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Federal News

IRS Announces 2026 COLAs for Transportation Fringes, FSA Deferrals

The IRS released cost-of-living adjustments (COLAs) for 2026 reflecting increases in the flexible spending arrangements (FSA) deferral limit and excludable transportation fringes, among other changes. The Revenue Procedure also addresses changes made for tax year 2025 by Public Law 119-21, known as the One Big Beautiful Bill Act (OBBA).

Qualified transportation fringes

The amounts that may be excluded from gross income for employer-provided qualified transportation fringe benefits (transportation in a commuter highway vehicle and any transit pass) and qualified parking for 2026 increase to \$340 (\$325 in 2025).

Health FSAs

For plan years beginning in 2026, the dollar limitation under IRC §125(i) on voluntary employee salary reductions for contributions to health FSAs increases to \$3,400 (\$3,300 in 2025). For cafeteria plans that permit the carryover of unused amounts, the maximum carryover amount increases to \$680 (\$660 in 2025).

Standard deduction

The standard deduction amounts for 2026 increase to \$32,200 for married couples filing jointly or surviving spouses, \$16,100 for single taxpayers and married taxpayers filing separately, and \$24,150 for heads of household. For 2025, the OBBA increased the

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standard deduction amounts to \$31,500 for married couples filing jointly or surviving spouses, \$15,750 for single taxpayers and married taxpayers filing separately, and \$23,625 for heads of household.

Federal tax levies

For taxable years beginning in 2026, the dollar amount used to calculate the amount determined under IRC §6334(d)(4)(B) increases to \$5,300 (\$5,100 in 2025).

Foreign earned income exclusion

For 2026, the maximum foreign earned income exclusion amount under IRC §911(b)(2)(D)(i) is \$132,900 (up from \$130,000 in 2025). The maximum amount of the foreign housing cost exclusion is \$18,606 (up from \$18,200 in 2025).

Medical Savings Accounts

To be eligible to make contributions to a Medical Savings Account (or to have the employer make the contributions), an employee must be covered by a high deductible health plan. For 2026, a high deductible health plan is a plan with an annual deductible of \$2,900-\$4,400 for individual coverage (up from \$2,850-\$4,300 in 2025) and 5,850-\$8,750 for family coverage (up from \$5,700-\$8,550 in 2025). Maximum out-of-pocket expenses can be no more than \$5,850 for individual coverage (up from \$5,700 in 2025) and \$10,700 for family coverage (up from \$10,500 in 2025).

Long-term care insurance benefits

If a long-term care insurance contract makes per diem benefit payments, the amount of the payments that is excluded from income in 2026 is capped at \$430 per day (up from \$420 in 2025).

Adoption assistance

For 2026, the maximum amount that can be excluded from an employee's gross income for qualified adoption expenses under an employer's adoption assistance program or in connection with the adoption of a child with special needs is \$17,670 (up from \$17,280 in 2025). The amount excludable from an employee's gross income begins to phase out for taxpayers with adjusted gross income of \$265,080 (up from \$259,190 in 2025) and is completely phased out for taxpayers with adjusted gross income of \$305,080 (up from \$299,190 in 2025).

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Qualified small employer HRA

For 2026, a qualified small employer health reimbursement arrangement (QSEHRA) is an arrangement which, among other requirements, makes payments and reimbursements for qualifying medical care expenses of an eligible employee that do not exceed \$6,450 (up from \$6,350 for 2025), or \$13,100 in the case of an arrangement that also provides for payments or reimbursements for family members of the employee (up from \$12,800 for 2025).

Pipeline construction industry per diem option

For 2026, an eligible employer may pay certain welders and heavy equipment mechanics up to \$23 per hour for rig-related expenses that will be deemed substantiated under an accountable plan (up from \$22 in 2025) and up to \$14 per hour for fuel (same as in 2025), when paid in accordance with Rev. Proc. 2002-41 (2002-23 IRB 1098).

Penalties increase

For tax years beginning in 2026 (forms filed in 2027), the penalty amounts under IRC §6721, failure to file correct information returns, and the penalty amounts under IRC §6722, failure to furnish correct payee statements, remain \$340 under the general rule, \$60 if corrected on or before 30 days after the required filing date, and \$130 if corrected after the 30th day but on or before August 1. For businesses with annual gross receipts of \$5 million or less, the maximum penalty increases to \$1,397,000 (up from \$1,366,000) under the general rule, to \$244,500 (up from \$239,000) if corrected on or before 30 days after the required filing date, and to \$698,500 (up from \$683,000) if corrected after the 30th day but on or before August 1. For businesses with annual gross receipts of more than \$5 million, the maximum penalty increases to \$4,191,500 (up from \$4,098,500) under the general rule, to \$698,500 (up from \$683,000) if corrected on or before 30 days after the required filing date, and to \$2,095,500 (up from \$2,049,000) if corrected after the 30th day but on or before August 1. For intentional disregard of the obligations under either of these provisions, the penalty increases to \$690 per return for 2026 (up from \$680), and there is no calendar year limit.

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IRS Announces 2026 COLAs for Transportation Fringes, FSA Deferrals (cont'd)

OBBBA changes

The revenue procedure contains amendments to the Internal Revenue Code made by the OBBBA, including:

Child tax credit (\$70104).

The child tax credit under IRC §24(h) is increased to \$2,200 from \$2,000 per qualifying child for 2026. The amount will be adjusted annually by the cost of living rounded to the next multiple of \$100.

Employer-provided child care credit (\$70401).

The OBBBA amends IRC §45F to increase the employer-provided child care tax credit, which is an incentive for businesses to provide child care services to employees. The credit is increased to \$500,000 from \$150,000 per year (\$600,000 for eligible small businesses) and will be adjusted annually for inflation after 2026.

Forms 1099-MISC and 1099-NEC reporting (\$70433).

The OBBBA amends IRC §6041(a) to increase the reporting threshold for reporting on Forms 1099-MISC, Miscellaneous Information, and Forms 1099-NEC, Nonemployee Compensation, from \$600 to \$2,000. This provision is effective beginning with payments made in 2026 and will be subject to inflation adjustments beginning in 2027.

Student loans (\$70412).

The OBBBA makes permanent the temporary Coronavirus Aid, Relief, and Economic Security Act provision allowing qualified employer-provided student loan repayment assistance to be treated as qualified educational assistance under IRC §127. In 2027, the limit for qualified educational assistance will be adjusted for inflation in multiples of \$50. The current limit is \$5,250.

Tax rates (\$70101).

The OBBBA makes permanent tax rates for individual taxpayers from the Tax Cuts and Jobs Act – 10%, 12%, 22%, 24%, 32%, 35%, and 37%.

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Social Security Wage Base Increases to \$184,500 for 2026

The Social Security Administration (SSA) announced that the 2026 social security wage base will be \$184,500, an increase of \$8,400 from \$176,100 in 2025.

Maximum social security tax.

The maximum social security tax employees and employers will each pay in 2026 is \$11,439, an increase of \$520.80 from \$10,918.20 in 2025.

Medicare tax.

As in prior years, there is no limit to the wages subject to the Medicare tax therefore, all covered wages are subject to the 1.45% tax. As in 2025, wages paid in excess of \$200,000 in 2026 will be subject to an extra 0.9% Medicare tax that will only be withheld from employees' wages. Employers will not pay the extra tax. Note that the \$200,000 threshold for the Additional Medicare tax is not subject to adjustments for inflation.

FICA (combined) tax.

The FICA tax rate, which is the combined social security tax rate of 6.2% and the Medicare tax rate of 1.45%, will be 7.65% for 2026 up to the social security wage base.

Self-employed.

The social security wage base for self-employed individuals in 2026 will also be \$184,500. There is no limit on covered self-employment income subject to the Medicare tax. The self-employment tax rate will be 15.3% (combined social security tax rate of 12.4% and Medicare tax rate of 2.9%) up to the social security wage base. In 2026, the maximum social security tax for a self-employed individual will be \$22,878.

Quarters of coverage retirement earnings test

The SSA also announced that the amount of earnings needed to qualify for a quarter of coverage to receive full social security benefits will be \$1,890 in 2026, up from \$1,810 in 2025. Retirees who will not reach full retirement age in 2026 can earn up to \$24,480 a year (\$2,040 a month) without losing any benefits (up from \$23,400 a year/\$1,950 a month in 2025) for these retirees, \$1 in benefits will be withheld for every \$2 in earnings above the applicable limit. Retirees who reach full retirement age in 2026 will lose \$1 in benefits for every \$3 earned above \$65,160 (up from \$62,160 in 2025), but only counting earnings before the month they reach full retirement age. Starting with the month retirees reach full retirement age, they will receive full benefits with no limit on earnings.

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FICA threshold for domestic, election workers

The threshold for coverage under social security and Medicare for domestic employees (i.e., the “nanny tax”) will increase to \$3,000 in 2026 (up from \$2,800) the coverage threshold for election workers will increase to \$2,500 (up from \$2,400)

IRS Releases Draft 2026 Publication 15-T

On November 5, the IRS released a draft of the 2026 Publication 15-T, Federal Income Tax Withholding Methods, with a worksheet that contains the tax tables. A final version of Publication 15-T is not available yet. In past years, the IRS has said the table data can be used for programming. There is no confirmation for this year due to the government shutdown.

DOL Publishes Four FLSA, FMLA Opinion Letters

The U.S. Department of Labor (DOL) published four opinion letters that provide guidance to help employers comply with the Fair Labor Standards Act (FLSA) and the Family and Medical Leave Act (FMLA). The opinion letters provide official written interpretations from the DOL that address real-world questions and explain how laws apply to specific circumstances.

For information regarding FLSA: Tip pool (FLSA2025-03), FLSA: Emergency pay (FLSA2025-04), FLSA: Horizontal joint employers (FLSA2025-05), and FMLA: Leave calculation (FMLA2025-02-A) opinion letters please see the DOL website or Payroll Currently, Volume 33 Issue 11.

Opinion letter program

The DOL relaunched its opinion letter program in June. Employers can use the DOL’s Opinion Letters webpage to explore past guidance and submit new requests.

IRS Provides Penalty Relief for TY 2025 OBBBA Reporting Requirements

For tax year (TY) 2025, the IRS will provide employers with penalty relief in connection with new information reporting requirements for qualified tips and qualified overtime compensation required under Public Law 119-21, known as the One Big Beautiful Bill Act (OBBBA) [Notice 2025-62, 11-5-25]. The penalty relief is under IRC §6721 for failure to file correct information returns and §6722 for failure to furnish correct payee statements. The IRS is aware employers may not have the information required to be reported under the OBBBA. The IRS had already announced that Forms W-2 and Forms 1099 for TY 2025 will not be updated to account for OBBBA- related changes (see PAYROLL CURRENTLY, Issue 9,



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Vol. 33). Instead, the IRS will treat TY 2025 as a transition period for IRS enforcement and administration of the new information reporting requirements for cash tips and qualified overtime compensation under the OBBBA.

Transition penalty relief for TY 2025

The guidance states that employers will not face penalties for failing to provide a separate accounting of any amounts reasonably designated as cash tips or the occupation of the person receiving such tips. In addition, employers will also not face penalties for failing to separately provide the total amount of qualified overtime compensation to employees. The relief is limited to returns and statements filed and provided for TY 2025. PayrollOrg's Government Relations staff met with the IRS this summer and requested this transition relief (see "Inside Washington" for August 2025). The notice encourages employers to provide employees, particularly those in a tipped occupation, with the occupation codes and separate accountings of cash tips. Employers also are encouraged to provide employees with separate accountings of overtime compensation. Employers can inform employees through an online portal, written statements, or, in the case of qualified overtime compensation, in Box 14 of the employee's Form W-2.

IRS Updates Notice With Deposit Requirements for Employment Taxes

The IRS updated Notice 931, Deposit Requirements for Employment Taxes, which contains federal tax deposit requirements for forms in the 94X series, including Form 941, Employer's Quarterly Federal Tax Return.

Deposits must be made by EFT

Employers must use electronic funds transfer (EFT) to make federal tax deposits, which can be made using the Electronic Federal Tax Payment System (EFTPS), IRS Direct Pay (see PAYROLL CURRENTLY, Issue 4, Vol. 33), or an IRS business tax account (see PAYROLL CURRENTLY, Issue 2, Vol. 33). Payroll service providers, tax professionals, or other trusted third parties can also arrange to make electronic deposits for employers.

Payments over \$1 million.

The updated notice includes information about cutoff times for payments submitted via EFTPS that are over \$1 million. EFTPS accepts same-day payments of \$1 million or less if the payment is submitted before 3 p.m. ET on a business day. Payments that are more than \$1 million must be submitted by 8 p.m. ET the day before the date the deposit is due.

DHS Ends EAD Automatic Extensions

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The Department of Homeland Security (DHS) issued an interim final rule to end the automatic extension of employment authorization documents (EADs) for aliens who file renewal applications in certain employment authorization categories effective October 30, 2025 [90 F.R. 48799, 10-30-25]. The interim final rule does not affect EADs automatically extended before October 30, 2025. EADs issued on or after October 30, 2025, will now expire on the day after the end validity date on the document.

Interim final rule

DHS is amending its regulations to eliminate automatic extensions for EAD validity and/or employment authorization for up to 540 days for renewal applications filed on or after October 30, 2025. These renewal EAD applicants will no longer receive automatic extensions of their EADs and/or employment authorization. No impact on TPS documentation. The interim final rule does not impact automatic extensions otherwise provided by law or in a Federal Register notice that extends the validity of temporary protected status (TPS)-related employment documentation. More information is available on USCIS's Employment Authorization Document webpage.

Form I-9 requirements

The interim final rule does not modify the current requirements an employer must follow for Form I-9, Employment Eligibility Verification, for reverifying employment authorization and documentation. USCIS said it will update I-9 Central and the M-274, Handbook for Employers, to provide specific guidance on Form I-9 completion. Find Form I-9 and links to I-9 Central and the M-274 Handbook in PayrollOrg's Resource Library



State News

California

IRC conformity. The state’s Internal Revenue Code (IRC) conformity date has been updated to 1-1-25, from 1-1-15. Because 1-1-25 is before H.R. 1, known as the One Big Beautiful Bill Act (OBBBA Pub. L. 119-21), was signed into law, state tax law will not conform to changes included in the OBBBA. This means California will not offer a state tax exemption for overtime pay or a state tax deduction for tip income. The law updating the state’s IRC conformity decouples it from several provisions of the Tax Cuts and Jobs Act (TCJA). California’s previous conformity date was before the TCJA was signed in 2017, so the state had not been following the TCJA.

Pay data reporting requirements updated. Beginning with reports due in 2026, employers are required to keep any demographic information collected stored separately from employee personnel records. Also beginning in 2026, penalties for noncompliance are mandatory. Penalties of up to \$100 per employee for any employer that fails to file the required report, and up to \$200 for subsequent failure, are currently discretionary. For reports due in 2027, the number of job categories will increase from 10 to 23.

Iowa

State agencies required to use E-Verify. Effective 10-8-25, the governor signed an executive order requiring all state government agencies to verify employment eligibility. All state agencies within the executive branch, along with the Board of Regents, must use E-Verify to confirm the employment eligibility of newly hired employees.

Maine

Minimum wage, tip credit to increase. Effective 1-1-26, the minimum wage will increase to \$15.10 per hour from \$14.65 per hour (this updates The Payroll Source®, §2.11-1). Also effective 1-1-26, the minimum cash wage for tipped employees will increase to \$7.55 per hour from \$7.33 per hour. This means that the tip credit will increase to \$7.55 per hour from \$7.32 per hour, effective 1-1-26.

OBBBA guidance issued. The state will not adopt the “no tax on tips” and “no tax on overtime” provisions for state tax purposes for tax year 2025. Both provisions are from H.R. 1, known as the One Big Beautiful Bill Act (OBBBA Pub. L. 119-21). Decisions have not been finalized for future years.

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White collar salary threshold to increase. Effective 1-1-26, the minimum salary exemption threshold for executive, administrative, and professional employees will increase to \$871.16 per week from \$845.21 per week (or to \$45,300.32 per year from \$43,950.92 per year). The minimum salary threshold for exempting a worker from overtime pay must exceed 3,000 times the state minimum wage.

Withholding tables updated. Effective for wages paid on or after 1-1-26, the wage bracket and percentage method withholding tables have been updated (see 2026 Withholding Tables for Individual Income Tax). The supplemental wage tax rate remains 5%.

Massachusetts

OBBBA draft guidance issued. The Department of Revenue (DOR) drafted guidance that explains Massachusetts income tax determines gross income based on the Internal Revenue Code (IRC) as amended and in effect on January 1, 2024. Because H.R. 1, known as the One Big Beautiful Bill Act (OBBBA Pub. L. 119-21), was signed on July 4, 2025, Massachusetts will not conform to the “no tax on tips” and “no tax on overtime” provisions for state tax purposes. The draft guidance contains a chart that lists no to conformity for both items.

Michigan

State tax deductions for tips, overtime permitted. For tax years 2026 to 2028, Michigan will permit state tax deductions for qualified tips and qualified overtime compensation, conforming the state to H.R. 1, known as the One Big Beautiful Bill Act (OBBBA Pub. L. 119-21). For nonresidents, only qualified tips and qualified overtime compensation attributable to services performed in Michigan may be deducted. Note that the federal allowances are retroactive to 1-1-25. For state tax purposes, the deductions will not be permitted until tax year 2026.

Minnesota

PFML to go into effect in 2026. By 12-1-25, employers must inform employees about their rights and benefits under the paid family and medical leave (PFML) program. Employees must be notified in their native language. Employers must hang a workplace poster in English and any language spoken by five or more employees. Contributions are 0.88% of employee wages up to the federal social security wage base in 2026 (\$184,500). Employers must pay at least 50% of the total contribution and can deduct the rest from employee wages, meaning the maximum employee contribution rate will be 0.44% for 2026 (\$811.80). Contributions will be due on a quarterly basis, with the first payment due on

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April 30, 2026. Small employers will pay 0.22% (half of the standard employer contribution rate).

Nebraska

Minimum wage, tip credit to increase. Effective 1-1-26, the minimum wage will increase to \$15 per hour from \$13.50 per hour (this updates The Payroll Source®, §2.11-1). Also effective 1-1-26, the tip credit will increase to \$12.87 per hour from \$11.37 per hour (this updates The Payroll Source®, §2.11-2). The minimum cash wage remains \$2.13 per hour.

New Jersey

Minimum wage to increase tip credit unchanged. Effective 1-1-26, the minimum wage for most employers will increase to \$15.92 per hour. The minimum cash wage for tipped employees will increase to \$6.05 per hour. The tip credit remains \$9.87 per hour.

New Mexico

Electronic filing and payment required. Effective 1-1-26, employers must file quarterly withholding returns and make withholding tax payments electronically. Employers must also file annual withholding statements electronically. Currently, employers with 25 or more employees are required to file withholding returns and make withholding tax payments electronically. Also effective 1-1-26, quarterly withholding returns will be due on the 25th day of each month following the end of the calendar quarter. Currently, the due date is the last day of the month following the end of the quarter.

Ohio

Minimum wage, tip credit to increase. Effective 1-1-26, the minimum wage will increase to \$11 per hour. The tip credit will increase to \$5.50 per hour. The minimum cash wage for tipped employees will increase to \$5.50 per hour. Employers grossing less than \$405,000 (currently \$394,000) annually can pay employees the federal minimum wage rate of \$7.25 per hour.

Rhode Island

OBBBA guidance issued. The Department of Revenue (DOR) clarifies that employees may qualify for the “no tax on tips” and “no tax on overtime” provisions in H.R. 1, known as the One Big Beautiful Bill Act (OBBBA Pub. L. 119-21), for federal tax purposes. However, Rhode Island is decoupled from this tax treatment and will not allow for these exclusions from state taxable income.

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South Dakota

Minimum wage, tip credit to increase. Effective 1-1-26, the minimum wage will increase to \$11.85 per hour. Also effective 1-1-26, the minimum cash wage (50% of minimum wage) for tipped employees will increase to \$5.93 per hour. The tip credit will increase to \$5.92 per hour.