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Tax Newsletter

Five OBBBA Changes on 2025 Returns

New law provisions in effect now

The impact of the new One Big Beautiful Bill Act (OBBBA)—signed last 4th of July—will resonate for years to come. Some major changes are reflected on your 2025 personal income tax return. Here are five key OBBBA provisions that could have implications this tax return season.

1. Senior citizen deduction: Individuals who are age 65 or older already benefit from an additional standard deduction. In 2025, this deduction is \$2,000 for single filers and \$1,600 for each qualified spouse filing a joint return. But the OBBBA provides a brand-new tax “bonus” for senior citizens.

This bonus deduction is \$6,000 for each qualified individual whether you claim the standard deduction or itemize. Accordingly, if both spouses are age 65 or over, a couple can add on a \$12,000 deduction virtually out of the blue. To qualify, you must have turned age 65 before January 1, 2026.

However, the senior citizen deduction is phased out based on modified adjusted gross income (MAGI). The phase-out begins at \$75,000 of MAGI for single filers and \$150,000 for joint filers.

2. Auto loan interest: For the first time in decades, individuals can deduct some or all of their annual auto loan interest. The OBBBA creates a deduction for up to \$10,000 of interest paid on a loan to buy a qualified domestically-assembled vehicle. This deduction is available for 2025 through 2028.

The deduction may be claimed whether or not you itemize but is also subject to a phase-out based on MAGI. In this case, the phase-out begins at \$100,000 of MAGI for single filers and \$200,000 for joint filers.

3. SALT deductions: Previously, the Tax Cuts and Jobs Act (TCJA) temporarily capped the annual itemized deduction for state and local tax (SALT) payments at \$10,000. The OBBBA raises this annual limit to \$40,000, beginning in 2025, and indexes it for inflation, with certain provisos.

As before, you may deduct both (a) property tax and (b) income or sales tax payments. In addition, the \$40,000 cap is gradually reduced if MAGI exceeds \$500,000 until it reaches a bottom cap of \$10,000. And the \$40,000 cap is scheduled to revert to \$10,000 in 2030.

4. Overtime pay: Beginning on 2025 returns, you can deduct qualified overtime pay—based on a “time-and-a-half” rate for non-salaried workers—for up to \$12,500 for single filers and \$25,000 for joint filers. This change is retroactive to wages earned on or after January 1, 2025. However, the deduction is only available for the “premium” portion of overtime pay attributable to the time-and-a-half rate.

This deduction is phased out beginning at \$150,000 of MAGI for single filers and \$300,000 for joint filers. It is scheduled to expire after 2028.

5. Tips: The OBBBA also carves out an “above-the-line” deduction of up to \$25,000 for qualified tips received during the year, comparable to the tax break for overtime pay. The deduction is available for tips received in industries where tipping is commonplace. For instance, waiters and hair salon workers would normally qualify, but not airplane pilots or nurses.

Other OBBBA changes may affect the 2025 return that is due April 15, 2026, but many will kick in next year or later.

Best approach: Do not leave matters to chance. Rely on a tax professional to help you maximize the benefits.

R&E Expenditures Back on Fast Track OBBBA restores current deductions

Does your company spend money on research and experimental (R&E) activities to keep up with the competition or stay ahead of the pack? Due to recent legislation, those costs were no longer currently deductible and had to be amortized over time. But the One Big Beautiful Bill Act (OBBBA) restores the current deduction for R&E expenditures, retroactive to the beginning of 2025.

Background: Prior to the Tax Cuts and Jobs Act (TCJA), qualified R&E expenditures could be deducted in full in the tax year in which they were incurred. This deduction was separate and apart from the research and development (R&D) credit, although the two tax breaks relied on some of the same eligibility rules. Notably, R&E expenditures had to meet the following requirements to be currently deductible.

- The expenditures are incurred in connection with a trade or business.
- The expenditures are reasonable based on the circumstances.
- The activities are in the nature of research and development in an experimental or laboratory sense and aimed at discovering information that eliminates uncertainty in product development or improvement.
- The activities are for the development or improvement of products and processes, including software.

These expenditures included wages, materials, contract research, patent attorney fees and related costs.

Beginning in 2022, the TCJA required businesses to capitalize and amortize the expenditures over five years. This period was extended to 15 years for foreign research expenditures.

Now the OBBBA revives the pre-TCJA tax treatment for R&E expenditures. Beginning on 2025 returns, a business can choose to currently deduct its qualified R&E expenditures instead of amortizing them over five years. Caveat: The 15-year write-off period remains in place for foreign expenditures. In addition, a business can elect to accelerate domestic research expenditures that were capitalized and not yet amortized over a period of one or two years.

The OBBBA contains various other transitional rules that may apply to R&E expenditures. For example, an eligible small business may elect to retroactively deduct expenditures going back to 2022. This could affect deductions claimed on 2022, 2023 and 2024 tax returns. As a result, however, businesses may have to reduce the R&D credits claimed. This would be reflected on the amended returns filed with the IRS.

Finally, qualified small businesses may elect to retroactively treat this tax election as a change in their accounting method. The OBBBA instructs the IRS to provide more insights about this election in the near future.

Bottom line: Clearly, the rules for deducting R&E expenditures are not so cut-and-dried. Rely on your professional tax advisors for the necessary guidance.

The Tax Basics on Scholarships **Quick primer on the main rules**

Congratulations! You have just learned that your high school senior has qualified for a scholarship at a prestigious university this fall. Hopefully, the stipend will make a dent in a tough nut to crack. But what are the tax implications?

Answer: It depends. Generally, scholarships and fellowships at doctorate programs are exempt from federal income tax as long as certain conditions are met. However, in other cases scholarships or fellowships constitute taxable income that must be reported on the recipient's federal income tax return.

For starters, your child does not owe any tax on a scholarship that goes toward earning a college diploma. It does not matter if the money comes from the school or an outside source. To qualify for a tax exemption, the following three requirements must be met.

1. The child must be a degree candidate at an eligible educational institution. This is an institution with a regular faculty and curriculum and a regularly enrolled body of students.
2. The scholarship is used to pay for qualified expenses. This includes tuition and fees, books and related costs like supplies or equipment required for specific classes. It does NOT apply to room and board.
3. The award does not represent wages for teaching or other work.

In some cases, only a portion of the scholarship will be exempt from tax. For instance, if your child is in line for a \$25,000 award where \$15,000 is allocated to tuition and \$10,000 to room and board, the tuition part—\$15,000—is still excluded from tax. Accordingly, the remaining \$10,000 is treated as taxable income.

For these purposes, a “degree candidate” is defined as someone who—

- Attends a primary or secondary school or is pursuing a degree at a college or university, or
- Attends an educational institution that (1) provides a program that is acceptable for full credit toward a bachelor's or higher degree or offers a program of training to prepare students for gainful employment in a recognized occupation; and (2) is authorized under federal or state law to provide such a program and is accredited by a nationally recognized accreditation agency.

Conversely, a scholarship or fellowship is taxable if it represents compensation. For example, suppose your child in grad school is required to serve as a teaching assistant to qualify for a \$20,000 award. As a result, the entire \$20,000 is taxable, even if some or all of the money goes to tuition. The school will generally provide a Form W-2 to the student stating the income amount to be reported on their federal income tax return.

Finally, as alluded to above, scholarships are fully taxable to a student who is not a degree candidate at an eligible institution.

What about athletic scholarships? The rules can be tricky, but currently these amounts are usually exempt from tax, even if the school reasonably expects the student to participate in a particular sport. However, money awarded for a college athlete’s “name, image or likeness” (NIL) is generally taxable to the student-athlete.

Time out: The tax rules in this area are still evolving. Huddle with your professional tax advisor for the right tax play for your situation.

Will Your Child Graduate to a Roth?

If your child in high school or college expects to earn money from a summer job, they may want to splurge on new kicks or the latest iPhone. But you can propose a practical alternative for at least part of the cash: Contributing to a Roth IRA.

Are they old enough to do it? There is no age restriction as long as the child has “earned income” like wages. Contributions for the 2026 tax year are limited to \$7,500.

Be aware that tax-free distributions from a Roth IRA generally are not available until age 59½, but contributions may grow into a sizeable nest egg. Also, early withdrawals may be allowed without tax penalty due to disability or for a first-time home purchase (up to \$10,000). Finally, your child will learn a valuable lesson about saving for retirement!

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