New Year, New Tax Rules

By Brian Powers

The 2025 budget reconciliation bill (H.R. 1), also known as the One Big Beautiful Bill Act, or OBBBA, added new tax rules and made permanent many of the 2017 changes from the Tax Cuts and Jobs Act. Some of these new tax laws affect 2025 taxes (filed in 2026). Most will start in 2026 or later.

Key Tax Updates

What follows are most of the tax changes that you, as a small retail business owner, will face. *Disclaimer:* I am not a tax expert. Please discuss these issues with your tax professional.

SALT deduction cap increase. The state and local tax, or SALT, deduction allows taxpayers to deduct from their federal taxable income certain taxes paid to state and local governments. This includes state and local income taxes, property taxes, and sales taxes. Next year, the cap jumps from $10,000 to $40,000. It will continue to rise 1% each year through 2029.

Qualified business income deduction. The 20% deduction for noncorporate taxpayers, particularly for self-employed individuals and small business owners, which was instituted in 2017, was originally set to expire after 2025. It is now made permanent.

The rule allows eligible business owners to deduct 20% of their *qualified business income*, or QBI, from their federal income tax. For 2026, a new $400 minimum deduction applies to taxpayers with at least $1,000 of QBI. This deduction can lead to substantial tax savings.

QBI is the net amount of income, gain, deduction, and loss from a qualified trade or business. The multiple restrictions on QBI depend on the nature of the trade or business, total wages paid, and other matters.

To qualify for the QBI deduction, the business must be a pass-through (noncorporate) entity such as a sole proprietorship, partnership, S corporation, or LLC. Or it must be a certain type of trust or estate. Also, the taxpayer’s total taxable income must fall within certain limits, or the deduction might be reduced or eliminated.

Finally, rules apply depending on the amount of compensation the business pays. Owners must pay themselves reasonable wages, and those wages do not count as QBI.

As with everything tax-related, the rules get pretty complicated. This deduction, however, can result in significant tax savings for a small business. Tax software is a big help, but there is no substitute for a live tax professional to answer your questions.

Charitable contributions. Corporations can now deduct charitable contributions exceeding 1% of taxable income, up to 10% of taxable income. These deductions may carry forward for five years under certain circumstances.

Bonus depreciation. The OBBBA permanently reinstates 100% bonus depreciation. This allows businesses to deduct the full acquisition cost of qualifying assets immediately, rather than being able to deduct only annual depreciation expense for that asset.

For tax year 2026, companies can immediately expense up to $2.56 million of qualifying purchases, up from $1.25 million in 2025. The deduction phases out once total spending exceeds $4.09 million.

Interest expense limitation. The OBBBA changes how interest expenses are calculated. This will allow more businesses to deduct interest payments, especially if they have large capital investments.

Research and development deductions. Full deductions for R&D expenses have been reinstated. This should encourage innovation and investment in new projects.

Health and dependent care benefits. These continue to be a powerful way to reduce taxable income while supporting employees' well-being.

Premiums paid for group health insurance are fully deductible. Contributions to health savings accounts (HSAs), health reimbursement arrangements (HRAs), or flexible spending accounts (FSAs) can lower both FICA and income taxes.

Contribution limits in 2026 rise to $4,400 for individual HSAs and $8,750 for family coverage. The health FSA limit increases to $3,400, and the dependent care FSA is $7,500 per household.

Employer-provided childcare credit. Beginning in 2026, the OBBBA significantly increases the employer-provided childcare credit.

This year, employers can claim a tax credit equal to 25% of expenses incurred for providing childcare to employees, plus 10% of eligible resource and referral expenses, up to $150,000 per year.

In 2026, the 25% credit jumps to 40% of eligible costs. The maximum credit allowed increases to $500,000. For eligible small businesses, the credit is even higher: 50% of eligible costs and a maximum annual credit of $600,000.

Education Reimbursements for Employees. This is an often-overlooked tax strategy for small businesses. Setting up an education assistance plan is relatively simple. It can cover eligible expenses like books and training materials, equipment and supplies, and tuition and other fees.

The IRS allows employers to reimburse employees up to $5,250 per year for education costs, even if the training doesn't directly relate to their current job. This payment is tax-free to the employee and fully deductible for the business.

Form W-2

Each year brings W-2 changes that impact how income, deductions, and benefits are reported. Employers who fail to keep abreast of these changes risk penalties, audits, and filing delays.

Employers must issue W-2s to all employees—full-time, part-time, and temporary—by Jan. 31. Copies must also be filed with the Social Security Administration and possibly with your state department of revenue.

The IRS has released draft versions of the 2026 Form W-2 and Form W-2C. These include several changes arising from the OBBBA. These updates reflect new deductions and reporting obligations for employers. As of this writing, these changes to the W-2 forms have not been made final.

You can view and download the most recent forms at the IRS website: irs.gov/forms-instructions-and-publications. Your tax professional should also be able to provide you with the revised W-2 forms.

Tax on Overtime and Tips

The OBBBA allows eligible employees to deduct up to $25,000 of qualified tips and up to $12,500 of qualified overtime pay from their federal income taxes for the tax year 2025. These deductions apply only to federal income tax. They do not exempt tips or overtime from Social Security, Medicare, or state taxes.

For 2025, the IRS issued Notice 2025-62 (on Nov. 5, 2025), which provides employers transition relief for reporting of tips and overtime compensation. The IRS encourages employers to provide employees with separate accounting of overtime or tip compensation if they are able to do so, but this is not *required*. Employers will not face penalties for failing to provide a separate accounting of these amounts.

Beginning in the 2026 tax year, however, the IRS will require employers to report "qualified overtime compensation" on the W-2. As noted above, the form will likely include new lines for this purpose. Likewise, the 2026 Form W-4, expanded to five pages, will include new lines for employees to report estimated qualified tip and overtime income.

You can provide Notice 2025-69 to employees seeking IRS guidance on the eligible deduction for qualified tips and overtime: irs.gov/newsroom/treasury-irs-provide-guidance-for-individuals-who-received-tips-or-overtime-during-tax-year-2025

Increased Reporting Thresholds

The reporting threshold for a couple of forms will rise from $600 to $2,000, with adjustments for inflation starting in 2026. Form 1099-MISC applies to nonwage income like prizes and rents. Form 1099-NEC is for reporting nonemployee compensation (like independent contractors).

The threshold for Form 1099-K, which applies to payments through third-party networks, has reverted from $600 to its old level of $20,000 and requires at least 200 transactions. This reduces the number of forms to file.

Note that all income remains taxable, even if it falls below these new reporting thresholds.

Changes for Individuals—and Small Business Owners

Certain changes in the OBBBA affect individual taxpayers, which ultimately affect small business owners:

Higher standard deductions. These deductions increased for all categories of individual taxpayers.

New deductions for older taxpayers. These are for taxpayers age 65 and older, but certain income limits apply.

Complex, Even for Experts

The U.S. Tax Code, also known as the Internal Revenue Code, is extensive and complex. The official statutes, IRS regulations, and rulings total about 10 million words or about 75,000 pages. Not only is the code lengthy, but it is filled with incomprehensible rules and regulations. This makes it challenging even for tax professionals to navigate.

General information and guidance on OBBBA are available from the IRS at irs.gov/newsroom/one-big-beautiful-bill-provisions But when considering your tax liability, it’s best to seek professional advice.