



IOWA GENERAL ASSEMBLY
LEGISLATIVE SERVICES AGENCY

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DATE: February 5, 2007

TO: All Legislators

FROM: Ann M. Ver Heul

**RE: 2006 Tax Year Legislators' Business Expense
Deductions Pursuant to Tax Home Provision**

**I. 2006 Tax Year Federal Business Expense Deductions
for State Legislators**

Internal Revenue Code Sec. 162(h), relating to travel expenses of state legislators, allows state legislators whose district homes are more than 50 miles from the state capitol a per diem deduction on their federal returns for business expenses incurred while at the capitol.

The maximum per diem which is allowed as a deduction for legislators pursuant to Internal Revenue Code Sec. 162(h) is determined by the per diem rate for federal employees in Des Moines, as determined by the General Services Administration, for the tax year in question. For tax year 2006, the applicable federal per diem rates were as follows:

DIVISIONS

LEGAL SERVICES
RICHARD L. JOHNSON

•

FISCAL SERVICES
HOLLY M. LYONS

•

COMPUTER SERVICES
GLEN P. DICKINSON

•

ADMINISTRATIVE SERVICES
TIMOTHY C. FALLER

January 1, 2006 – September 30, 2006: \$117.00 per day
Ratio: \$73.00 - Lodging
\$44.00 - Meals

October 1, 2006 – December 31, 2006: \$118.00 per day
Ratio: \$74.00 - Lodging
\$44.00 - Meals

Please note: New federal per diem rates issued by the General Services Administration now take effect on October 1 of each year. The rates for Iowa changed on October 1, 2006. It is possible that there may be a rate change later this year for part of 2007.

Ann M. Ver Heul

LEGAL COUNSEL
515.281.3837
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ann.ver.heul@legis.state.ia.us

A. The actual per diem provided to you by the State (expense of office), which is \$86.00 per day, is not includable in gross income because it is considered a reimbursement for business expense. This per diem is excludable from your gross income for each day the legislature was in session (including periods of four consecutive days or less when the legislature was

in recess). For 2006, the legislature was in session for 116 calendar days, i.e., 115 calendar days for the regular session and one calendar day for the special session in July.

However, pursuant to Iowa Code section 2.10 all legislators were paid expense of office per diem for only 101 calendar days, that is 100 calendar days for the regular session and one calendar day for the special session. This amount, which is \$8,686.00, is not included in your gross income because it is "deemed substantiated" as a reimbursed business expense pursuant to Internal Revenue Code Sec. 162(h).

B. If you itemize deductions, the unreimbursed excess of the allowable amount under Internal Revenue Code Sec. 162(h) from January 1, 2006, through September 30, 2006, is \$31.00 per day. This amount is deductible along with other itemized deductions if the total of all miscellaneous itemized deductions exceeds 2 percent of your adjusted gross income. In order to determine the deductibility of this unreimbursed portion of the allowable per diem, the excess amount is allocated between "meals" and "lodging and other travel expenses", in accordance with the federal per diem reimbursement rules for travel in the United States.

From January 1, 2006, through September 30, 2006, which is the period of time during which you received expense of office, the ratio for Iowa is that 62 percent of the amount is allocated to lodging and other travel expenses and 38 percent of the amount is allocated to meals. Since the state per diem rate is \$86.00 per day, the unreimbursed excess amount is \$31.00 (\$117.00 - \$86.00) for this expense period. Using the federal ratio, the following allocation is applicable:

Unreimbursed Amount	Lodging	Meals
\$31.00	\$19.00	\$12.00

1. Of the amount allocated to lodging and other travel expenses (\$19.00), the amount is fully deductible by legislators who itemize, along with all other miscellaneous itemized deductions, subject to the fact that it, along with all other miscellaneous itemized deductions, must meet a floor of 2 percent of the taxpayer's adjusted gross income.

2. For state legislators, the amount allowable for meals is the federal per diem allocation (\$12.00) less \$2.00 per legislative day. Of this amount (\$10.00), 50 percent or \$5.00 per legislative day is deductible by legislators who itemize, as an employee business expense, subject to the fact that it, along with all other miscellaneous itemized deductions, must meet a floor of 2 percent of the taxpayer's adjusted gross income.

These unreimbursed amounts do not require substantiation.

C. If you itemize deductions, you are entitled to a deduction for each day that the legislature was in session (including periods of four consecutive days or less when the legislature was in recess) for which you did not receive expense of office. In 2006, the legislature was in session for 15 calendar days during the regular session, for which legislators did not receive expense of office. If you itemize deductions, you are entitled to a deduction for each of those 15 days.

If you itemize deductions, you are also entitled to a deduction for each day that your presence was recorded at a committee meeting during the interim. This information is provided to you by the Chief Clerk's Office or by the Senate Finance Clerk and will indicate the number of days your presence was recorded at a committee meeting during the interim. The interim per diem payments which you received (\$86.00 per day) are treated as taxable wages on your W-2 form due to the statutory language which authorizes them.

These unreimbursed federal per diem amounts of \$117.00 or \$118.00 per day must be allocated between "lodging and other travel expenses" and "meals" in accordance with the ratio for such expenses under the federal per diem reimbursement rules for travel in the United States. Since the unreimbursed amount is \$117.00 per day for the period from January 1, 2006, through September 30, 2006, and \$118.00 per day for the period from October 1, 2006, through December 31, 2006, the following allocation is applicable:

Unreimbursed Amount	Lodging	Meals
\$117.00	\$73.00	\$44.00
\$118.00	\$74.00	\$44.00

1. Of the amount allocated to lodging and other travel expenses (\$73.00 or \$74.00), the amount is fully deductible by legislators who itemize, along with all other miscellaneous itemized deductions, subject to the fact that it, along with all other miscellaneous itemized deductions, must meet a floor of 2 percent of the taxpayer's adjusted gross income.

2. For state legislators, the amount allowable for meals is the federal per diem allocation (\$44.00) less \$2.00 per legislative day. Of this amount (\$42.00), 50 percent or \$21.00 per legislative day is deductible by legislators who itemize, as an employee business expense, subject to the fact that it, along with all other miscellaneous itemized deductions, must also meet a floor of 2 percent of the taxpayer's adjusted gross income.

Once again, these unreimbursed amounts do not require substantiation.

D. Attached to this memo is a form for a "Statement of Election of Tax Home Pursuant to Internal Revenue Code Sec. 162(h)". If this form is completed and attached to your income tax return, you should be in compliance with the proposed tax regulation 26 C.F.R. Sec. 1.162-24, which requires any state legislator who makes a tax home election under Sec. 162(h) for the taxable year to attach such a Statement of Election to the income tax return.

E. In past years, I have provided you with some information concerning the Federal Taxpayer Relief Act of 1997. It appeared that Section 975 of the Act, which amended 26 U.S.C. Sec. 62, might provide an above-the-line deduction for travel expenses of state legislators while they are at the state capitol if they were paid in whole or in part on a "fee basis".

According to NCSL, the IRS has been inconsistent in its interpretation of Section 975 and the definition of "fee basis". That is, some legislators have been allowed above-the-line deductions pursuant to Section 975 and some such deductions have been disallowed.

However, an IRS Chief Counsel's Office Advice Memorandum issued in 1999 and a subsequent IRS information letter published in 2002 indicate that state legislators are not compensated on a "fee basis" and thus are not allowed to deduct their unreimbursed employee

business expenses above-the-line on their federal tax returns. These expenses can only be considered as miscellaneous itemized deductions and are subject to the 2 percent floor. A copy of an NCSL memorandum concerning this issue is attached.

Neither NCSL nor this memo provides tax advice on how individual legislators should file their tax returns. The purpose of this memo is simply to make you and your tax preparer aware of tax provisions which may apply to Iowa legislators. NCSL will provide background information on Internal Revenue Code Sec. 162(h) and Section 975 of the Taxpayer Act of 1997 upon request. NCSL can be reached at 303/364-7700.

II. 2006 Tax Year State Business Expense Deduction for State Legislators

Iowa Code section 422.7(10) provides that state legislators who live more than 50 miles from the state capitol may claim the same deductions on their Iowa income tax returns for expenses incurred for meals and lodging as are allowed for federal income tax purposes.

State legislators who live 50 miles or less from the state capitol may claim deductions at a rate of \$50.00 per "legislative day". However, state legislators may choose to itemize deductions for expenses incurred for meals and lodging. Based on the language of Iowa Code section 422.7(10), it appears that the deduction of \$50.00 per day is available for each day the legislature was in session, including periods of four consecutive days or less when the legislature was in recess, and for each day the legislator's presence was reported at a committee meeting during the interim as is true under the federal provision.

III. Miscellaneous Business Expense Deductions

Please note that in 2006 you received constituent pay in the amount of \$200.00 per month. This constituent pay is included in taxable wages on your W-2 form and is also deductible as a business expense provided that you can substantiate the expenditures with receipts and a daily log listing the time, place, purpose, and amount of each expense claimed. You also received payments for mileage and taxable meals. If these amounts are direct reimbursement for expenses which you have already substantiated, they are also deductible as business expenses.

IV. Legislator W-2 Forms

Jean McPherson, from Centralized Payroll at the Iowa Department of Administrative Services, has provided an explanation of the information contained on legislators' W-2 Wage and Tax Statement for 2006.

V. 2007 Business Expense Deductions - NEW PROVISIONS EFFECTIVE

Beginning in 2007 with the 82nd General Assembly, legislators will be paid a per diem based on the maximum amount generally allowable to employees of the executive branch of the federal government for per diem while away from home at the seat of government instead of \$86.00 per day. As noted above, this amount is currently \$118.00 per day through September 30, 2007. This means that in 2007, \$118.00 per day will be excluded from the gross income of those state legislators whose homes are more than 50 miles from the state capitol for state and federal income tax purposes for up to 110 calendar days for which you may receive expense of office this year. You may also receive per diem for meetings you attend during the

interim or for attendance at a special session. Legislators will also receive a monthly constituent expense allowance beginning in 2007 of \$300.00 instead of \$200.00.

If you or your tax preparer have any questions about the information contained in my memo, please feel free to contact me. My telephone number is 515/281-3837. My e-mail address is ann.ver.heul@legis.state.ia.us

CC: Iowa House: Representatives and Former Representatives
Chief Clerk
House Finance Clerk

CC: Iowa Senate: Senators and Former Senators
Secretary of the Senate
Senate Finance Clerk

0616RR

**STATEMENT OF ELECTION OF TAX HOME
UNDER INTERNAL REVENUE CODE SECTION 162(h)**

TAXABLE YEAR: 2006

TAXPAYER'S NAME _____

SOCIAL SECURITY NUMBER _____

ADDRESS (within legislative district represented): _____

NUMBER OF LEGISLATIVE DAYS: 116

FEDERAL PER DIEM RATE FOR STATE CAPITOL:

 January 1, 2006 - September 30, 2006 \$117.00

 October 1, 2006 - December 31, 2006 \$118.00

**DISTANCE IN MILES BETWEEN TAXPAYER'S RESIDENCE WITHIN
LEGISLATIVE DISTRICT REPRESENTED AND CAPITOL BUILDING OF THE
STATE:** _____



Iowa Department of
Administrative Services

State Accounting Enterprise

Chester J. Culver, Governor
Patty Judge, Lt. Governor

Mollie K. Anderson, Director
Calvin R. McKelvogue, Chief Operating Officer

DATE: January 26, 2007
TO: Ann Ver Heul, Legislative Services Agency
FROM: Jean McPherson, DAS-SAE-Centralized Payroll
RE: W-2 Information for Legislators – Calendar Year 2006

This memo is provided to assist you in helping legislators better understand the information contained on their W-2s. Please feel free to share this information with them if they have questions about what appears on their W-2. No changes were made to the format of this year's W-2 (Wage and Tax Statement 2006), and all the same fields are being used in the same manner as in recent years.

The amounts to be added and subtracted in the following calculations can be found on the employee's last pay warrant of the year, in the year-to-date columns.

Box 1 *Wages, tips, other comp.*

- + Gross pay (includes interim per diem payments)
- + Constituent pay
- + Expense of office (if living within a 50 mile radius of the Capitol)
- + Taxable travel
- + Other certain employee business expense reimbursements
- Retirement deducted from employee's wages (shown in box 14)
- Pre-tax health, dental and life insurance premiums paid by employee
- Annuities / Deferred Comp (shown in box 12 of the W-2)
- Pretax flexible spending for dependent care benefits (shown in box 10 of the W-2)
- Pretax flexible spending for medical expenses
(unlike dependent care, this is not reported elsewhere on the W-2)

Box 2 *Federal income tax withheld*

Determined by federal tax tables and the information provided by the employee on their federal form W-4 concerning marital status and withholding allowances.

Box 3 *Social security wages (up to \$94,200 in 2006)*

- + Gross Pay
- + Taxable Travel
- Pretax health, dental and life premiums paid by employee
- Pretax flexible spending plans for dependent care and/or medical expenses

Box 4 ***Social Security tax withheld (OASDI)***

Social security wages (box 3) x 6.20%

Box 5 ***Medicare wages and tips***

Social security wages; no ceiling.

Box 6 ***Medicare tax withheld***

Medicare wages and tips (box 5) x 1.45%.

Box 7 ***Social Security tips*** (not applicable)

Box 8 ***Allocated tips*** (not applicable)

Box 9 ***Advance EIC payment***

The amount paid to an employee who qualified for advance earned income credit.

Box 10 ***Dependent care benefits***

The total amount deducted for participating employee's flexible spending account – dependent care only.

Box 11 ***Nonqualified plans***

Amount of distributions to an employee from a nonqualified deferred compensation plan or 457 plan.

Box 12a-12d Codes used are applicable to some, but not all, employees:

- C - Value of group-term life insurance covered over \$50,000 (imputed income)
- E - Section 403(b) contributions
- G - Section 457(b) contributions (deferred compensation)
- P - Excludable reimbursed moving expenses

Box 13 “Statutory employee” box will have an X in it if the employee is a statutory employee.
“Retirement plan” box will have an X in it if the employee was a participant in a State retirement plan. “Third-party sick pay” is not applicable to State employees.

Box 14 Employee's deductions for their State retirement plan if their retirement plan is IPERS, Judicial, POR (Peace Officers Retirement), or TIAA CREF.

Box 16 ***State wages, tips, etc.***

Same as Federal taxable wages (box 1)

Box 17 ***State income tax***

State income tax withheld; determined by state tax tables and the information provided by the employee on their state form W-4 concerning marital status and withholding allowances.

You may contact me at 515-281-3976 if you have any questions about this information.



NATIONAL CONFERENCE of STATE LEGISLATURES

The Forum for America's Ideas

Legislator Tax Home (updated November, 2006)

The National Conference of State Legislatures does not provide tax advice or opinions to state legislatures or to state legislators. This overview is for purposes of general guidance only. State legislators who wish to take these deductions should consider consulting a tax expert to ensure compliance with the federal tax provisions.

SUMMARY

State legislators who live more than 50 miles from the state capitol may choose to claim their district residence as their "tax home." In doing so, legislators may claim the expenses they incur while conducting official legislative business as a tax deduction on their federal income tax return. This deduction is known as the "legislators tax home deduction." It was created as part of the 1981 Economic Recovery Tax Act (Public Law 97-34) and is Section 162(h) in the IRS Code.

LEGISLATOR TAX HOME

How are the "Tax Home" Rates Determined?

State legislators who reside more than 50 miles "from the capitol building of the State" are eligible to claim the tax home deduction for living expenses. The allowable amount of the tax home deduction is the greater of the federal or state per diem rates for the state capital city, as long as the state rate does not exceed 110 percent of the federal rate. The federal rates are the same as those allowed to executive branch employees in the Federal Government. Each year, the U.S. General Services Administration (GSA) assesses the current federal per diem rates, makes adjustments where necessary, and prints the new federal per diem rates in the Federal Register. The Department of Defense sets the rates for Alaska and Hawaii. Contact NCSL to obtain the current GSA per diem rate schedule.

Calculating the Tax Home Deduction:

Category A

If a legislator is reimbursed an amount equal to the per diem amount allowable under 162(h) and the reimbursement is reported as income, the amount may be subtracted under Section 62(2)(A) of the Internal Revenue Code to arrive at adjusted gross income (AGI). This is termed an "above the line" deduction.

Category B

If a legislator is reimbursed less than the per diem amount allowable as a deduction under 162(h), the amount actually reimbursed is subtracted "above the line" to determine AGI. The difference between the allowable amount and the actual reimbursed amount is treated as a miscellaneous itemized deduction on a Schedule A and is subject to two rules. First, the excess is allocated to lodging and meals according to the ratio of meals and lodging under the federal per diem reimbursement rules applicable to the state capital, and only 50% of the amount allocated to meals is deductible (26 USC 274(n)(1)(A)). Second, miscellaneous itemized deductions are only deductible if they exceed 2% of adjusted gross income.

Once the daily deduction is determined, a state legislator may multiply this rate by the number of "legislative days" that the legislator conducted legislative business during the year. This final calculation is the total allowable deduction for a given year. In Section 162(h)(2), a legislative day is defined as any day during such year on which:

- a) the legislature was in session (including any day in which the legislature was not in session for a period of 4 days or less);
- b) the legislature was not in session but the physical presence of the individual was formally recorded at a meeting of a committee of such legislature.

The IRS Code does not define "legislative session" or "committee."

LEGISLATOR TAX GUIDES: Some state CPA societies publish an annual tax guide for state legislators that provides more detail on these and other tax provisions. See your state chapter to find out if one is available.

NCSL does not provide tax advice on how individual legislators should file their returns. Legislators are advised to consult with a tax specialist when applying the tax home provisions.