

2012 Virginia Legislators' Tax Guide



Virginia Society of
Certified Public
Accountants

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The VSCPA is here to help!

This guide is intended for use in preparing your 2011 income tax return. Legislators are employees of the Commonwealth of Virginia and are entitled to deduct, on their federal and Virginia income tax returns, certain business expenses that are ordinary and necessary in pursuit of the performance of their duties.

A question-and-answer format is used to provide specific answers to some frequently asked questions concerning income tax laws as they relate to your unique position as a member of the General Assembly. You also may find answers to specific questions not addressed here in Internal Revenue Service (IRS) Publication 463, Travel, Entertainment, Gift, and Car Expenses. The IRS website is www.irs.gov.

Throughout this guide, there is an important emphasis placed on recordkeeping. The burden of proving the appropriateness and extent of deductibility is on the taxpayer.

Therefore, it is imperative that the taxpayer keep sufficiently detailed records. Failure to adequately support a deduction will result in its disallowance.

This guide is not intended to cover all tax matters related to an individual's tax return. Relevant changes enacted by tax legislation during recent years have been considered. Items of personal nature, such as medical expenses, interest and charitable contributions, or tax matters unrelated to your position as an elected official are not covered.

The size of this guide limits the depth of the coverage of the topics addressed. In cases where the complexity of the subject matter is beyond the scope of this guide, you are encouraged to contact your CPA for additional assistance.

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Advertising

As a member of the General Assembly, I may place ads in trade journals, ad books or magazines published by various organizations in my district. I may also sponsor television or radio shows or events open to the general public. Can I deduct costs associated with these activities?

Generally, yes. These types of expenses are considered advertising expenses and are usually deductible. Generally, amounts paid or incurred for advertising are considered normal trade or business expenses. Because placing ads in trade journal, ad books or magazines to promote your name and maintain or improve relations with your constituency is a normal and necessary part of your business as an elected official, you are entitled to deduct these costs on your tax return. Be aware, however, of the timing of these ads. Ads placed during a reelection campaign period would usually be considered campaign expenses, and therefore, nondeductible.

Expenses to promote goodwill in the community would also be considered advertising expenses and therefore deductible. For example, a legislator may sponsor a television or radio show or an event attended by constituents. The costs associated with these events would be fully deductible. As an added bonus, any food and beverages distributed to the general public during an event to promote goodwill will be fully deductible and not subject to the usual 50 percent limit on meals and entertainment.

It is important that you maintain your invoices and proof of payment for advertising expenses to substantiate your deduction. It is also good practice to keep a copy of the advertisements in your files. For detailed guidance, see discussion in the section on [Recordkeeping](#).

Are my campaign expenses deductible for tax purposes?

Unfortunately, no. Even though holding public office is considered a trade or business under the Internal Revenue Code (IRC) § 7701(a)(26), another provision (IRC § 162(e)(1)(B)), provides that no deduction is allowed for any amount paid or incurred in connection with any political campaign on behalf of any candidate for public office.

The list of nondeductible campaign expenses is comprehensive and applies whether or not a candidate is elected. Included in the list are expenses for attending political conventions, contributions to the political party that sponsored a candidate's candidacy, campaign travel expenses, campaign advertising, expenses of defending a position in a contested election, filing fees or the cost of legal fees paid

in litigation over redistricting. In addition, campaign expenses may not be capitalized and amortized over the term of the office.

Furthermore, campaign expenses are still treated as nondeductible for those who could characterize them as expenses to promote an existing trade or business. For example, an attorney could not deduct campaign expenses on the theory that it promoted his professional legal practice.

Finally, even though a candidate may later institute a defamation suit for damage to his professional reputation for allegations made during a campaign, these litigation expenses are also considered nondeductible political campaign expenses.

Automobile & Travel Expenses

How do I report my automobile expenses on my tax return?

Because you are considered an employee of the Commonwealth of Virginia, all vehicle expenses are reported on Form 2106, Employee Business Expenses, Part II. Each section in this guide has a reference number that ties directly to Form 2106 to assist you in correctly reporting your automobile expenses as well as other unreimbursed business expenses. These expenses will be included on Schedule A, line 21, as unreimbursed employee expenses and are included with your other miscellaneous deductions. Expenses are deductible to the extent you're eligible to itemize total miscellaneous deductions. The expenses must exceed 2 percent of adjusted gross income to be deductible. See IRS § 162(h) election on page 8 for more information.

How much can I deduct for the auto mileage I incur traveling to and from Richmond?

The Commonwealth of Virginia reimburses each legislator for one weekly trip to and from Richmond while the legislature is in session. If the reimbursement you receive equals your expenses, there is no effect on your taxable income. However, this is rarely the case. Special party caucuses or special committee meetings may require additional trips for which you are not reimbursed. Such unreimbursed mileage expense is tax deductible as an employee business expense on Form 2106. In every case when the deductible mileage expense and the reimbursements are not equal, you should report all mileage, both reimbursed and unreimbursed, on Form 2106. The reimbursement received from your employer are reported on Form 2106, Part I, line 7 and are treated as an offset to your total expense. See IRS § 162(h) election for more information.

What other automobile mileage expenses can I deduct?

Members of the General Assembly incur a great deal of mileage expense while in their home district. All travel to mass meetings, and to meetings where you will speak or which you believe are important to attend because of your political position, are tax deductible. You should maintain a mileage log and record all business miles driven and for what purpose. This mileage can become substantial, particularly for those members who are responsible for large districts. The legislator may be required to travel from one town to another to attend civic functions, political functions or other meetings related to legislative duties. Include this expense in Part II of Form 2106.

Can I deduct mileage expenses incurred while going to meetings during a political campaign for my re-election? I feel it is incumbent on me as a state legislator to attend these meetings to explain to my constituents the activities of the General Assembly, the legislation on which we are working, the disposition and explanation of legislation that has gone through committees, and legislation on which we have already acted.

The Internal Revenue Code specifically states that all campaign expenses are not tax deductible (See section on campaign expenses). Because of this, it is very important for the legislator to distinguish between those expenses that are directly related to a campaign for re-election and those that are attributable to serving the constituency. Whether the expense is an election expense or business expense depends on the facts and circumstances. To avoid any conflict with the IRS, you might set up a time period to distinguish between campaign expenses and business expenses. For example, you might separate your campaign and business expenses by determining that campaign expenses include all expenses incurred during the month before the date of the nominating convention, primary election or general election. Record all expenses incurred during this time as nondeductible campaign expenses. Business expenses would include expenses incurred prior to this one-month period.

If I use another mode of transportation to get to Richmond, such as a train or plane, can I deduct these expenses?

If you use a train, airplane or other means of transportation for an overnight stay in Richmond, these expenses should be detailed on Form 2106, Part I, line 3. Report the reimbursement you received for travel that were not reported to you in box 1 of Form W-2 on Part 1, line 7 of Form 2106.

The expense incurred in excess of reimbursement will be deductible. However, any mileage reimbursement in excess of such travel expense will be taxable income to you. You cannot claim both the mileage you would have incurred had you driven to Richmond and the cost of the train fare or airline ticket.

Do I still claim a tax deduction for the mileage for that particular day, even though I did not drive my own car?

No. In addition, if you do receive reimbursement for this mileage, the reimbursement amount is taxable income.

How do I report a reimbursement?

On Part I, line 7 of Form 2106, you should report any amounts you received that were not reported to you in Box 1 on your Form W-2. This could include amounts that didn't appear on your Form W-2 at all, or amounts that appear under code "L" in Box 12 on Form W-2.

While away from home, staying in Richmond for the legislative session, I am required to drive to the state capitol each day. Can I deduct this mileage as a business expense?

Yes. Although commuting miles are not considered business miles, if Richmond is not your "tax home," mileage between your temporary quarters and the State Capitol is deductible and is not considered commuting. See IRS § 162(h) election for more information.

Is a fine a tax-deductible expense?

No. A traffic violation fine is a penalty and is not a deductible expense.

Can I deduct mileage expense from my home to my office?

No. The mileage from your residence to place of business is a nondeductible commuting expense.

If the Commonwealth of Virginia reimburses me a lesser amount than the IRS standard mileage rate, can I deduct the difference on my income tax return?

Yes. Show your total business mileage expense on Form 2106, Part II, Section B, titled "Standard Mileage Rate." The reimbursement is reported on Form 2106, Part I, line 7. The difference will result in an additional deduction.

The IRS allows me to deduct the standard mileage rate or to itemize all of my actual automobile expenses and then to take a portion of those expenses based on the percentage that my business miles are to the total miles traveled during the year. Which method results in the greatest deduction for me?

The IRS suggests if you have the option of using either the standard mileage rate or actual expense method, you should figure your expenses both ways to find the method most beneficial to you. But when completing Form 2106, fill in only the sections that apply to the method you choose.

What if I am leasing my automobile?

A taxpayer who leases an automobile in connection with his or her trade or business may deduct the portion of the lease payments that are allocable to the business use of the automobile. In addition, operating expenses actually paid by a lessee-taxpayer may be deducted to the extent they are allocable to business use. Any advance payments made in leasing the automobile must be spread over the entire lease period. Payments made to purchase a car, even though denominated as lease payments, are not deductible. The taxpayer may have to include in income an inclusion amount based on the lease payment. Consult your CPA. The deduction depends on the actual facts and circumstances.

What is the "Standard Mileage Rate?"

For 2011, the standard mileage rate is 51 cents per mile for all miles of use for business purposes from Jan. 1 through June 30 and 55.5 cents per mile from July 1 through Dec. 31.

If I use actual expenses one year, can I use the standard mileage rate the following year?

The IRS allows two methods for computing vehicle expenses — the standard mileage rate and the actual expense method. The standard mileage rate can only be used if: you owned the vehicle and used the standard mileage rate for the first year you placed the vehicle in service; or you leased the vehicle and are using the standard mileage rate for the entire lease period. Once you have used actual expenses, you must continue to use the actual expense for the remaining life of the vehicle.

If I use actual expenses, specifically what expenses am I allowed to deduct?

In addition to gasoline, oil and lubrication, you may include the cost of repairs, tires, supplies, insurance, taxes, tags and licenses. The single largest item usually is depreciation, which also may be called “cost recovery” or “deduction under MACRS or ACRS” in IRS instructions.

What about the interest expense on my automobile?

Interest, even though incurred with respect to a vehicle used by you as an employee of the Commonwealth, is considered a personal expense and is not deductible.

If I use the standard mileage rate, are there additional expenses I can deduct for the use of my automobile?

Yes. Parking fees, tolls and local transportation are reported on Part I, line 2, of Form 2106. Personal property taxes on the automobile are deductible as an itemized deduction on Schedule A, line 7, for the standard mileage rate or actual expenses. These taxes should be reported net of any “car tax” refund received in 2011.

Since I receive reimbursement from the Commonwealth for mileage allowance once a week to Richmond during the session, plus mileage reimbursement for special legislative committee meetings and other special committee assignments, would it be best to just disregard the reimbursement entirely, assume it is completely offset by mileage expenses and, therefore, not report anything?

If business mileage records are maintained and you are fully reimbursed at the IRS rates for actual mileage driven, it is not necessary to report anything in your federal income tax return. However, if you are reimbursed for mileage not driven (for example, when you share a ride or if you do not attend a weekly session), then you have an excess reimbursement that must be reported as taxable income. If an employee incurs business expenses for which he or she is partially reimbursed, the employee must report all reimbursements and related expenses in order to be permitted to deduct the unreimbursed portion of his or her business expenses.

Campaign Expenses

Are my campaign expenses deductible for tax purposes?

A candidate’s campaign expenditures out of his or her own resources are not deductible as ordinary business expenses for income tax purposes. Even though a public office is defined as a trade or business (IRC § 7701(a)(26)), none of a candidate’s campaign expenses are deductible.

Regardless of the result of the election, a candidate cannot deduct expenses for attending political conventions, contributions to the political party which sponsored his or her candidacy, campaign travel expenses, his or her own campaign advertising, the expenses of successfully defending a position in a contested election, filing fees, or the cost of legal fees paid in litigation over redistricting. Nor may these expenses be amortized, as capital expenditures, over the term of the office.

Even though a political office might be viewed as a stepping stone to some other business or profession, this is not enough to change the result. Thus, political campaign expenses are not deductible by a lawyer seeking election as a legislator in the hope that the exposure will build his or her professional practice.

Even though a candidate felt that his or her professional reputation was damaged during a political campaign, the candidate cannot deduct the cost of any defamation litigation for allegations published during the campaign. In 1962 Congress enacted IRS § 162(e)(2)(A) of the Internal Revenue Code, which disallows all deductions for expenditures in any political campaign for a candidate for public office. Additional details may be obtained from the Campaign Treasurer’s Handbook available from the American Institute of CPAs or your local CPA.

Capital Gains & Losses

Gain or loss is generally realized when property is sold or exchanged. A gain results when the property is sold or exchanged for more than the adjusted basis of the property. A loss is realized when the property is sold or exchanged for less than the adjusted basis of the property.

Gains and losses are classified as either ordinary or capital. Capital gains and losses are then classified as either short-term or long-term. Almost everything you own and use for personal purposes or investment is considered a capital asset. A non-capital asset is property that is not a

capital asset (e.g. property used in your trade or business or as rental property).

Long-term and short-term capital gains and losses are offset against one another to produce net capital gain or loss. Long-term holding period is more than one year and short-term is one year or less. For individual taxpayers, long-term gain may qualify as adjusted net capital gain eligible for maximum tax rate of 15 percent, or 0 percent to the extent taxpayer's taxable income is taxed at a rate below 25 percent.

Some long-term real estate gain qualifies for 25 percent maximum rate and some other types of long-term gain, such as from collectibles, are subject to 28 percent maximum rate. Individual taxpayers may deduct up to \$3,000 annually of excess capital losses from ordinary income, and capital losses in excess of \$3,000 limit may be carried forward indefinitely.

Sale of Your Home

If you sold or exchanged your main home, do not report it on your tax return unless your gain exceeds your exclusion amount or you received a 1099-S form. Consult your CPA. Generally, if you meet the two tests below, you can exclude up to \$250,000 of gain. If both you and your spouse meet these tests and you file a joint return, you can exclude up to \$500,000 of gain (but only one spouse needs to meet the ownership requirements in Test 1).

Note: Along with this section, you should review the office expenses section of this guide. A taxpayer may not use the principal residence exclusion for any gain related to the depreciation expense claimed for a home office.

Test 1: You owned and used the home as your main home for two years or more during the five-year period ending on the date you sold or exchanged your home. If the home was acquired through a 1031 exchange, then it must be the principal residence for a minimum of five years.

Test 2: You have not sold or exchanged another main home during the two-year period ending on the date of the sale or exchange of your home. See Publication 523, *Selling Your Home*, for details, including how to report any taxable gain on Schedule D, if:

- You do not meet one of the above two tests;
- You (or your spouse, if married) used any part of the home for business or rental purposes after May 6, 1997, or;
- Your gain exceeds your exclusion amount.

Entertainment & Meal Expenses at Home

I am required to meet with a constituent regarding a state problem and I meet him for breakfast, lunch or dinner and pay for his meal. Can I deduct this as a tax expense?

Yes. Remember to keep up your expense diary as to who, why, where, when and how much. Also, remember that only 50 percent of the cost is deductible.

Because of my position in the community, I occasionally entertain other elected officials such as mayors or members of city council, primarily for the purpose of maintaining communications, exploring each other's problems and determining common solutions. Can I deduct this expense?

Yes, as long as it is related to your legislative position and you can show the business purpose for the entertainment or meeting. Here again, it is necessary to keep an itemized record to indicate the date, place, who was there and the purpose of the meeting. Once more, only 50 percent of the entertainment expense is deductible.

The following summarizes the rules and definitions pertaining to the deduction for business related entertainment expenses.

General rule

You can deduct ordinary and necessary expenses to entertain a client, customer, or employee if the expenses meet the directly-related test or the associated test.

Definitions

- Entertainment includes any activity generally considered to provide entertainment, amusement, or recreation, and includes meals provided to a customer or client.
- An ordinary expense is one that is common and accepted in your trade or business.
- A necessary expense is one that is helpful and appropriate.

Tests to be met

Directly-related test

- Entertainment took place in a clear business setting, or
- Main purpose of entertainment was the active conduct of business, and
 - You did engage in business with the person during the entertainment period,
 - You had more than a general expectation of getting income or some other specific business benefit.

Associated test

- Entertainment is associated with your trade or business, and
- Entertainment directly before or after a substantial business discussion.

Other rules

- You cannot deduct the cost of your meal as an entertainment expense if you are claiming the meal as a travel expense.
- You cannot deduct expenses that are lavish or extravagant under the circumstances
- You generally can deduct only 50 percent of your unreimbursed entertainment expenses.

IRS § 162(h) Election

The tax code provides for a simplified method of accounting for travel expenses for electing state legislators. If a state legislator lives more than 50 miles from his or her state capital, he or she can elect IRS §162(h), which provides a formula for determining the amount of deductible travel expenses the legislator can claim as unreimbursed business expenses on [Form 2106 \(PDF\)](#). Instructions for the form can be found by [clicking here \(PDF\)](#). The deduction is based on the total legislative days during the year multiplied by the federal per diem rate.

Election

The election is made by attaching the form on the next page to the taxpayer's return. The election can even be made for a prior tax period by filing an amended return, recalculating expenses according to the form and attaching the statement to the amended return. Remember, if you make this election you cannot claim a deduction for automobile expenses or any other kind of travel expenses.

Legislative Days (Section I)

The election is available for any day that the legislator is in session or in a committee meeting. Note, also, that if the legislator was not actually in session, but the session break was four consecutive days or less, the interim days are counted as session dates. For example, the legislature has a break of three days, Friday, Saturday and Sunday, but the legislator attended the session on Thursday and Monday. Even though the legislator was not actually in session for the extended weekend, because the break is less than four consecutive days, those days count as session days.

Per Diem Rates (Section II)

The potential deduction is based on the number of legislative days times the federal per diem rate. The federal per

diem rates have been included on the election statement for your calculation. You can access the appropriate IRS form by [clicking here](#).

Reimbursed Expenses (Section III)

If you have been reimbursed for any of your travel expenses, include the total of those reimbursements on line 7 of Form 2106. Reimbursement of lodging should go in column A. Reimbursement of meals should go in column B. If you were reimbursed for a certain number of days based on the federal per diem rates, use the calculation on the election form.

Living Expenses

Legislators receive a per diem allowance equal to the allowable 2011 federal per diem for lodging, meals and incidental expenses applicable to Richmond for each day the General Assembly is in session. The receipt of this amount is not affected by whether the delegate maintains temporary living quarters in Richmond. The per diem is not included in your W-2.

The per diem reimbursement is an "accountable plan" for those delegates who are considered away from home on business because you are required to substantiate all of your expenses. What constitutes being "away from home on business" has been and still is a difficult issue. (See discussion of "tax home" in the section for ordinary business expenses.)

If your actual expenses exceed this per diem allowance, you can claim the excess by reporting the total actual expenses and the total reimbursement on Form 2106. However you must maintain adequate records of the details of your expenses. In addition, the expenses in excess of reimbursements are subject to a limitation and are only deductible to the extent the total exceeds 2 percent of adjusted gross income.

Because many of the substantiation rules require evidence of your business schedule, it is wise to maintain a calendar or diary of your schedule and events related to legislative duties as part of your tax records.

The IRS updates the per diem amounts at least annually.

What expenses can I deduct for living in a hotel or apartment while attending sessions in Richmond?

For hotels, motels and similar commercial places for residing while in Richmond and away from your normal residence (your "tax home"), you are allowed to deduct the actual amount paid for the room (including any taxes

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Internal Revenue Code (IRC) § 162(h) Election

I elect, under the above referenced section, to designate my residence within my legislative district as my tax home for tax year _____. Accordingly, I elect to claim legislative expenses under IRC § 162(h).

Legislator's name: _____

Social Security Number: _____

Address within district: _____

Mileage between home in legislative district and State Capitol Building: _____

Section I: Legislative days Jan. 1, 2011, to Dec. 31, 2011

Committee days: _____

Session days: _____

Special session days: _____

Total legislation days: _____

Section II: Deductions for legislative days

| | Lodging | Meals | Total |
|------------------------------------|---------|-------|-------|
| (1) Standard federal per diem rate | \$114 | \$66 | \$180 |
| (2) Total days from Section I | | | |
| (3) Deductions (1) x (2) | | | |
| | (a) | (b) | |

Enter amount (a) on Form 2106, Part 1, line 3, column A. Enter amount (b) on line 5, column B.

Section III: Reimbursement of expenses

[Complete only if subsistence payments (\$180/day) have not been included in box 1 of your Form W-2.]

| | Lodging | Meals | Total |
|------------------------------------|---------|-------|-------|
| (1) Standard federal per diem rate | \$114 | \$66 | \$180 |
| (2) Total days from Section I | | | |
| (3) Reimbursements (1) x (2) | | | |
| | (a) | (b) | |

Enter amount (a) on Form 2106, Part 1, line 7, column A. Enter amount (b) on line 7, column B.

or service charges). If a hotel or motel room is shared with other legislators, each may claim the share of the expense he or she paid.

If you have a fixed monthly rate that you are paying the motel or hotel, that amount would be allowed as a deduction as long as it is paid by you and as long as it is for the purpose of providing a place to stay while you are away from home on business. If you live in an apartment or share an apartment with another person, you are allowed

to claim the actual amount that you pay for your share of the rent, utilities, telephone bills and any furniture you may be required to rent to furnish the apartment.

In each case, whether you stay in a hotel, motel or apartment, you should keep the receipts so these can be provided to the IRS upon request. It would be desirable for each member of a group living in a hotel or apartment to have copies of the paid vouchers and an annual summary of the total costs of the apartment or hotel that shows the manner in which costs were divided among the various persons.

Where do I report the per diem paid to me?

If your business expenses exceed the amount reimbursed by the state, use Form 2106 to report all business expenses, both reimbursed and unreimbursed. Then include all reimbursements including the per diem received on Form 2106, Part I, line 7.

While in Richmond, may I deduct the cost of meals?

Yes, but the deduction is limited to 50 percent of the cost of the meal. Actual out-of-pocket expense that you incur and pay may be deducted if you are away from home overnight. The requirement again necessitates keeping a record to show the amount that you personally paid for breakfast, lunch, dinner and/or any other meal expense you incur while you are in Richmond.

If a registered lobbyist or friend pays for your meal, this is not a deduction to you since you have not paid for the meal. Similarly, when you are attending dinners in Richmond held by various associations, the Chamber of Commerce, etc., you are not allowed the deduction for this meal.

If you are living in quarters that provide cooking facilities, the cost of groceries and necessary beverages is an allowable, deductible expense, subject to the 50 percent limitation. Receipts are required to be kept for certain expenses.

It is suggested that you keep as many receipts as possible, as well as all cancelled checks, to support your business expenses.

Again, these expenses are only deductible to the extent the expense is not reimbursed.

May I deduct a standard per diem amount for meals instead of substantiating actual cost?

A standard per diem for meals and incidental expenses is included in the per diem you receive from the state. If you choose to consider this per diem as the reimbursement for all business meal costs that you incur, you report neither the expense nor the reimbursement.

When I am in Richmond, can I deduct a per diem allowance that would include both meals and lodging in lieu of keeping track of actual expenses?

A state legislator would normally not be able to deduct expenses for travel away from home during the legislative session because the state capital would be considered his or her principal place of business. However, for purposes of determining whether a travel expense is incurred away from home, a state legislator may elect to have his or her residence in his or her legislative home district treated as his or her tax home. If the election is made, a state legislator is deemed to be away from home in the pursuit of a trade or business on any day that the legislature is in session (including periods of up to four consecutive days when the legislature is not in session) or on any day when the legislature is not in session but the legislator's presence is formally recorded at a committee meeting. The legislator's place of residence within the represented legislative district is deemed to be the legislator's tax home. Legislators whose place of residence is 50 miles or less from the state capital may not elect to have these rules apply. There is no requirement that the taxpayer be a legislator for the entire tax year.

For each day that a state legislator is deemed to be away from home, the amount deemed expended on living expenses is determined under one of two standards, and whichever results in the larger deduction is applied. Under one standard, the amount deemed expended per day will equal the generally allowable per diem allowance available to employees of the executive branch of the federal government for such day while away from home but within the U.S. The second standard provides that the amount deemed expended will equal the amount generally allowable to

employees of the state in which the legislator sits as a per diem allowance by the state while employees are away from home, to the extent that the amount does not exceed 110 percent of the amount computed under the first standard. The unreimbursed expenses of a state legislator are deductible as a miscellaneous itemized deduction, subject to the 2 percent floor. Additionally, the 50 percent limitation on the deduction of meal expenses must be taken into account before the 2 percent floor is applied. Because the expense amount a legislator is allowed to deduct under IRS § 162(h) is determined by reference to a per diem allowance, an allocation must be made between meals and lodging so that the 50 percent limitation on the deduction of meal expenses can be applied. The allocation is made on the basis of the ratio of the amounts allowed for meals and lodging that are found in the Federal per diem amount applicable to the legislator's state capital at the end of the legislator's tax year. The amount allowable for meals is the amount allowed for meal and incidental expenses reduced by \$2 per legislative day (or any other amount allocated to incidental expenses under the Federal Travel Regulations). If the legislator is reimbursed by the state in an amount less than that allowed under IRS § 162(h), the reimbursed amount is deductible from gross income in computing adjusted gross income (above-the-line deduction). The excess is deductible under the rules that require the special allocation.

If I choose to claim per diem amounts as described in the prior question, how do I elect it?

The election to claim the IRS § 162(h) deduction must be made by the due date (taking into account extensions) of the tax return for the tax year at issue. The election is made by attaching a statement to the return that:

1. Contains the taxpayer's name, address and TIN;
2. Identifies the election;
3. Indicates that the election is being made under IRS § 162(h);
4. Specifies the period for which the election is being made; and
5. Contains any information required by the Internal Revenue Code or necessary to show that the taxpayer is entitled to make the election.

If I choose to claim the per diem amount, can I deduct any other expenses?

You may not deduct any other amount for meals, lodging or other living expenses for any legislative day, but you may deduct expenses for travel, telephone calls or local transportation.

Can I deduct the expense of meals I have purchased for constituents who have come to Richmond and other persons where it involved legislative business?

Yes. Subject to the 50 percent limitation, the cost of meals paid for by you is an allowable deduction as long as that expense is related to legislative business. You must keep the receipt and record the name of those who attended the meal, the date, location and some specific information to show the business nature of the meal.

Because we are in Richmond for long periods of time, I find it necessary and desirable to have my spouse and children come to Richmond on occasion. Can I deduct the cost of their travel to Richmond and motel and meal costs?

No deduction is allowed for travel expenses paid or incurred for a spouse, dependent or other individual accompanying a person on a business trip unless the spouse, dependent or other individual is an employee of the person paying or reimbursing the expenses, the travel is for a bona fide business purpose and the expenses would otherwise be deductible. This same rule applies if your spouse accompanies you on a trip for a legislative conference.

While in Richmond on certain special occasions such as Lee-Jackson-King Day, I will have a gathering of fellow legislators and other individuals connected with the legislature. Can I deduct this as a business expense?

If the gathering can be shown to have a business purpose, it would qualify as a business deduction. You should have paid receipts for support and indicate the business purpose and who attended the function. Again, however, any food or beverage expenses would be subject to the 50 percent limitation.

If these occasions include business and non-business individuals, you must divide the expenses between your business and non-business elements. You can deduct only the business part, not the non-business part. For example, if you have 100 individuals at the event and 10 are non-business, you can only deduct 90 percent of the total cost.

At the end of a session, if fellow legislators and I take the secretaries who work long hours during the year out to dinner, or if we buy them candy, would this be a deductible expense?

Fifty percent of the dinner expense would normally be deductible if the secretaries were employees of the legislators.

Since the secretaries are employees of the state, there is a non-employee-employer relationship. To be deductible in the non-employee-employer relationship, the expense must be directly related to the active conduct of the taxpayer's trade or business. IRS regulations state that to satisfy this requirement the taxpayer must have "more than a general expectation of deriving some income or other specific trade or business benefit (other than the goodwill of the persons entertained) at some indefinite future time from the making of the expenditure."

In addition, there is a limit of \$25 per recipient per year in the case of business gifts.

While in Richmond, I entertain at the Downtown Club. In order to use the Club, I must pay dues as well as the costs. Can I deduct the cost of these dues?

No. Dues paid to these types of clubs are nondeductible.

Office Expenses

See *IRS Publication 587, Business Use of Home*, for more details.

What are the rules regarding claiming a home office deduction and what expenses can I claim?

The hurdles have been set relatively high in order to qualify to deduct expenses for the business use of your home. Since state legislators are employees of the state, the home office must not only be used as a principal place of business, but it must be used for the convenience of the employer (not the employee.) This term is generally subject to interpretation and there is little case history related to it. It would therefore be advisable to get a letter from your employer stating that you maintain a home office for their benefit. If these hurdles can be overcome, the legislator can deduct a portion of his or her utilities, home insurance, repairs and maintenance and depreciation related to the portion of the home used exclusively as an office. The appropriate percentage is calculated as the square footage of the space used exclusively for business compared to the entire livable square footage of the home. Unfortunately, these expenses are again limited by the net income (wages less other deductible business expenses) derived from your position as a legislator. You must complete Form 8829, Expenses for Business Use of Your Home to calculate the amount of allowable expenses for business use of your home. This calculation is rather lengthy and complicated and should be figured with the help of a tax advisor. The result of this calculation will be included on line 4 of Form 2106.

What if I maintain a separate office in my jurisdiction? What expenses can I claim for that office?

If you maintain a separate office in your local jurisdiction, expenses related to that office are included on line 4 of Form 2106. Deductible expenses include rent, utilities, insurance, maintenance and real estate taxes. In addition, if you own any fixed assets such as office furniture or computers, the depreciation on those assets can be calculated on Form 4562 and included on Form 2106.

What if I am reimbursed for my home office or outside office expenses?

Any expenses for which you are reimbursed cannot be claimed as a deduction. If, however, you are reimbursed for your expenses and the reimbursement is included in your W-2 income, then you can continue to claim expenses as noted above.

Can I deduct any costs of my home as a business expense?

For tax years beginning after 1998, a home office qualifies as the "principal place of business" when:

1. The office is used by the taxpayer to conduct administrative or management activities of a trade or business of the taxpayer, and
2. There is no other fixed location for the business to conduct its administrative or management activities. This allows you to deduct travel between a home office and other places for business purposes.

Any deduction which meets these two tests is limited to the net business income generated at this location. Any expenses disallowed because of this net income limitation can be carried over to future years and deducted subject to the same net income limitation.

Employees may deduct home office expenses only if the exclusive business use is "for the convenience of his employer." This phrase is not really definitively explained in statute. But the question of whether something is for the convenience of the employer generally is determined by all facts and circumstances in each case.

If you maintain an office in Richmond throughout the year, you may not be able to benefit from this provision. Because this is a complicated area and individual situations will vary, you should consult with your CPA.

Specifically, what can I deduct as a home office expense?

If the tests described in the previous answer can be met,

and to the extent a separate section of the home or apartment is used for your legislator's duties only and there is no private use whatsoever of that portion, you may deduct the following items:

Types of Expenses

Home operation expenses are distinguished by three categories and depend on the percentage of your home used for business. The table below describes the method to use for each category.

1. **Cost recovery or rent:** Cost recovery is computed by taking the cost (or fair market value if less) of your home, after deducting the land cost, over a cost recovery period. Compute the percentage of space in your home used exclusively for business purposes to the total space in your home. This percentage is applied to the total annual cost recovery and the resulting portion may be deducted on your tax return. If you are renting, the business portion (percentage) of your residence is applied to your annual

rent to determine the deduction.

2. **Other expenses:** Utilities and insurance related to maintaining an office in your home may be apportioned based on the percentage of the space of your home or apartment that is exclusively used as an office. Also, any maintenance expenses to keep up this particular room or area may be deducted as a business expense for that particular year. Examples of such items would be cleaning and painting. Carpentry work to install cases or carpeting or similar improvements in this particular room would be a capital expense and may be deducted over a cost recovery period.
3. **Office equipment/furniture:** In your home office, the cost of office equipment and furniture such as a desk, file cabinet, adding machine and similar items may be recovered over a cost recovery period and the business portion of this recovery may be deducted.

| Expense | Description | Deductibility |
|--|--|--|
| Direct (painting or repairs, office equipment) | Expenses only for the business part of your home | Full |
| Indirect (mortgage interest, real estate taxes, depreciation, security system, general repairs, landscaping, utilities, insurance) | Expenses for running your entire home | Based on the percentage of your home used for business |
| Unrelated | Expenses only for the parts of your home not used for business | Not deductible |

Is it advisable to try to alter my use of the home to qualify for the office at home deduction?

In some cases it is not advisable to deduct these types of expenses. You should consult your CPA as to whether the deduction is advisable in your situation.

How do I handle salaries?

Salary or wages constitute another deductible expense you may incur. If you hire someone to assist you in legislative matters and to handle constituent contacts, such as a full- or part-time secretary, the compensation paid is deductible. If an individual is on your payroll, you must obtain a federal identification number and pay the proper payroll taxes (the employer's portion is also deductible). For details on the proper accounting and tax reporting of payrolls, contact your CPA for advice.

If you have student or volunteer help in working on local legislative matters, and no out-of-pocket expense is incurred by you, then there is no tax deduction.

What happens if I sell my personal residence that I have been depreciating and taking the expense for office use of home?

If you were entitled to take depreciation deductions because you used your home for business purposes, you cannot exclude the part of your gain equal to any depreciation allowed or allowable as a deduction for periods after May 6, 1997.

Therefore, if you sell your personal residence that you used for business, you may be taxed on the gain attributable to the depreciation taken. Consult your CPA.

An example follows:

Legislator A sells his or her main residence at a \$50,000 gain. The legislator meets the use and ownership tests to exclude his or her gain from income tax. However, a portion of the home was used for business from 1998 to 2002. The amount taken for depreciation was \$2,000. The legislator can exclude \$48,000 (\$50,000 minus the depreciation of \$2,000) and the legislator is taxed on the recapture of depreciation of \$2,000.

If I have a legislative assistant in my home district, but pay him or her a token amount each month, am I required to go through the process of filing payroll tax returns and withholding payroll taxes?

In most situations, all amounts paid for services are subject to the payroll tax laws. In addition, the worker's compensation rules may apply. However, there are some exceptions (such as in the case of an independent contractor). The status of employee or independent contractor is a complex issue. You should consult your CPA to evaluate each situation.

Instead of (or in addition to) an office in my home, I maintain a rented office in my district for the purpose of serving my constituency. What expenses can I deduct on my tax return for the cost of maintaining this office?

We understand all legislators receive a monthly reimbursement for office expenses amounting to \$500 currently for most legislators. This amount has been reported on your Form W-2 as income. This allowance does not meet the requirements of an accountable plan because the expense details are not reported to the employer and any amount in excess of substantiated expenses is not required to be returned.

If your office is being used exclusively for legislative purposes, all expenses related to this office — rent, utilities, cost recovery on improvement and equipment, etc. — are deductible as a miscellaneous itemized deduction. You must, however, be careful if the same office is used strictly for political purposes during campaigns (and possibly some office expenses are paid out of campaign contributions). To that extent you would have to exclude those expenses from your own tax return, since you personally have not incurred any out-of-pocket expenses.

If campaign contributions for maintaining the office exceed the cost of operating the office, then you incur taxable income. Detailed records should always be maintained, and

in this case you should keep a detailed record of all receipts used from sources other than yourself, including the monthly allowance, to determine whether or not your expenses exceeded your income or vice versa.

If expenses exceed funds from these other sources, and such expenses are in fact campaign expenses, then these specific expenses are not deductible. (See questions and answers under section on campaign expenses.)

If I were reimbursed for my expenses (office rent, telephone, postage, staff, etc.) under an accountable plan, and this amount was not reported on my Form W-2, how do I report this reimbursement?

If you report details of the expenses to the Commonwealth of Virginia (your employer), and you are required to return any amount in excess of the substantiated expenses, then the amount received from your employer is excluded from gross income, is not reported on Form W-2, and is not subject to income tax withholding or other employment taxes. (See introduction.)

Ordinary Business Expenses

As noted previously, legislators are employees of the Commonwealth of Virginia. Generally, expenses which are ordinary and necessary to the performance of the legislator's duties are deductible on their federal income tax return.

Where to Deduct

The appropriate form for detailing deductible business expenses is *Form 2106 — Employee Business Expenses*. This form is subject to revision from time to time by the IRS. In the past, some legislators may have attempted "above the line" deductions of their expenses. Chief Counsel Advice 199939001 and the instructions to form 2106 state that this is not proper, and Form 2106 should be used. Since legislators are employees, business expenses must be deducted on Form 2106.

Where appropriate, each section of this guide has a reference to a line number on Form 2106 to help you understand the questions and answers contained in this guide and to assist you in properly reporting your tax deductible information on your federal income tax return.

"Tax Home"

"Home" as used by the IRS is not necessarily synonymous with domicile or residence. A taxpayer's "tax home" has to be determined in light of all facts and circumstances relative to a particular taxpayer. The determination of what is allow-

able for traveling expenses depends on what is considered a taxpayer's tax home.

If, for example, your duties as a legislator were your main source of income, Richmond, being your principal place of employment, would probably be your "tax home" for IRS purposes. Your living expenses while at home in Richmond would be nondeductible. State legislators who normally reside in the Richmond area cannot deduct their commuting expenses.

Generally, the answers in this guide assume that Richmond is not the legislator's tax home. Thus, the answers will not apply to legislators who normally reside and work in the general vicinity of Richmond, including those whose "tax home" is Richmond.

A state legislator can elect under IRS § 162(h) to use his or her legislative district as a "tax home." A legislator making the election is treated as having spent an amount equal to the greater of the state per diem or the federal per diem while in the state capitol. If the state per diem is greater than the federal per diem, it cannot exceed it by more than 10 percent. When a legislator's tax home is farther than 50 miles from the state capitol building, the legislator is deemed away from home on legislative business on each legislative day and on each day he attends committee meetings where his or her presence is formally recorded.

You may wish to consult your CPA or tax adviser who can assess your situation and advise you as to the treatment of these expenses in your particular case.

Other Expenses

What other expenses can I deduct on my tax return?

There are many other expenses you might incur as a result of your position as a member of the General Assembly. Generally, these expenses are also reported on Form 2106 and are subject to the 2 percent floor. These include:

- Stationery and postage relating to mail concerning your business as a member of the General Assembly
- Any other supplies such as pens, paper clips, etc., that are necessary to maintain your office and serve your constituency
- Dues to organizations to which you normally would not have belonged prior to being a member of the General Assembly, but to which you now belong as a matter of policy and since it is instrumental to your being a state

legislator (examples include dues to organizations in your community and political groups); dues to organizations of which you normally are a member may be partially deductible to the extent you can show a business use and purpose (however, club dues are no longer deductible)

- Newspapers and magazines — the costs of obtaining additional publications because of your position as a state legislator and because they are necessary for you to improve yourself as a legislator are deductible; such publications would include special weekly papers in your district and publications relating to politics, the state or related areas of government
- The cost of holiday cards to precinct committee members and leaders in the community is a form of advertising expense, again directly related to your business as a member of the General Assembly; to the extent that you buy holiday cards and mail them to people related to you in politics, this becomes a tax-deductible expense (cost of the cards, envelopes, postage and photographs if your family photograph is included in the card)
- The cost of newsletters sent to constituents
- Computer and printing supplies, software applications, and other peripherals utilized primarily in the course of your duties as a member of the General Assembly

Personal Financial Planning

You may qualify to make either a deductible or non-deductible contribution to an IRA. Both you and your spouse (working or non-working) may each contribute the lesser of (1) 100 percent of your individual compensation includible in gross income for the year, or (2) \$5,000 to your IRA.

Individuals age 50 and over can make an additional \$1,000 annual catch-up contribution.

Features of regular deductible IRAs include:

- The deductible IRA contribution limit for a Single Active Participant in a Qualified Plan is phased out between \$56,000 and \$66,000 of Modified Adjusted Gross Income (MAGI) in 2011. The deductible IRA contribution MAGI limit for Married Filing Jointly Active Participants is \$90,000 and \$110,000 in 2011. The 2011 deductible IRA contribution MAGI for an individual filing a "Married Filing Separately" return will be phased out if your MAGI is more than \$10,000.
- Each spouse's deduction is calculated separately if only one is covered by a pension plan; however the deduction for the non-covered spouse is phased out as the joint modified adjusted gross income between \$1697,000 and \$179,000.

The Roth IRA is another type of IRA. Basically, contributions are non-deductible going in and distributions are non-taxable coming out. In other words, it is a “back-ended” IRA. Other general features of the Roth IRA are:

- Contributions are limited to lesser of (1) 100 percent of your individual compensation includible in gross income for the year, or (2) \$5,000 per year less amounts contributed to other IRAs. (\$6,000 if age 50 or older) .
- Contributions can be made even after age 70 ½ if there is earned income.
- No minimum distributions are required upon turning age 70 ½.
- AGI limits are \$169,000 to \$179,000 (married filing jointly), \$0 to \$10,000 (married filing separately) and \$107,000 to \$122,000 (single and head of household).
- The above ranges apply regardless of whether the taxpayer is an active participant in an employer-sponsored retirement plan.
- Qualified distributions are tax-free if five years have passed since the first contribution, and
 - o Taxpayer is at least 59 ½ years old or disabled, or
 - o Distributions are used for qualifying first-time homebuyer expenses.

A regular IRA owned by the taxpayer may be converted to a Roth IRA. The 10 percent early distribution tax would not apply to the conversion. Individuals may convert funds from an existing IRA, 401(k) plan and certain other qualified retirement plans to a Roth IRA regardless of the taxpayer’s Modified Adjusted Gross Income (MAGI). Paying the tax on an existing IRA and converting it into a Roth IRA could provide unlimited tax-free build-up until death. Distributions to the beneficiary also would be tax-free. To convert or not to convert will require individual analysis. Factors to be considered in resolving this question include:

- Taxpayer’s current tax bracket vs. tax bracket projected for retirement years
- Taxpayer’s other sources of funds in both the current year and retirement years
- Taxpayer’s age and expected retirement date

Reconversions will also require individual analysis, and you should consult your CPA as to whether the reconversion is advisable in your situation.

See *IRS Publication 590* or consult your CPA for additional information.

Recordkeeping

See *IRS Publication 463, Travel, Entertainment, Gift and Car Expenses, Section 5* for further information.

What kind of information do I need to substantiate my deduction for automobile, travel, entertainment and other business expenses?

As in prior years, strict substantiation rules for travel and entertainment expenses, including meals and lodging away from home and business gifts are required to prove your claim for these expenses. If adequate records are not kept, no deduction will be allowed. This is because written evidence is more reliable than oral evidence alone. However, if you prepare a record in a computer memory device with the aid of a software program, it is considered an adequate record. It is also expected that taxpayers will be required to directly indicate on their income tax returns whether adequate records, or sufficient written evidence justifying the deduction, have been kept.

No deductions will be allowed for any automobile expenses or travel expenses (including meals and lodging while away from home), for any items concerning a type of activity generally considered entertainment, amusement or recreation (or a facility used in connection with such activity), or any expenses for gifts, unless you substantiate the following elements:

1. The amount of expense or other item;
2. The time and place of the travel, entertainment, amusement, recreation or use of the facility, or the date and description of the gift;
3. The business purpose of the expense or other item; and
4. The business relationship to the taxpayer of the persons entertained, using the facility or receiving the gift.

No deduction will be allowed for approximations or estimates, or for expenses that are lavish or extravagant.

What type of proof represents adequate records?

The taxpayer should keep proof needed in an account book, diary, statement of expense or similar record. You should also keep documentary evidence that, together with your record, will support each element of an expense.

- Documentary evidence — Documentary evidence consists of such items as receipts, canceled checks, or bills, to support your expenses.
- Adequate evidence — The support used must show the amount, date, place and essential character of the expense.

- Duplicate information — The taxpayer does not have to duplicate information shown on a receipt as long as your records complement each other in an orderly manner.
- Timely kept records — The taxpayer should record the elements of expense or of business use at or near the time of the expense. A timely kept record has more value than a statement prepared later when generally there is a lack of accurate recall. It is not necessary to write down every element of expense on the day of the expense. If you maintain a log on a weekly basis that accounts for the use during the week, the log is considered a timely kept record.
- Proving business purpose — The taxpayer must generally provide a written statement of the business purpose of an expense.
- Confidential information — Confidential information relating to an expense is not necessary to provide as an element of the deduction. However, you must maintain this information and have it available to fully prove the element of expense.

Examples of documentation and adequate evidence necessary for claiming expenses incurred are:

Automobile expenses — In order to claim actual expenses associated with the business use of your automobile, adequate records must be maintained and you must prove the following elements:

1. Total expenditures related to operation of the automobile, i.e., depreciation, insurance, fuel, repairs, etc. Total expenses are accumulated for year-end allocation between personal and business use;
2. The date of business use and the destination;
3. The business purpose of the trip; and
4. The number of business miles driven and the total mileage driven for the year.

At the end of the year total automobile expenses are allocated between business and personal use based on the number of business and personal miles driven. If you choose to use the standard mileage you will only be required to record the date of the business use, the destination, the business purpose of the trip and the number of business miles. (See also the detailed explanation under the section on automobile expenses.)

Travel — You must prove the following elements:

1. The amount of each separate expenditure for travel away from home, such as the cost of your transportation or lodging, but the daily cost of your breakfast, lunch, dinner

- and other incidental elements of such travel may be totaled if they are set forth in reasonable categories such as meals, gasoline and oil and taxi fees;
2. The dates of your departure and return home for each trip, and the number of days spent on business away from home;
3. The destination or the locality of your travel, described by name of city, town or similar designation; and
4. The business reason for your travel or the business benefit derived or expected to be gained from your travel.

Entertainment — You must prove the following elements:

1. The amount of each separate expenditure for entertaining, except for incidental items such as taxi fares and phone calls, which may be totaled on a daily basis;
2. The date the entertainment took place;
3. The name, address or location and type of entertainment, such as dinner or theater, if the information is not apparent from the name or destination of the place;
4. The reason for the entertainment or the business benefit derived or expected to be gained from entertaining and, except for certain business meals, the nature of any business discussion or activity that took place; and
5. The occupation or other information about the person(s) entertained including name, title or other designation sufficient to establish the business relationship to you.

Entertaining before or after business discussion — To deduct your expenses for entertaining directly preceding or following a substantial and bona fide business discussion on the grounds that the entertainment was associated with the active conduct of your trade or business, in place of element 4 above, you must prove the date, duration and location of the business discussion, the nature of the discussion and the business reason for the entertainment or any business benefit derived or expected to be gained from entertaining. Also, you must identify the person(s) entertained who participated in the business discussion.

Business gifts — You must prove the following elements:

1. The cost (deduction is limited to \$25 per recipient per year);
2. The date of the gift;
3. The description of the gift;
4. The reason for giving the gift or any business benefit derived or expected to be gained from giving it; and
5. The occupation or other information about the person receiving the gift, including name, title or other designation sufficient to establish the business relationship to you.

Substantiation of automobile expenses, travel, entertainment and business gift expenditures should be kept in a log, account book, diary, statement of expenses or similar record, supported by adequate documentary evidence that is sufficient to establish the elements for the expenditures. For example, entries on a desk calendar, not supported by evidence, are not proper substantiation.

You are not required to record information in your account book or other record that would duplicate information shown on a receipt as long as your records and receipts complement each other in an orderly manner. Neither are you required to record amounts your employer pays directly for any ticket or other travel item. However, if you charge these items to your employer (through a credit card or otherwise) you must make a record of the expenditures.

Your records must be timely. You should record the elements of an expenditure in your account book or other record at or near the time of the expenditure to ensure your allowance of the maximum deduction for these expenses. Record entries made later, when there is a lack of accurate recall, will not comply with these rules.

Season or series tickets — Often season or series tickets are purchased for business use and to support various events. The taxpayer must treat each ticket in the series as a separate item. The taxpayer individual ticket cost is calculated by dividing the number of games or performances by the total cost (not more than face value) of the series of tickets. An adequate record must be kept to show the use of each ticket and whether the ticket is a gift or entertainment. The name of the recipient and the purpose of providing the ticket must also be included.

Skyboxes and other private luxury boxes — Rental of these boxes for more than one event at the same sports arena is generally limited to the price of a non-luxury box seat ticket.

When reporting my various expenses for tax purposes, do I have to list each item by a specific category?

The categories of expenses for automobile, travel, meals, entertainment and gifts and their elements must be listed separately. Each payment is considered a separate expenditure and must be reported:

Breakdown of expenses — All elements of automobile expense, travel, entertainment and gift expenditures must be proved. If you can prove the elements of time, cost,

place and business relationship of the expenditure, but fail to prove its business purpose, generally no deduction will be allowed.

A written statement of the business purpose of an expenditure generally is required, but the degree of substantiation of the business purpose will vary according to the facts and circumstances in each case. If the business purpose of an expenditure is clear from the surrounding facts and circumstances, a written explanation is not required.

Each separate payment usually is considered a separate expenditure. Thus, if you entertain a constituent at dinner and then take him to the theater, the dinner expense and the cost of the theater tickets are separate expenditures and must be recorded separately in your records. Some items may be totaled in reasonable categories. You may make one daily entry for such categories as taxi fares, telephone calls, meals while traveling away from home, gas and oil and other incidental costs of travel. Tips may be grouped with the costs of the services rendered to you. You are not required to total the tips but may record them separately if you desire.

Other items should be totaled. Concurrent or repetitious expenses of a similar nature occurring during the course of a single event will be considered a single expenditure. Therefore, if you pay separately for each serving of refreshments, such as at a cocktail lounge, the total paid for the refreshments will be treated as a single expenditure.

Documentary evidence is required to support all expenditures for lodging while traveling away from home and for any other expenditure of \$75 or more, except that if evidence is not readily available for transportation charges it will not be required. Though documentation for expenses under \$75 is not required, they must be established by an account book, diary, statement of expense or similar record. Documentary evidence is a receipt, paid bill, or similar evidence sufficient to support an expenditure.

Documentary evidence ordinarily will be considered adequate to support an expenditure if it discloses the amount, date, place and essential character of the expenditure. For example, a hotel receipt is sufficient to support expenditures for business travel if it contains the name and location of the hotel, the dates you stayed there and separate amounts for charges such as lodging, meals and telephone.

Similarly, a restaurant receipt is adequate to support an expenditure for a business meal if it contains the name

and location of the restaurant, the date and amount of the expenditure, and, if a charge is made for an item other than meals and beverages, an indication that such is the case.

Some documents are not adequate evidence. A cancelled check, together with a bill from the payee, ordinarily will establish the element of cost. However, a cancelled check will not by itself support a business expenditure without other evidence to show that the check was for a business purpose.

Confidential information relating to an element of an otherwise deductible expenditure, such as the place, business purpose or business relationship, need not be set forth in your account book, diary or other record if the information is recorded elsewhere at or near the time of the expenditure and is available to fully substantiate that element of the expenditure.

If you entertain a large number of people, you do not have to record each name where a readily identifiable class of individuals is involved. It will be sufficient if you designate the class. However, if the identity of a class is not sufficient to identify the persons entertained, then an individual designation of each person will be required.

The name of the recipient of a business gift does not always have to be recorded. A more general designation will be sufficient if it is evident that you are not attempting to avoid the \$25 annual limitation on the amount that can be deducted for gifts to any one individual. For example, if you purchase a large number of inexpensive tickets to local high school basketball games and distribute one or two tickets to each of a large number of constituents, it will usually be sufficient to record a general description of the recipients of the tickets.

There are special rules for cases when, because of the inherent nature of the situation in which an expenditure is made, you are unable to obtain a receipt or when you cannot produce a receipt for reasons beyond your control, such as a loss of the receipt by fire, flood or other casualty.

What happens if I do not or were not able to obtain a complete record to prove an element of expense or my records are destroyed?

The taxpayer may lose or not receive a receipt for substantiation purposes, have incomplete records or the records are destroyed. In these cases, the taxpayer must use other evidence to prove the element of expense.

The expense can be proved by:

- Providing a written or oral statement containing specific information about the element, and other supporting evidence that is sufficient to establish the element; or
- Direct evidence as to description of a gift, or the cost, time, place or date of an expense can be written or the oral testimony of your guests or other witnesses which can corroborate the information about the element of the expense.

How long do I have to keep records and receipts for expenses deducted on my tax return?

The taxpayer must retain his or her records and related documentary evidence in support of travel, entertainment, gift and automobile deductions during the period that his or her tax return is subject to audit. Normally, this period is three years from the date of filing the tax return on which the deduction is claimed. However, the period of limitations is longer if the taxpayer consents to an extension or if there has been a substantial omission from gross income. Moreover, there is no statute of limitations in cases of fraud. Amending a prior year tax return restarts the statute of limitations.

If I elect to claim the per diem amount as discussed under the section on living expenses, do I still need to maintain all these records?

You are relieved from recordkeeping for many of the details for your own meals and lodging under this option. However, you must still be able to substantiate the time, place and business purpose, unless the IRS § 162(h) election is used.

Recordkeeping for Travel

The following table is a summary of records you need to prove for travel expenses. You must be able to prove the elements listed in the first column of the chart. You prove them by having the information and receipts (where needed) for the expenses listed across the top portion of the chart.

Note: You cannot deduct amounts that you approximate or estimate.

You should keep the proof you need in an account book, diary, log, statement of expense, trip sheet or similar record. You should also keep documentary evidence (such as receipts, canceled checks, or bills) that, together with your record, will support each element of an expense.

| Elements to be substantiated | For expenditures for use of automobiles | For expenditures for travel away from home | For expenditures for entertainment | For expenditures for gifts |
|------------------------------|---|--|---|--|
| Amount | Amount of each expenditure related to the operation of the automobile including depreciation, insurance, fuel and repairs. | Amount of each separate expenditure for transportation, lodging and meals. Permissible to total incidental expenses in reasonable categories, such as gasoline and oil, taxis, daily meals for travelers, etc. | Amount of each expenditure. Incidental items, such as taxis, telephone, etc., may be totaled on a daily basis. | Cost of gift. |
| Date | Date of business use of the automobile. | Dates of departure and return for each trip and number of days attributable to business activities. | Date of entertainment or use of a facility for entertainment. (Duration of business discussion.) | Date of gift. |
| Place | Destination and mileage. Unless the standard mileage rate is used, must also keep a record of the total mileage (business and personal) so expenses can be allocated to business use at year end. | Destination by name of city or other appropriate designation. | Name and address or similar designation of place of entertainment. | |
| Description | Not applicable. | Not applicable. | Not applicable. | Description of gift. |
| Purpose | Business reason for automobile use. | Business reason for travel or nature of business benefit derived or expected to be derived. | Business reason or nature of business benefit derived or expected to be derived, including nature of business discussion or activity. | Business reason for making the gift or nature of business benefit derived or expected to be derived. |

Can I deduct the cost of my home telephone since I use it for making and receiving calls from constituents and for other state business?

The basic cost of the telephone is an expense you would incur regardless of whether you were a member of the General Assembly. If you are charged in addition to the basic rate for calls, the additional charges are a deductible expense, as long as they relate to state business and to your position as a member of the General Assembly. The basic rate, however, would not be a deductible expense. If you have a separate telephone installed exclusively for the purpose of your legislative business, then the entire cost of this telephone could be deducted as a business expense.

The cost of long distance phone calls and telegrams that relate to state business is a deductible expense. Use of an answering service is also a deductible expense, if it is related to your position as a member of the General Assembly. An answering machine again is an expense required by your office and therefore would be a deductible business expense.

Cellular Telephones

Cellular telephones and other similar telecommunications equipment are no longer considered listed property. Beginning in 2010, an employee may be able to deduct job-related expenses related to using a cell phone even though the use was not for the convenience of his or her employer and required as a condition of employment.

Although cellular telephones are no longer subject to the increased recordkeeping requirements of listed property, adequate records to establish the business use percentage of cellular phones must still be maintained.

The business use percentage is used to determine the correct amount of depreciation that an employee may deduct. In addition, the business use of the cost of cellular telephone minutes can be deducted as an unreimbursed employee business expense.

Virginia 529 Plan

The Virginia College Savings Plan offers four section 529 investment options: The Virginia Prepaid Education Program, The Virginia Education Savings Trust, CollegeAmerica and CollegeWealth.

The Virginia Prepaid Education Program (VPEP) locks in future college costs at Virginia public colleges for children in the ninth grade or younger. Either the account owner or the beneficiary must be a Virginia resident at the time the account is opened. VPEP covers full in-state tuition and mandatory fees and the investment is backed by a statutory guarantee. VPEP can also be used at any accredited school or college in the country eligible to accept federal financial aid although full coverage of tuition at these schools is not guaranteed.

The Virginia Education Savings Trust (VEST) offers a choice of 18 investment portfolios. Students of all ages can participate regardless of where they reside. VEST covers all major college expenses including tuition, fees, room and board, textbooks, required computers and supplies. VEST can be used at any accredited school or college in the country eligible to accept federal financial aid.

CollegeAmerica is offered through the American Funds, one of the oldest and largest mutual fund companies in the country and is available to all 50 states. CollegeAmerica offers 24 American Funds that fits every participant's financial plan, time horizon and tolerance for risk. Students of all ages can participate regardless of where they reside. With CollegeAmerica, you can save for all major college expenses. CollegeAmerica can be used at any accredited school or college in the country eligible to accept federal financial aid. Ask your financial advisor for information about CollegeAmerica.

CollegeWealth is Virginia's FDIC-insured 529 savings program. This program partners with BB&T and Union First Market banks. Families can open a savings account for their children's or their own higher education regardless of where they reside. The accounts are subject to regular FDIC insur-

ance rules. With CollegeWealth, you can save for all major college expenses. CollegeWealth can be used at any accredited school or college in the country eligible to accept federal financial aid.

All account owners who have Virginia taxable income and file Virginia income tax returns can deduct from their taxable income up to \$4,000 per year per account or the amount contributed during the year, whichever is less, with unlimited carryforward until all contributions to the account have been deducted. If the funds are not used for higher education expenses the contributor must add the deducted amounts back to income for state income tax purposes. Exceptions to this recapture rule include refunds as a result of death, disability, or receipt of a scholarship. Account owners age 70 or above are not subject to the \$4,000 cap and may subtract the entire amount paid during the year.

The Virginia state tax advantages are only available for investments in Virginia's Section 529 programs: VPEP, VEST and CollegeAmerica and CollegeWealth.

For more information, visit www.Virginia529.com.

Note: Taxpayers should be aware that gifts to 529 plans are part of annual gifting limitations to individuals. For 2011, the annual gift exclusion is \$13,000. Gifts in excess of this amount require the taxpayer to file a federal gift tax return. Please consult your tax advisor for more information on gift tax returns.

Virginia Income Tax

Are all of the business-related expenses discussed above deductible on my Virginia income tax return?

Since the Virginia income tax is based on income for federal purposes, with certain modifications, your business-related expenses generally would be deductible on your Virginia income tax return to the same extent as on your federal income tax return. For Virginia income tax information, go to the Virginia Department of Taxation website.

What items must be considered in determining Virginia taxable income?

Virginia requires certain additions and subtractions in computing taxable income. Additions include interest on obligations of other states, interest of federally exempt U.S. obligations, accumulation distribution income, lump-sum distribution income and other additions.

Subtractions include income from obligations of the U.S., disability income and other subtractions, such as foreign source income and Virginia College Savings Plans.



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