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GMS Flash Alert

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United States – Inflation Adjustments for Tax Year 2026

On October 9, 2025, the U.S. Internal Revenue Service (IRS) released the annual inflation adjustments to be used by individual taxpayers on their 2026 returns (that is, the returns that are generally filed in 2027).[1] Over 60 tax provisions were updated, including tax rates and thresholds applicable to all taxpayers and certain provisions applicable to international assignees and expatriates.

The IRS also modified certain sections of the previous 2024 annual inflation adjustments to reflect amendments to the Internal Revenue Code by the One, Big, Beautiful Bill Act (OBBBA).[2] These changes relate to 2025 returns that are to be filed in 2026.

Additionally, on November 13, 2025, the IRS released the annual inflation adjustments applicable to 401(k) plans, IRAs, and other retirement savings and pension vehicles.[3]

In addition to the IRS releases, the U.S. Social Security Administration (SSA) announced[4] on October 24, 2025, that the maximum amount of wages subject to the Social Security tax will increase from $176,100 to $184,500 in 2026. This 4.7-percent increase is slightly more than the 4.4-percent increase of the prior year. The press release was accompanied by a fact sheet outlining the inflation adjustments to other key social security thresholds and limitations.[5]

WHY THIS MATTERS

Employers seeking to estimate the tax cost of an assignment from the United States to a foreign location may need to update their tax calculations to account for the increase in the foreign earned income exclusion and housing cost limitations. Additionally, employers may consider updating tax gross-up estimates to account for the updated income tax rate brackets and Social Security tax. Certain pension and Social Security limitations may be higher or lower due to assignment-related allowances, and these too may need to be taken into account in tax-equalization settlement calculations.

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Tax Rates for Individual Taxpayers, Adjusted for Inflation

With inflation adjustments, Rev. Proc. 2025-32 provides that for tax year 2026:

- The top income tax rate remains 37% for individual single taxpayers with taxable incomes greater than $640,600 ($768,700 for married couples filing jointly).
- The other income tax rates for single taxpayers will be:
  - 35% for taxable incomes over $256,225 ($512,450 for married couples filing jointly)
  - 32% for taxable incomes over $201,775 ($403,550 for married couples filing jointly)
  - 24% for taxable incomes over $105,700 ($211,400 for married couples filing jointly)
  - 22% for taxable incomes over $50,400 ($100,800 for married couples filing jointly)
  - 12% for taxable incomes over $12,400 ($24,800 for married couples filing jointly).
- The lowest rate is 10% for single individuals with taxable incomes of $12,400 or less ($24,800 for married couples filing jointly).

Standard Deduction

The standard deduction amount for 2025, as amended by OBBBA, is increased as follows:

- For married couples filing jointly – $31,500 (an increase of $1,500 from the pre-OBBBA amount);
- For single taxpayers and married individuals filing separately – $15,750 (an increase of $750);
- For heads of households – $23,625 (an increase of $1,125).

The standard deduction amounts for 2026 will be increased, as follows:

- For married couples filing jointly – $32,200 (an increase of $700 from the post-OBBBA prior year amount);
- For single taxpayers and married individuals filing separately – $16,100 (an increase of $350);
- For heads of households – $24,150 (an increase of $525).

The personal exemption for tax year 2026 remains at $0 and was made permanent by OBBBA.

For 2026, there is no limitation on itemized deductions. The limitation was made permanent by OBBBA. However, for taxpayers in the highest tax bracket (37%) a limitation is imposed on the tax benefit from itemized deductions.

Tax Provisions for International Assignees and Expatriates

- The maximum foreign earned income exclusion is increased to $132,900 for tax year 2026, up from $130,000 for tax year 2025.
  - ➢ Accordingly, the foreign housing base amount is increased to $21,264 for tax year 2026, while the maximum foreign housing expense amount is increased to $39,870 for tax year 2026.

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- An expatriate is a “covered expatriate” if the individual’s “average annual net income tax” for the five tax years ending before the expatriation date is more than $211,000 for tax year 2026, up from $206,000 for tax year 2025.

- The statutory exclusion amount for covered expatriates has been increased to $910,000 for tax year 2026, up from $890,000 for tax year 2025.

Estate and Gift Exclusions

- The OBBBA increases the lifetime exemption amount for transfers during 2026 to $15,000,000 (up from $13,990,000 for transfers in 2025).

- The annual exclusion amount for gifts remains at $19,000 for calendar year 2026.

- The first $194,000 of gifts made to a spouse who is not a citizen of the United States (other than gifts of future interests in property) are not included in the total amount of taxable gifts made during calendar year 2026 (up from $190,000 in 2025).

Medical and Health-Related Amounts

- The dollar limitation for employee salary reductions for contributions to health flexible spending arrangements (FSA) is $3,400 for tax year 2026 (up from $3,300). For cafeteria plans that permit the carryover of unused amounts, the maximum carryover amount is $680 for tax year 2026 (up from $660).

- Concerning medical savings accounts (MSAs), for tax year 2026, participants who have “self-only” coverage in an MSA, the plan must have an annual deductible that is not less than $2,900 (up from $2,850 in 2025), but not more than $4,400 (up from $4,300). The maximum out-of-pocket expense limit for “self-only” coverage is increased to $5,850 for tax year 2026 (up from $5,700).

- For participants with family coverage MSAs, for tax year 2026, the annual deductible must be not less than $5,850 (up from $5,700), but not more than $8,750 (up from $8,550). The maximum out-of-pocket expense limit for family coverage is increased to $10,700 for tax year 2026 (up from $10,500).

Other Items

- The **alternative minimum tax (AMT) exemption** amount is increased for tax year 2026 to $90,100 and begins to phase out at $500,000 for single filers. For married couples filing jointly, the AMT exemption amount will be $140,200 and the exemption begins to phase out at $1,000,000. For 2025, the AMT exemption amount was $88,100 and began to phase out at $626,350 ($137,000 for married couples filing jointly and began to phase out at $1,252,700).

- The maximum **earned income tax credit** amount for tax year 2026 is $8,231 (up from $8,046 for 2025) for qualifying taxpayers who have three or more qualifying children.

- The **qualified transportation fringe benefit** for tax year 2026 will have a monthly limitation of $340 for certain commuter transportation, transit passes, and qualified parking (up from $325 for 2025).

- The maximum **credit allowed for adoptions** is the amount of qualified adoption expenses up to $17,670 (up from $17,280 for 2025).

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Pension Limitations

- The contribution limit for employees who participate in 401(k), 403(b), governmental 457 plans, and the federal government's Thrift Savings Plan is increased to $24,500 (up from $23,500 in 2025). The catch-up contribution limit for employees aged 50 and over is increased to $8,000 for 2026 (up from $7,500 for 2025).
    - However, the higher catch-up contribution limit for employees who are aged 60, 61, 62, and 63 in 2026 remains at $11,250, instead of the $8,000 noted above, for 2026.
- The limit on annual contributions to an IRA is increased to $7,500 for 2026 (up from $7,000 for 2025). Likewise, the IRA catch-up contribution limit for individuals aged 50 and over is increased to $1,100 for 2026 (up from $1,000 for 2025).
- Taxpayers can make deductible contributions to traditional IRAs if they meet certain conditions. If during the year either the taxpayer or the taxpayer's spouse was covered by a retirement plan at work, the deduction may be phased out, depending on the taxpayer's filing status and adjusted gross income (AGI). (If neither the taxpayer nor the spouse is covered by a retirement plan at work, the phase-outs do not apply.)
- The phase-out ranges for 2026 for those covered by workplace retirement plans are as follows:
    - For single taxpayers, the phase-out range is increased to between $81,000 and $91,000 (up from between $79,000 and $89,000 (the ability to make deductible contributions being entirely phased out at the higher amount);
    - For married couples filing jointly, if the spouse making the IRA contribution is covered by a workplace retirement plan, the phase-out range is increased to between $129,000 and $149,000 (up from between $126,000 and $146,000);
    - For an IRA contributor who is not covered by a workplace retirement plan and is married to someone who is covered, the phase-out range is increased to between $242,000 and $252,000 (up from between $236,000 and $246,000);
    - For a married individual filing a separate return who is covered by a workplace retirement plan, the phase-out range is not subject to an annual cost-of-living adjustment and remains between $0 and $10,000.
- To make contributions to a Roth IRA, a taxpayer's AGI must not exceed a certain level. The phase-out ranges for Roth IRA contributions are:
    - For single and head of household taxpayers, between $153,000 and $168,000 (up from between $150,000 and $165,000) (the ability to contribute to a Roth IRA being entirely phased out at the higher amount);
    - For married couples filing jointly, $242,000 and $252,000 (up from between $236,000 and $246,000);
    - The phase-out range for a married individual filing a separate return who makes contributions to a Roth IRA is not subject to an annual cost-of-living adjustment and remains between $0 and $10,000.

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KPMG INSIGHTS

Inflation adjustments are largely routine. Nevertheless, these annual changes may have an impact on the operation of payrolls and shadow payrolls, as well as on taxpayers' ability to make pension contributions, and on the calculation of taxpayers' actual and hypothetical tax liabilities. In light of this, the changes should be communicated to relevant stakeholders as soon as possible, to help ensure that processes and software can be updated in a timely fashion. Pre-departure conversations with assignees should include mention of applicable tax rates, thresholds, exemptions, and allowances and the impact on the assignee.

Employers and employees concerned about the effect of the above-noted changes and how to budget for and otherwise plan the employee's assignment, should contact their qualified tax professional or a member of KPMG's Global Mobility Services practice in the United States.

FOOTNOTES:

1 See: IRS Information Release IR-2025-103 and IRS Rev. Proc. 2025-32. For coverage of last year's inflation adjustments, see *GMS Flash Alert* 2024-216, November 4, 2024.

2 One, Big, Beautiful Bill Act, Pub. L. No. 119-21, 139 Stat. 72 (OBBBA).

3 See: IRS Information Release IR-2025-111 and IRS Notice 2025-67.

4 See Social Security Administration press release, "Social Security Announces 2.8 Percent Benefit Increase for 2026."

5 See Social Security Administration Fact Sheet "2026 Social Security Changes."

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RELATED RESOURCE

For a related report, see "Rev. Proc. 2025-32: Inflation adjustments for 2026, individual taxpayers" in *TaxNewsFlash – United States* (October 9, 2025), a publication of KPMG LLP in the United States.

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