice requirements.

Paid Family and Medical Leave Credit

- The 2017 provisions are permanently extended.
- Employers can choose to claim the credit based on wages paid or insurance premiums paid for certain policies.
- Employers within a controlled group are treated as a single employer and must have a written paid leave policy (with certain exceptions).
- No federal tax credit is allowed for any paid leave portion that is legally mandated by a state or local government.
- Qualifying compensation is annualized for purposes of calculating the compensation limits, and pro-rata for part-time employees.

Information reporting thresholds

- The threshold for reporting payments in the course of a trade or business increased from $600 to $2,000.
- This threshold for backup withholding conforms to the $2,000 threshold for reporting.
- The threshold will be indexed to the annual cost of living adjustment for calendar years after 2026.

ETAAC releases annual report

The Electronic Tax Administration Advisory Committee (ETAAC), established by Congress in 1998, provides a forum for the public to discuss concerns and submits an annual report to Congress of recommendations regarding electronic advancements and taxpayer security. In the 2026 annual report, released June 17, 2026, the ETAAC provides several recommendations related to payroll taxes:

- **Recommendation 1: Accelerate information reporting to combat fraud**

  To better detect and prevent refund fraud, the committee recommends accelerating the filing deadline for several critical information returns, including Form 1099-R (Distributions from Pensions, Annuities, Retirement, etc.) and Form 1099-K (Payment Card and Third Party Network Transactions), to January 31. The accelerated deadline provides the IRS with crucial data to verify income and withholding claims before fraudulent refunds can be issued.

- **Recommendation 14: Enhance e-services for payroll reporting agents**

  Payroll reporting agents currently lack adequate online tools to interact with the IRS. The report urges the creation of a dedicated online portal for these agents. This portal would allow them to validate client Taxpayer Identification Numbers, manage authorizations electronically, retrieve bulk transcripts, and resolve account issues efficiently, which could reduce the burden on IRS phone support significantly and enhance the taxpayer experience.

- **Recommendation 17: Prioritize e-filing for employer payroll tax returns**

  The requirement to file amended payroll tax returns (Form 94X series) on paper creates massive processing backlogs and errors, evidenced by the volume of Employee Retention Credit claims that took more than a year to process for some taxpayers. The ETAAC recommends prioritizing the development of an e-filing system for these amended returns to ease the administrative burden on small businesses, accelerate processing, and minimize manual transcription errors. This was also a recommendation from the Taxpayer Advocate Service in their annual report.

- **Recommendation 18: Make electronic W-2 delivery default**

  To mitigate mail-related identity theft and streamline delivery, the ETAAC proposes shifting the default method for employees to receive Form W-2 to electronic delivery from physical mailing. Reversing the current requirement to an "opt-out" system—where employees automatically receive Forms W-2 electronically unless they explicitly request paper—will align with modern digital payroll practices, increase security, and lower distribution costs for employers.

IRS announces 2027 HSA contribution limits

The IRS issued **Rev. Proc. 2026-24**, establishing the following 2027 annual Health Savings Account (HSA) limits for high-deductible health plans:

- **Contribution limit:**
  - Self-only coverage: $4,500
  - Family coverage: $9,000
- **Minimum deductible:**
  - Self-only: $1,750
  - Family: $3,500
- **Out-of-pocket maximums (including deductible):**
  - Self-only: $8,700
  - Family: $17,400
- **Direct Primary Care Service Arrangement (DPCSA)**

  Under OBBBA, a DPCSA is not treated as part of a high-deductible health plan provided that, with respect to any individual, the aggregate monthly fees are limited to $150 (or $300 in the case of an individual with any DPCSA that covers more than one individual).

Employers offering HSA-compatible plans should coordinate with payroll and benefits teams to update plan limits and ensure controls are in place to prevent excess contributions.

Projected 2027 Social Security wage base

In its 2026 Annual Trustees Report, released June 9, 2026, the Board of Trustees of the Federal Old-Age and Survivors Insurance and Federal Disability Insurance Trust Funds (Social Security) projected the 2027 Social Security wage base to be $190,200, up from $184,500 in 2026. The final wage base will be published in October.

The report notes that the Social Security fund is projected to be solvent through 2034 if there are no substantial changes to the program. The Board of Trustees provides recommendations for increases in tax rates and decreases in benefits that could make the fund solvent through 2100.

DOL issues opinion letters addressing overtime, bonuses, meal breaks, and preshift activities

The Department of Labor (DOL) issued four opinion letters addressing federal wage and hour standards under the FLSA. The DOL stated that the opinion letters provide official written interpretations addressing specific factual circumstances and may have broader interest to others affected by similar issues. The public can request an opinion letter at https://www.dol.gov/agencies/whd/opinion-letters/request.

The opinion letters address whether an exempt employee may perform additional work in a secondary hourly role, whether a bonus calculated by reference to total earnings satisfies overtime pay requirements, whether time spent during a meal break traversing employer premises and passing through controlled access is compensable, and whether certain hospital employee preshift activities are compensable work.

Proposed federal legislation would require payroll tax withholding for certain independent contractors

On June 2, 2026, H.R. 9114, titled the "Gig Is Up Act," was introduced in the House and referred to the Committee on Ways and Means for consideration. The bill would amend the Internal Revenue Code to require certain large businesses to pay an amount equal to twice the current employer portion of Social Security and Medicare taxes on compensation paid to independent contractors if they were treated as employees. Half of the Social Security and Medicare taxes paid would be included in the contractor's net earnings from self-employment.

The bill would apply to a business with, "[a]t least **$100,000,000** in gross receipts for a calendar year, and with whom at least **10,000** individuals contract to provide services other than as an employee during the calendar year." While this bill is in its infancy, it indicates the appetite for more direction around federal tax and reporting for gig economy workers.

State and local updates

Arkansas releases withholding tax formulas

On May 29, 2026, Arkansas released updated withholding tax tables and instructions, reflecting the reduced individual income tax rate signed into law on May 6, 2026. The updated rate (up to 3.7 percent) is effective January 1, 2026.

Georgia updates 2026 Employer's Tax Guide

The Georgia Department of Revenue (the Department) updated its 2026 Employer's Tax Guide in June 2026. The Department states that the guide is used to explain Georgia withholding tax guidelines.

Updates from the 2025 version include:

- Reduction to income tax rate and increase to standard deductions. While the tax rate decreased from 5.19 percent in 2025 to 4.99 percent (effective retroactively to January 2026), employers should have started withholding at the lower rate beginning May 11, 2026.
- Reminders of the effect of federal tax changes adopted by Georgia, including:
  - Not conforming to the federal increase to the state and local tax deduction cap (remains at $10,000)
  - Adopting exclusion from the employer requirement to report deduction for qualified overtime compensation and tips for 2026 only.

Accordingly, the new Form G-4, *Employee's Allowance Certificate*, was released June 3, 2026.

Massachusetts updates wage withholding regulations

The Massachusetts Department of Revenue published updated regulation 830 CMR 62B.2.1, Withholding of Taxes on Wages and Other Payments, dated June 5, 2026. Almost identical to the repealed section (830 CMR 62B.00), the updated regulation includes topics such as income subject to withholding, employers and other persons required to withhold, employer and employee reporting obligations, returns and payments, methods of calculation, multiple withholding, pensions and annuities, fringe benefits, and interest and penalties. Of note, the new regulation adds "calculation methods" to withholding tables as part of the Commissioner's ability to dictate tax to be withheld, likely to align with the new 4 percent surtax to high earners.

Massachusetts issues third quarter 2026 interest rates

The Massachusetts Department of Revenue issued Technical Information Release (TIR) 26-3 on May 27, 2026, announcing the quarterly interest rates on overpayments and underpayments. For withholding tax purposes, the TIR lists the overpayment interest rate as 6 percent and the underpayment interest rate as 8 percent.

New York issues third quarter 2026 interest rates

On June 1, 2026, the New York Department of Taxation and Finance issued the over-and underpayment interest rates for the third quarter of 2026. For withholding tax purposes, the overpayment interest rate is 6 percent, and the underpayment interest rate is 11 percent.

Virginia announces changes to online business accounts

Effective August 1, 2026, employers will be required to log in to separate websites to manager their payroll tax accounts. Prior to August 1, employers log into Virginia Tax Online Services for Business (iReg Login) for income tax withholding purposes and link their Virginia Employment Commission (VEC) unemployment insurance tax account to the same portal. Beginning August 1, there will be no change for the income tax withholding account, but employers must log in with the VEC (Employer Self Service) to access their unemployment insurance tax account. The VEC portal requires ID.me to log in, which is linked to an individual's Social Security Number and not general employer credentials. There can be multiple authorized users to access the employer account.

Contact us

John Montgomery
National Employment Tax Lead Partner
T: 212-872-2156
E: jmontgomery@kpmg.com

Mindy Mayo
Senior Managing Director, Employment Tax
T: 408-367-5764
E: mindymayo@kpmg.com

Manan Shah
Partner, Employment Tax
T: 404-739-5247
E: mananshah@kpmg.com

Samantha-Jo Marciliano
Managing Director, Employment Tax
T: 212-954-3841
E: smarciliano@kpmg.com

Some or all of the services described herein may not be permissible for KPMG audit clients and their affiliates or related entities.

Learn about us: | **kpmg.com**