

An hourglass-shaped graphic with a globe in the top bulb and another globe in the bottom bulb. The top bulb is dark blue, and the bottom bulb is light blue. The hourglass is light gray. The globe in the top bulb is dark blue, and the globe in the bottom bulb is light blue. The hourglass is centered on the page.

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*Tax Treatment of Away From Home Expenses of State
Legislators*

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Abstract. State legislators are allowed an away-from-home expense deduction equal to the number of legislative days times a per diem amount.

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Tax Treatment of Away From Home Expenses of State Legislators

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Summary

In general, taxpayers are permitted a deduction for traveling expenses, including meals and lodging, while away from their tax home in pursuit of a trade or business. State legislators have unusual problems with the determination of their tax home.¹ Accordingly, Congress addressed these problems through enactment of a special tax code provision which allows state legislators to treat as their tax home the district which they represent. State legislators are allowed an away-from-home expense deduction equal to the number of legislative days times a per diem amount. The legislator is deemed to be away from home on each legislative day, is not required to attend the legislature for each day counted, and is allowed to include four or fewer consecutive days of legislative recess in the number of days away from home. The per diem amount is the greater of the federal or state per diem amount for employees away from home. The state per diem amount may not exceed 110% of the federal rate. Revenue losses from this provision appear to remain low because of the limited number of state legislators. This report will be updated as developments warrant.

Legislative History and Rationale

Beginning with the passage of the Tax Reform Act of 1976 (P.L. 94-455) a special provision (only for taxable years that began before 1976) was added to the Internal Revenue Code (IRC) for state legislators. The provision provided that a state legislator may elect to treat the residence located within the legislative district which he or she represents as his or her tax home. Accordingly, the legislator was permitted an away-

¹ Federal legislators are limited to a \$3,000 per year deduction for expenses incurred while away from home and living in Washington, D.C. The law provides that a Member of Congress is deemed to reside in the state, congressional district, or possession which he represents in Congress. The away-from-home deduction is subject to the 2% miscellaneous itemized deductions limitation (i.e. subtract 2% of the taxpayer's adjusted gross income from the total amount of expenses).

from-home living expense deduction that equaled the number of legislative days in session multiplied by the executive branch federal government (domestic) per diem rate.

The law defined legislative days to include days in session and any day in which the legislature is in recess for four or fewer consecutive days. Also, legislative days include when the legislature is not in session but the legislator's presence is recorded at a state legislative committee meeting.

The Act limited the deduction claimed as an away-from-home living expense deduction to the amount declared on tax returns filed before May 21, 1976. This election was permitted for all tax years not yet expired.

The provision for state legislators' travel expenses while away from home was extended for a one-year period (tax years prior to January 1, 1977) by the Tax Reduction Act of 1977 (P.L. 95-30). Another one-year extension (for tax years before January 1, 1978) was included in an Act titled the Agricultural Act of 1949 — Payments (P.L. 95-258). A further extension for a three-year period (through January 1, 1981) was part of an Act known as the Fringe Benefit Regulations — Issuance — Prohibition (P.L. 96-167).

A permanent provision for state legislators' travel expenses was made a part of the Internal Revenue Code in 1981. Included in the Economic Recovery Tax Act of 1981 (P.L. 97-34), this provision allowed state legislators to elect to treat as their tax home the legislative district they represent. The law was modified so a legislator is deemed to be away from home on each legislative day, is not required to attend the legislature for each day counted, and is allowed to include four or fewer consecutive days of legislative recess (and committee meetings). This was accomplished by an exception to the overnight test of Code §162 for state legislators. As such, elected state legislators are deemed to have away-from-home living expenses equal to the number of legislative days times the per diem amount. Under the law, the per diem amount is the greater of the federal or state per diem amount for employees away from home. However, the law limits the state per diem amount to no more than 110% of the federal per diem rate.² These special rules do not apply to those state legislators living within 50 miles of the state capitol building.

Assessment

Generally the Internal Revenue Service looks to the “facts and circumstances” to determine the tax home of an individual (i.e. time spent, amount of income derived, degree of business activity, and other significant contacts in each location). There was considerable uncertainty, as well as litigation, before enactment of the legislative solution which provided that the tax home of state legislators is the home district. State legislators argue that their public service imposes unique obligations and requirements for state legislative service. For example, the state constitution may require the legislator to be domiciled within the legislative district he/she represents thereby preventing a permanent move to the state capital where legislative functions occur. State legislative sessions may

² The Internal Revenue Service provides federal per diem rates for travel within the continental United States in Internal Revenue Service's Publication 1542, Revised Jan. 2005, at [<http://www.irs.gov/pub/irs-pdf/p1542.pdf>], visited Feb. 17, 2005.

vary in length from year to year, and without a special rule to determine the legitimate “tax home” of state legislators, the legislator’s tax home could change from one year to the next.

State legislators may not find it possible to rent accommodations “on demand” for just those times when the legislature is in session. The job of a state legislator requires frequent travel between the state capital and the legislative district. Some states have citizen legislators³ and provide low pay. If state travel reimbursements are included in legislators’ income without benefits from offsetting deductions, it forces such legislators to further subsidize the costs of their state service. It has also been argued by legislators that costs incurred for campaigning and entertaining (of constituents at the state capital) would be deductible as a cost of doing business for a businessman but were unavailable as a deduction for state legislators.

One underlying factor in providing a special rule for state legislators is that some state legislatures meet for extended periods of time which may require the establishment of a second home or an office near the Capitol, or both. The maintenance of two places results in legislators incurring duplicate living expenses. Further, it has been noted that the costs of maintaining a residence or office do not stop when the legislature is out of session.

It is generally conceded that it is appropriate to have statutory rules and that without a special rule to determine the legitimate tax home of state legislators the tax home may change from one year to the next year under a facts and circumstances test. Thus, it is generally conceded that establishing the tax home of state legislators eliminates uncertainty when filing federal taxes. Legislators were also concerned about adverse public opinion for claiming a deduction not specifically authorized which could lead to a tax audit.

Economists typically apply the principle of horizontal equity, that taxpayers with identical incomes in like circumstances should be treated equally when evaluating income tax policy — essentially a fairness doctrine. In that context, the provision of special rules for state legislators provides greater advantage to those in the business of representing their districts or counties than persons engaged in other trades or businesses. Generally, a taxpayer must either be away from home overnight or for a sufficient period that requires sleep or rest to qualify for travel expense deductions. Current law grants legislators a uniquely favorable tax status based upon a statutory formula of legislative days times a daily per diem rate. Thus, unlike other business taxpayers, the law does not require legislators to be away from home overnight nor does it require the legislator’s presence at the state capital that day. Allowance of days when the state legislator has returned to his legislative district makes this the only group of taxpayers able to deduct personal living expenses. Additionally, the availability of a statutory formula means that normal substantiation rules do not apply (i.e. a safe harbor) and legislators, unlike other taxpayers, are not required to substantiate away-from-home expenses. Finally, no other group of taxpayers may “elect” their tax home.

³ This term implies that persons expect relatively short legislative sessions and the position is not a full-time occupation.

The law allows the deduction equal to the greater of the federal or state rate (as long as the state per diem does not exceed 110% of the federal per diem). This adds complexity. Since the deduction is for a computation for federal tax liability some have argued that the federal per diem should be used in determining federal tax liability. While some have argued that the General Services Administration has been slow to adjust federal per diem rates, the per diem amounts may change over the course of a year and are generally viewed as fair.

It appears likely that this provision leads to greater federal revenue losses than if state legislators were required to deduct business expenses in the same manner as other taxpayers. Some may argue that it is not fair to incur such federal revenue losses for state legislators while federal legislators are provided a more limited maximum away-from-home deduction amount of \$3,000. However, others would note that the particular circumstances of many state legislators would constitute a significant hardship if this special tax deduction were eliminated or reduced.

Revenue Loss

In 1981 the provision was estimated to reduce federal budget receipts by approximately \$9 million in 1982, \$5 million in 1983, \$6 million in 1984, \$6 million in 1985, and \$7 million in 1986. These estimates were prepared by the Joint Committee on Taxation. Revenue losses from this provision remain low primarily because of the limited number of state legislators. However, since per diem rates are adjusted periodically to reflect cost-of-living increases, the yearly revenue costs have probably risen since establishment. In general, the Joint Committee on Taxation does not estimate provisions which lose less than \$50 million per year in their annual committee print Estimates of Federal Tax Expenditures. The projected revenue loss did not appear in the most recent issue.⁴

⁴U.S. Congress, Joint Committee on Taxation, *Estimates of Federal Tax Expenditures for Fiscal Years 2005-2009*, committee print, 109th Cong., 1st sess., JCS-1-05 (Washington: GPO, 2005), at [<http://www.house.gov/jct/s-1-05.pdf>], visited Feb. 17, 2005.