



# Tax Guide for Maryland State Legislators

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THIS TAX GUIDE HAS BEEN PREPARED BY  
MEMBERS of MACPA'S FEDERAL and STATE TAXATION COMMITTEES

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MACPA Members, 2006 Tax Guide for State Legislators Subcommittee



Dear Maryland State Legislator:

The Maryland Association of Certified Public Accountants, Inc. (MACPA) is pleased to present this "Tax Guide for Maryland State Legislators," which has been prepared specifically for members of the Maryland General Assembly for the 2006 tax year.

The purpose of this income tax guide is to provide answers to questions that you may have concerning the income tax laws as they relate to your unique position as an elected official. This guide is not designed to address tax matters unrelated to your activities as a state legislator.

For tax questions not answered in this guide, for consultation on other tax or accounting questions and for assistance in the preparation of your income tax returns, we suggest that you contact your Certified Public Accountant or MACPA at 800-782-2036.

Sincerely yours,



Tamara Bensky, CPA  
*Chair*



J. Thomas Hood, III, CPA  
*Executive Director & CEO*

## INTRODUCTION

When reading the material presented in this guide, you will become aware of the various income tax deductions that may be available to you as a state legislator. Individual questions and answers emphasize the necessity for adequate record keeping, and it is important to remember that the burden of proof regarding substantiation for deductions is yours. Failure to maintain adequate records may result in the disallowance of claimed deductions.

As you will note when referring to certain questions and answers, the concept of “tax home” is frequently discussed. For tax purposes, the determination of your “tax home” is the principal focus in establishing the deductibility of certain expenditures. The determination of your “tax home” is made based upon the facts and circumstances relative to a particular individual and is not necessarily your domicile or residence.

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## AUTOMOBILE AND OTHER TRAVEL EXPENSES

1. **Q. What can I deduct for traveling to and from Annapolis?**

- A. A deduction is allowed for your actual travel costs to the extent that you are not reimbursed by the State. As a State legislator, some or all of such travel is considered “business travel.” Calculation of the deductible amount is discussed below.

For most purposes, this travel will be done by personal vehicle. To determine the actual costs of a personal vehicle, include the costs of gasoline, oil, repairs, licenses, insurance and depreciation. Receipts of service records should be maintained to document these costs. The deduction allowed is based upon an allocation between your personal and business use. In order to support this allocation, you must maintain a log book indicating the nature of your use of the auto.

If you use your vehicle less than 50% for business, any depreciation would be calculated using the straight-line method. If it is used 50% or more for business, the MACRS accelerated method is used. Depreciation may be further limited by the luxury automobile rules.

For taxpayers who do not wish to maintain detailed receipts, the IRS does allow the use of standardized rates. However, this method may result in a smaller tax benefit. As with the actual expense method, you must maintain a log to determine the number of business miles.

Under this optional method, the taxpayer may deduct 44.5 cents per mile for all business miles driven in 2006. See Question 6 for the definition of business mileage. The 2007 rate will increase to 48.5 cents per mile.

The business portion of parking fees and tolls is deductible in addition to the optional standard rates. The interest on your auto loan is personal interest and is not deductible.

2. **Q. How do I report mileage or automobile expenses incurred as a State legislator on my tax return?**

- A. You are considered to be an employee of the State of Maryland. All mileage expenses or automobile expenses are reported on Form 2106—Employee Business Expenses. Since these expenses are miscellaneous itemized deductions subject to the 2% of adjusted gross income floor, they may not be fully deductible.

3. **Q. What other mileage expenses can I deduct?**

- A. As a member of the General Assembly, you may incur travel expenses while in your home district. Travel expenses to community meetings, speaking engagements or meetings of importance to your legislative position are deductible. A record of all mileage and expenses should be made in your log book.

This expense can become substantial, particularly for those individuals whose Senate or House districts are large.

4. **Q. What about travel expenses incurred while going to meetings during a political campaign for my reelection? Although I am running for reelection, I still feel it is necessary to attend these meetings to explain to my constituents the activities of the General Assembly, the legislation on which we are currently working and/or the disposition and explanation of legislation that has gone through committees or upon which we have already acted.**

- A. The Internal Revenue Code specifically states that no campaign expenses are 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 reelection and those expenses that can be directly attributable to serving the legislator’s constituency.

5. **Q. If I use another mode of transportation to get to Annapolis, can I deduct these expenses?**
- A. If you use a bus, airplane or other means of transportation to Annapolis, these expenses should be detailed on Form 2106. You should also report the amount of reimbursement you received for travel on Form 2106 (thereby reducing your deduction), unless it is included in your W-2.
6. **Q. How do I determine deductible mileage?**
- A. All mileage incurred in connection with legislative business is deductible with the exception of that portion attributable to commuting.
7. **Q. What is commuting mileage?**
- A. Generally, any mileage incurred between your personal residence and your place of business (tax home) is considered to be commuting. If you travel each day from your residence to the State Capitol Building in Annapolis, this is considered commuting except as noted in question 9.
8. **Q. How should I treat reimbursements for travel received from the State of Maryland?**
- A. If business mileage records are maintained and you are fully reimbursed for actual mileage driven and the amount does not exceed the current federal rate (see question 1) then it is not necessary to report this reimbursement on your 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 this reimbursement must be reported as taxable income.
- Should your reimbursement exceed the federal rate allowed, then this amount must be reported on your return. If you are required to include this reimbursement in income, then you should also deduct any related expenses.
- You may not deduct any expenses for which you are reimbursed unless you report the reimbursement as income.
9. **Q. Is my tax home considered to be my office in the legislative district that I represent, or the State Capitol Building in Annapolis?**
- A. This will depend upon the facts and circumstances in each case. Generally, this determination is based upon the amount of time you are required to spend at each location for business purposes. If you are required to spend the majority of your time at the State Capitol Building in Annapolis, then Annapolis will be considered your tax home. If the legislative sessions are relatively short or infrequent, and you are not required to be present in Annapolis for numerous committee meetings, your office in your legislative district will be considered your principal place of business and your tax home.
- An exception to the above may be made where your principal residence within the legislative district you represent is more than 50 miles from the State Capitol Building. In this case, you may elect to treat your home legislative district as your principal place of business. This option is available even though you spend the majority of your time in Annapolis.

## OUT-OF-TOWN LIVING EXPENSES

10. **Q. What are the advantages of electing to treat my legislative district as my tax home when my principal residence located within that district is more than 50 miles from Annapolis?**
- A. Additional deductions are allowable for out-of-town travel. If this election is made, you will be entitled to a deduction for living expenses incurred while traveling to and staying in Annapolis.
11. **Q. What types of living expenses qualify for deductions made under this election?**
- A. Living expenses for this purpose refer to expenses for meals subject to the limitations noted in question 17 and lodging, laundry expenses and other expenses incidental to travel in pursuit of legislative business.
- Living expenses do not include travel fares, the cost of telegrams or telephone calls or local transportation expenses for business purposes. These items are deductible under the rules discussed above, in addition to the deduction available for living expenses.
12. **Q. How is the deduction for out-of-town living expenses computed where such an election is made?**
- A. The deduction is computed by multiplying each legislative day by the greater of:
- (1) The per diem amount allowed for employees of the State of Maryland who are away from home (but not over 110% of the federal per diem), or
  - (2) The per diem amount allowed for federal government employees who are away from home.
- The Oct. 1, 2006 to Sept. 30, 2007 federal per diem for Annapolis, MD is \$116 for lodging excluding taxes and \$64 for meals and incidental expenses.
13. **Q. What is a legislative day for purposes of computing this deduction for living expenses?**
- A. A legislative day includes the following:
- (1) Any day on which the legislature is in session, including any day on which the legislature was not in session for a period of four consecutive days or less, or
  - (2) Any day on which the legislature was not in session, but your physical presence is formally recorded at a committee meeting.
14. **Q. What expenses can I deduct for amounts paid living in a hotel, motel, apartment, camper or similar mode of residence while attending sessions in Annapolis?**
- A. For hotels, motels and other similar commercial places of residence while in Annapolis and away from your normal tax home, you are allowed to deduct the actual amount paid for the room (including any taxes or service charge for which you may be charged).
- If a hotel or motel room is shared with other legislators or individuals, each may deduct the share of the hotel room expense actually paid. If you are paying the motel or hotel a fixed monthly rate, that amount would be allowed as a deduction as long as it is paid by you and while you are away from home on business.
- If you rent an apartment by yourself or share one with another individual, you are allowed to claim as a business deduction the actual amount that you pay for your share of the rent, utilities, telephone and any furniture you may be required to rent. In each case, you or someone within the group should keep the paid receipts for every dollar that is expended, so that these can be provided to any examining agent 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 and an indication as to how these costs were divided among the various roommates.

If you own a trailer or camper and bring it to Annapolis to live in while attending legislative sessions, you are generally allowed a deduction that would include depreciation, repairs and the cost of operating the camper facilities, such as batteries, water supply, etc. Caution should be exercised as certain expenses are subject to proration based upon your percentage of business use. Consult your Certified Public Accountant for further details.

15. **Q. Because I am in Annapolis for long periods of time, I find it necessary and desirable to have my spouse and children come to Annapolis on occasion. Can I deduct the cost of their travel to Annapolis, motel costs and cost of their meals?**
- A. No, unless you can establish that the presence of your spouse or child served a bona fide business purpose and/or they are bona fide employees and the expenses incurred are bona fide business expenses. This same rule applies if your spouse accompanies you on a trip for a legislative conference. The statute does not contain a definition of bona fide employee or bona fide business purpose, so questions regarding the requirements will be determined on a case-by-case basis.
16. **Q. After some committee meetings, which last late into the evening (until 11 p.m. or 12 midnight), I go out for a sandwich or some refreshments. Is this a deductible business expense?**
- A. Yes, subject to the limitations as discussed above (#11) and below (#17).

## ENTERTAINMENT EXPENSES

In order for entertainment expenses to be deductible, they must meet certain criteria. The expenses must be either “directly related to” or “associated with” the active conduct of your business. Therefore, the entertainment must occur during, directly before or directly after a substantial and bona fide business discussion. However, as indicated below, there are certain exceptions to these rules.

17. **Q. Are there any limitations to the deductibility of business meals and entertainment expenses?**
- A. Yes. Only 50% of the cost of meals and entertainment is deductible. This law also applies to meals consumed while away from home overnight on business.
- Additionally, if these expenses are considered unreimbursed employee business expenses, they must be treated as miscellaneous itemized deductions, which are deductible only to the extent that the aggregate of such deductions exceeds two percent (2%) of your adjusted gross income.
18. **Q. What is “entertainment?”**
- A. Entertainment includes any activity generally considered to constitute entertainment, amusement or recreation, whether or not the activity might also be characterized as advertising or public relations. Generally, this would cover entertaining guests at such places as night clubs, country clubs, theaters, sporting events and on yachts or on hunting, fishing, vacation and similar trips (see #34).

## BUSINESS MEALS

19. **Q. If, for business reasons, I take a constituent or business associate to breakfast, lunch or dinner at a restaurant, hotel or to a bar for a few drinks, but we do not discuss business, can I deduct the cost of this entertainment?**
- A. No. The expense would be deductible only if a business discussion is held preceding, during or after the meal.
20. **Q. If I am required to meet with a constituent regarding a state problem and I meet him at home for breakfast, lunch or dinner, am I able to deduct this cost?**
- A. Yes, as long as the cost is related to your legislative position and you can show a business purpose for the meal.

21. **Q. Frequently I have lunch with other legislators primarily for personal reasons. If we alternate in paying for lunch, does this make the cost deductible?**
- A. No. The cost of the lunch is not incurred in the conduct of legislative business, and therefore, is considered to be a personal or social expenditure. However, it could still be deductible as an out-of-town living expense, subject to the above requirements (see #11).
22. **Q. While in Annapolis on certain special occasions, such as St. Patrick's Day, I will have a gathering of fellow legislators and other individuals connected with the legislature. Can I deduct the expense of this gathering as a business expense?**
- A. If the gathering can be shown to have a business purpose, then it would qualify as a business deduction. You should retain receipts for support, indicating the business purpose and the names of those who attended the function.
23. **Q. During the holiday season or at the end of a session, fellow legislators and I take the secretaries who work long hours during the year out to dinner. Is this a deductible business expense?**
- A. The dinner expense for the secretaries would normally be deductible if the secretaries were employees of the legislators. Since the secretaries are employees of the State, however, there is no employee-employer relationship. To be deductible under such circumstances, the expense must be directly related to a trade or business.
- The IRS Regulations say 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."

## ASSOCIATED ENTERTAINMENT EXPENSES

24. **Q. Are entertainment expenses incurred at places such as night clubs, theaters, sporting events or fishing trips or on yachts allowed if the expenses are incurred solely for business goodwill purposes?**
- A. Yes. If the taxpayer can show that the entertainment took place directly before or after a substantial and bona fide business discussion, the cost of such entertaining would generally be allowed.
25. **Q. What is a substantial and bona fide business discussion?**
- A. Whether a business discussion is substantial and bona fide depends upon the facts and circumstances of each case. However, it must be shown that you actively engaged in a business discussion, meeting, negotiation or other bona fide business transaction, other than entertainment, to obtain some business benefit. Also, it must be shown that business activity was substantial in relation to the entertainment.
26. **Q. How long must this discussion be in order to qualify as substantial?**
- A. There is no specified length. All the facts and circumstances will be considered. The substantial requirement will be satisfied if active conduct of business was the principal character of the combined business and entertainment activity. However, it is not necessary that more time be devoted to business than to entertainment.
27. **Q. How soon before or after the substantial and bona fide business discussion must the entertainment be so that the cost of "associated" entertainment is not disallowed?**
- A. Entertainment that takes place on the day of the business discussion will qualify. However, if the entertainment does not occur on the day of the business discussion, all the circumstances of the case will be considered, including the reasons for not having the entertainment on the day of the business discussion. For example, if the business associate is from out of town, the entertainment on the day before or the day after the business discussion will qualify.

28. **Q. Is it necessary that business actually result from each and every entertainment expenditure for which a deduction is claimed?**
- A. No.
29. **Q. How do you determine that the principal character or aspect of the combined business and entertainment was the transaction of business?**
- A. All the facts will be considered, including the nature of the business transacted during the entertainment and the reasons for conducting business during the period of entertainment. A business discussion which is only incidental to the entertainment does not qualify. However, it is not required that more time be devoted to business than to entertainment.
30. **Q. Are there situations where the conduct of business is considered not to be the principal character or aspect of the combined business and entertainment?**
- A. Yes. This would be true where the entertainment takes place on hunting or fishing trips or on yachts and other pleasure boats unless the taxpayer is able to establish otherwise.
31. **Q. Are there any other situations where entertainment generally is not considered to be directly related?**
- A. Yes. Entertainment occurring in circumstances where there is little or no possibility of engaging in the active conduct of business generally is not considered directly related. Examples of such circumstances are (a) meetings at night clubs, theaters, sporting events, or essentially social gatherings such as cocktail parties, and (b) situations where you meet with a group that includes persons other than business associates at places such as cocktail lounges; country, golf, and athletic clubs; or vacation resorts. However, you may overcome this presumption by establishing, for example, that you did engage in a substantial business discussion during the entertainment.
32. **Q. Would entertainment of business and civic leaders at the opening of a new hotel or theatrical production be considered in a clear business setting if the purpose is to obtain business publicity rather than create or maintain the goodwill of the persons entertained?**
- A. Yes. Generally, entertainment of a clear business nature occurring under circumstances where there is no meaningful personal or social relationship between you and the persons entertained will be considered directly related.

## ENTERTAINMENT FACILITIES

33. **Q. What is an entertainment facility?**
- A. Generally, an entertainment facility is any property used in connection with entertainment, such as a motor car, airplane, yacht, hunting lodge, fishing camp, swimming pool, tennis court, bowling alley, ski lodge, apartment or other housing located in a recreational area.
34. **Q. Under what circumstances would club dues and fees be deductible?**
- A. No deduction is allowed for amounts paid or incurred for membership in any club organized for business, pleasure, recreation, or other social purpose. This rule applies to all types of clubs, including business, social, athletic, luncheon and sporting clubs or membership in airline and hotel clubs. The deduction disallowance rule also applies to amounts paid or incurred for personal seat licenses.
35. **Q. Can I deduct all other expenditures for entertainment facilities?**
- A. No. Expenses with respect to an entertainment facility that are disallowed include depreciation and general operating costs, such as rent and utility charges, repairs, painting, insurance, salaries or expenses of caretakers or watchmen, etc. Losses realized on the sale or other disposition of a facility are also barred.

36. **Q. Do the rules concerning entertainment facilities also apply to expenses for items such as food and beverages furnished during entertainment at a facility?**
- A. No. Such costs would be subject to the general entertainment rules. For example, you can deduct the cost of business meals at a country club even under circumstances where you cannot deduct any of the dues to the club.
37. **Q. Are interest and taxes on a facility disallowed?**
- A. No. Expenses, such as interest, taxes, and casualty losses, are not subject to the entertainment rules and may be deductible under other provisions of the law, even if the facility is used solely for personal purposes.
38. **Q. Are box seats or season tickets to theaters and sporting events treated under the facility rules?**
- A. No. The cost of the box seat or season ticket is allocated to the separate amusement events. The expense for an event may be deductible regardless of whether the box seat or season ticket is used more than 50% for business purposes.
39. **Q. Can I deduct the cost of my luxury skybox?**
- A. If you are leasing the skybox for business purposes for only one event, then it would be an allowable entertainment expense. When the lease is for more than one event, the deductible amount would be limited to the cost of non-luxury box seats.
40. **Q. Are dues paid to professional associations deductible?**
- A. These organizations are not social, athletic or sporting clubs. Therefore, dues to these organizations are not affected by the entertainment rules and may be deductible as other business expenses. The same is true for civic organizations such as Kiwanis, Lions, Rotary and Civitan clubs.

## BUSINESS GIFTS

41. **Q. Can I deduct the cost of a business gift?**
- A. Yes. Up to \$25 annually may be deducted for each recipient. If the total cost of all of your business gifts to one individual during the taxable year exceeds \$25, you may only deduct \$25.
42. **Q. Since different rules apply to entertainment and to gifts, when is an expenditure considered entertainment and when is it a gift?**
- A. Any item that might be considered either entertainment or a gift generally will be considered entertainment and not a gift. However, special rules consider certain items as gifts. For example, packaged food or beverages furnished to a business customer for consumption at a later date, are considered gifts. However, a gift of tickets for a theater performance or a sporting event where the giver does not accompany the recipient, may be treated as either a gift or entertainment, whichever is more advantageous.
43. **Q. If I provide a gift to a constituent that costs \$25 and my spouse gives that same person a gift costing \$25 during the same year, may we deduct both gifts?**
- A. No. A husband and wife who make gifts are considered to be one taxpayer for purposes of computing the \$25 limitation. This rule applies even if the husband and wife have separate businesses and each has an independent business connection with the recipient.
44. **Q. Are there any exceptions to the \$25 limitation on business gifts?**
- A. Yes, there are three major exceptions:
- (1) Items costing \$4 or less on which the name of the taxpayer is clearly and permanently imprinted and is one of a number of identical items distributed generally by the taxpayer. This exception includes such items as pens, desk sets and plastic bags and cases on which the taxpayer's name is imprinted.

- (2) Advertising signs, display racks and other promotional material to be used on the business premises of the recipient.
- (3) Certain awards to employees: up to \$400 for an “employee achievement award” given away to a single employee in any quarter and up to \$1,600 for a “qualified plan award” given to a single employee per year. You should consult your Certified Public Accountant for guidance on your situation.

## MAINTENANCE OF AN OFFICE

45. **Q. Can a legislator deduct any costs of his home as a business expense?**
- A. Yes, provided a portion of the home (not a separate structure on a residential property) is used exclusively and on a regular basis as:
- (1) The principal place of legislative business, or
  - (2) A place where legislative business, such as meetings with constituents are conducted. In addition, this deduction is limited to the net income (exclusive of home office expenses) generated at this location. Any excess expenses may be carried forward to future years.
46. **Q. What expenses can I deduct for maintaining an office?**
- A. If the office is used exclusively for legislative purposes and qualifies for home office deductions, a percentage of all related expenses including rent or depreciation, utilities, insurance, maintenance, mortgage interest, and real estate taxes are deductible to the extent of income derived from your legislative activities. The cost of various depreciable assets, including furniture, computers and equipment, can be fully deducted in the year purchased (business portion if over 50%) up to \$108,000 for 2006 (known as section 179 deduction). This also is limited on the Maryland return. Other expenses such as clearing of snow, lawn care, etc. required for the proper maintenance of the entrance and office could be deductible. These expenses must be allocated between the business and non-business use portions. Be aware that there is a hierarchy in deducting expenses. The allocable portion of real estate taxes and mortgage interest must be utilized first. Those expenses which do not impact the basis of the property, such as insurance, utilities and maintenance, are deducted next, while depreciation expense is deducted last. You should consult your Certified Public Accountant for guidance in each situation.
- Expenses directly connected with only the office portion are fully deductible.
47. **Q. Instead of or in addition to an office in my home, I maintain a rented office in my district for purposes of serving my constituency. What expenses can I deduct on my tax return for the cost of maintaining this office?**
- A. If the office is being used exclusively for legislative purposes, all expenses related to this office, such as rent, utilities, depreciation on improvements and equipment, etc., are 100% deductible. However, to the extent these expenses are reimbursed or paid directly by the state, any deduction must be reduced by the payment or reimbursement.
48. **Q. What is the tax treatment of employee salaries?**
- A. Salaries or wages is another deductible expense you may incur. If you hire someone, such as a full-time or part-time secretary, to assist you in legislative matters and handling constituent complaints, the compensation paid is deductible. In addition, you are required to register with the State of Maryland for state income tax withholdings and unemployment insurance purposes. For details on the proper accounting and tax reporting of payrolls, contact your Certified Public Accountant for advice.
- If you have unpaid student or other volunteer help for local legislative matters and no out-of-pocket expense is incurred by you, there is no tax deduction. (See #47.)

49. **Q. If I have a legislative assistant in my home district and pay my assistant a token amount each month, am I required to go through the process of filing payroll tax returns and withholding payroll taxes?**
- A. In almost all situations, any amount paid for services is 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). You should consult your Certified Public Accountant for guidance in each situation.

### TELEPHONE EXPENSE

50. **Q. Can I deduct the cost of my home telephone since I use the telephone for placing and receiving calls from constituents and for other State business?**
- A. The basic cost of the home telephone, be it a private or party line, is not deductible since it is an expense that you would incur regardless of your position as a member of the General Assembly. If you are charged on the basic rate for calls in excess of a maximum amount, then the cost of these calls, as long as they relate to State business and to your position as a member of the General Assembly, is 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 telephone calls, cellular phone charges and telegrams that relate to State business are deductible expenses. 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 to record phone messages at home in your absence or a fax machine would qualify as an expenditure required by your office. The costs of relatively inexpensive equipment could be deducted in full while the cost of a more expensive device should be capitalized and depreciated over its useful life. (See #47.)

### ADVERTISING

51. **Q. As a member of the General Assembly, I am often called upon to pay for ads in trade journals, ad books, or magazines published by various organizations in my district. Can I deduct the cost of these ads?**
- A. Where these ads are paid for by you and are a necessary part of your business in order to maintain relations with your constituency and promote your name, this type of expenditure may be deducted. If these ads appear during your reelection campaign, it would be best to exclude the cost of these ads from your tax deductible items since campaign expenses are not deductible. Ads appearing during your campaign should be paid for by campaign contributions. The cost of ads appearing at any time in a publication that uses the proceeds of such advertisements to benefit a political party or candidate is not deductible.
52. **Q. As a member of the General Assembly, I am requested, and in effect required due to my position, to attend many dinners within my district. Can I deduct the cost of these dinners?**
- A. Yes, if you pay for your dinner. Any costs incurred to attend such dinners (travel expense, parking fees, etc.) are also deductible subject to the same rules and limits of other business meals. The costs of dinners that qualify as political fund raisers are not deductible.
53. **Q. As a method of advertising, I buy calendars, pens or similar items that are distributed to my constituency. This material displays my name, address and phone number so that I may be contacted by my constituents. Can I deduct the cost of those items?**
- A. Since this is directly related to the business purpose of adequately and properly serving your constituency, you may deduct the cost of these items on your tax return as unreimbursed business expenses.

## OTHER EXPENSES

54. **Q. What other expenses can I deduct on my tax return?**
- A. There are many other expenses you may incur as a result of your position as a member of the General Assembly. Again, these expenses would all be considered miscellaneous itemized deductions that may only be deducted to the extent they exceed two percent of your adjusted gross income. Some of these expenses would include the following:
- (1) Stationery and postage relating to mail concerning your business as a member of the General Assembly.
  - (2) Any other supplies such as pens, paper clips, pencils, etc. that are necessary to maintain your office and serve your constituency.
  - (3) The cost of obtaining newspapers, magazines and additional publications that are required to properly execute your legislative duties. Examples include special weekly papers in your district or special publications relating to politics, the State or other areas of government that are necessary for you to improve yourself as a legislator.
  - (4) The cost of holiday greeting cards mailed to community leaders. These costs include cards, envelopes, postage and your family photograph, if enclosed.
  - (5) The cost of newsletters sent to constituents is a tax deductible expense.

## RECORD KEEPING

55. **Q. What type of information do I need to substantiate my deduction for travel and entertainment?**
- A. Estimates are not acceptable in most circumstances. The taxpayer must substantiate all expenditures for business related travel and entertainment with adequate records that offer sufficient corroborating evidence. The following information is essential:
- (1) The amount spent daily for meals, lodging, and transportation other than by automobile. The costs of travel by automobile may be substantiated through using the standard mileage allowance (see question 1) for all of your business miles. Such expenses may be aggregated in reasonable categories such as gasoline and oil and taxi.
  - (2) The dates of departure and return, and the number of days spent on business.
  - (3) Destination or locality of the travel, designated by the name of a city, town, or similar description.
  - (4) The business relationship of the person or persons entertained, which may be indicated by name, title, occupation, or other designation sufficient to establish the relationship.
  - (5) Typically, the use of a travel/entertainment log or diary is the best means for maintaining adequate substantiation. (see Q & A 61.)
56. **Q. If I entertain a large group of people, must I maintain a record of each individual person attending?**
- A. If you entertain a relatively large group of people, you are not required to record the name of each individual present if a class designation would suffice to indicate the business relationship. However, members of the class must be readily identifiable. Thus, a designation such as “all the officers of the Chamber of Commerce” would be sufficient. But if the group is large and heterogeneous so that members could not be easily identified, you are required to list each person entertained.
57. **Q. If the entertainment expense is “associated with” rather than “directly related to” the active conduct of my legislative business, must I maintain certain records?**
- A. If the entertainment is “associated with” rather than “directly related to” the active conduct of your business, you must also record:

- (1) The date and duration of the business discussion which preceded or followed the entertainment.
  - (2) The place where the business discussion was held.
  - (3) The nature of the discussion, its purpose and the benefit derived or expected from the discussion.
  - (4) The identity of the persons entertained who participated in the business discussion.
  - (5) Campaign-related entertainment expenses are not deductible.
58. **Q. How do I substantiate my deduction for business gifts?**
- A. If you wish to deduct the cost of business gifts, you must substantiate the following:
- (1) The cost and a description of the gift.
  - (2) The date of the gift.
  - (3) The business reason for, or the benefit derived or expected, as a result of the gift.
  - (4) Your relationship to the recipient, including the name, title, or other designation sufficient to establish such relationship.
59. **Q. If I make a gift to a large number of individuals, must I maintain a record of each recipient?**
- A. It is not necessary to record the recipient's name in certain situations if the business relationship of the gift is clear and it is apparent that you are not attempting to avoid the \$25 per donee limitation. Thus, if you purchase a large number of inexpensive calendars and distribute one or two of them to each of a large number of constituents, you need not record the names of the recipients. However, you must still substantiate the cost, date, description and business purpose of the gift.
60. **Q. How do I substantiate my deduction for other business expenses?**
- A. Other business expenses must be supported by receipts, canceled checks and books of record. In every case, the business nature of the expense must be evidenced in some fashion.
61. **Q. What constitutes adequate records?**
- A. Adequate records consist of the following:
- (1) Diaries and account books.
  - (2) Other documentary evidence, i.e. logs, trip sheets, statement of expenses, etc.
62. **Q. When should I prepare these records?**
- A. It is required that the elements of an expenditure be recorded "at or near the time" when the expense was incurred. Such records are believed to have a "high degree of credibility not present with respect to a statement prepared subsequent to when there is generally a lack of accurate recall." Although no special form of records must be maintained, it is clear that the IRS assumes that the taxpayer will keep a diary or account book in which entries can be made on a daily basis.
63. **Q. What type of information should be contained in these entries?**
- A. The degree of specificity of entries in a diary or account book will vary with the facts and circumstances of each expenditure. Where documentary evidence is required, it is not necessary to make a diary entry that replicates information contained in the receipt if the receipt and diary complement each other in an orderly manner. Again, where the business purpose of an expenditure is evidenced from surrounding facts and circumstances, a written statement of such business purpose is not required. Confidential or highly sensitive information need not be recorded in a diary or account book. However, the taxpayer should be ready to submit a contemporaneous record of the expenditure to an IRS agent during an audit if he is to obtain a deduction for the expenditure.
64. **Q. Is a diary or account book standing alone always considered to be sufficient documentation?**
- A. A diary or account book standing alone is not always sufficient substantiation. The taxpayer must be prepared to produce documentary evidence (i.e., receipts, paid bills, etc.) in order to deduct lodging expenses incurred while traveling away from home and expenses in excess of \$75. Usually a receipt

will suffice if it contains enough information to establish the amount, date, place and character of an expense. Thus, a hotel receipt must include the name, location, date, and the separate charges for lodging, meals, telephone, etc. if it is to serve as adequate substantiation of a business travel expense. Similarly, a restaurant receipt must indicate the name and location of the restaurant, the date, and the charge for food, beverages and other items.

65. **Q. Will a canceled check alone ordinarily constitute adequate documentation of my expenses?**
- A. A canceled check alone will not ordinarily constitute adequate documentary evidence since it does not show in detail the specific items composing the total expenditure. However, a canceled check, in connection with the payee's bill, will typically be sufficient to substantiate the business nature of an expenditure.
66. **Q. Are there any alternatives available in supporting transportation expenses in excess of \$75 where the documentary evidence is not readily available?**
- A. Documentary evidence supporting an expenditure for transportation in excess of \$75 will not be required if such is not readily available. Such expenses can be easily authenticated by fare schedules and by mileage.

## RETENTION OF RECORDS

67. **Q. How long must I retain my records?**
- A. You must retain your records and related documentary evidence in support of travel, entertainment and gift deductions during the period that your tax return is subject to audit. Normally, this period is three years from the date of filing the tax return on which you claimed the deduction. However, the period of limitations is longer if you consent to an extension or if there has been a substantial omission from gross income. Moreover, there is no statute of limitations in case of fraud. It is generally recommended that actual tax returns be retained indefinitely. Documentation related to property (basis, depreciation, etc.) should be kept three years beyond the date of sale of such property.

## TAX LAW CHANGES

68. **Q. Are there any changes in the 2006 federal tax legislation that affect my tax situation as a legislator?**
- A. There were no changes specifically related to legislators in 2006. There were two major tax laws enacted in 2006. Both the Tax Increase Prevention and Reconciliation Act of 2006 and the Pension Protection Act of 2006 contain provisions that may apply to your personal tax situation.

## INCOME AND EXPENSE OF POLITICAL ORGANIZATIONS

69. **Q. Are campaign contributions includable in income?**
- A. Generally, no. Campaign contributions are not includable in income provided you establish a political organization to collect the funds. However, a segregated fund established and maintained by an individual may qualify as a political organization. A segregated fund must be separated from your personal assets. This fund may take the form of a checking or savings account that is clearly identified as a segregated fund. The contributions collected in this fund may only be used for expenditures for activities that are directly related to the election process.
70. **Q. When would political gifts received by me as a candidate be taxable?**
- A. Political funds are not taxable to the political candidate by or for whom they are collected if they are used for expenses of a political campaign or some similar purpose. Any amount diverted from the channel of campaign activity and used by the political candidate for any personal purpose, however, is income taxable to such candidate for the year in which the funds are used. Additionally, expenditures of political funds by a political candidate for other than campaign or similar purposes will be considered a diversion of such funds requiring the funds to be included in his income.

Deductions will be allowed for those expenditures that qualify as deductions under the applicable provisions of the Internal Revenue Code of 1986. For example, depending upon the facts and circumstances present, an expenditure could qualify as an ordinary and necessary business expense or a charitable contribution. Unexpended balances of political funds which are repaid to known contributors are not considered to be either expended or diverted.

**71. Q. If I am elected, may my excess campaign contributions be later used for any ongoing official office expenses?**

A. No. Pursuant to the Fair Election Practices Act and the Public Ethics Law of the State of Maryland, excess campaign contributions may not be later used by members of the General Assembly to pay a successful candidate's official expenses unrelated to an election.

**72. Q. Is there any other type of income that would not be taxable to me as a political candidate?**

A. Yes. Other types of nontaxable income in the segregated fund include contributions of property, membership dues, fees or assessments from a member of a political organization or proceeds from a political fund-raising event.

**73. Q. Are there new reporting requirements for political organizations?**

A. Federal legislation adopted in 2002 altered the filing requirements for certain political organizations under Section 527 of the Internal Revenue Code. State and local candidate committees are exempt from filing Forms 8871, 990-EZ, and 990. Since these organizations already disclose certain information to state agencies, it is not necessary to file forms with the Internal Revenue Service, which essentially duplicate this information.

The pre-July 2000 requirement to file Form 1120-POL was reinstated. This means that a candidate committee with taxable income after taking the \$100 specific deduction (usually investment income), must continue to file Form 1120-POL.

## TAX CREDIT AND DEDUCTION OF POLITICAL CONTRIBUTIONS

**74. Q. Can my constituents deduct the amount of their contributions to my campaign fund?**

A. No tax deduction or credit is allowed for any political contribution.

## CAMPAIGN EXPENSES

**75. Q. Are my campaign expenses deductible for tax purposes?**

A. Any campaign expenditures out of your 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, none of a candidate's campaign expenses are deductible. Regardless of the result of the election, you cannot deduct expenses for attending political conventions, contributions to the political party that sponsored your candidacy, expenses of campaign travel, campaign advertising, the expenses of successfully defending your 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 holding a political office may be viewed as a stepping stone to some other business or profession, this does not cause the expenses incurred during a political campaign to be deductible. Thus, political campaign expenses are not deductible by a lawyer seeking election as a legislator in the hope that the exposure will build his professional practice. Likewise, even though a candidate felt that his professional reputation was damaged during a political campaign, he cannot deduct the cost of any defamation litigation for allegations published during the campaign.

## MARYLAND INCOME TAX

76. **Q. Are all of the business related expenses discussed previously, deductible on my Maryland income tax return?**
- A. Since Maryland income tax is based upon the income developed for federal purposes with only certain modifications, most of your business related expenses would be deductible on your Maryland income tax return to the same extent as on your federal income tax return. However, there is one exception related to the federal depreciation rules. Maryland continues to follow the depreciation rules in place prior to the passage of the 2002 and 2003 federal changes. Under federal law, accelerated deductions related to federal bonus depreciation and the increased amounts of asset expensing under Section 179 of the Internal Revenue Code have not been adopted for Maryland tax purposes. You should consult your Certified Public Accountant for guidance in your situation.
77. **Q. Are there any business related items I can deduct on my Maryland return that I could not deduct on my federal income tax return?**
- A. Maryland allows an additional deduction, called a “subtraction from income,” for the costs of caring for your dependents while you work, including your work in the General Assembly. This is an item that is not a deduction on your federal return. (However, the federal rules allow for the use of child care expenses in calculating a federal tax credit, i.e., a direct reduction of your tax expense.) The Maryland subtraction amount is limited to \$3,000 for one (or \$6,000 for two or more dependents receive care). To claim this subtraction you must attach federal Form 2441 or federal Form 1040 A Schedule 1 to your Maryland return.
78. **Q. Have there been any law changes that will affect my 2006 Maryland return?**
- A. Nothing of relevance for 2006.

### What you need to know about Maryland’s Sales and Use Tax

Maryland’s 5% sales and use tax applies to all taxable tangible property that you use in Maryland, no matter where you bought it. If you are ordering from an out-of-state vendor, tangible personal property to be delivered into Maryland by the U.S. mail, telephone or the Internet, you may be subject to the Maryland use tax.

Certain services such as cleaning of commercial buildings, security services and the performance of background and credit checks are also subject to Maryland sales and use tax.

If you contract for taxable services or purchase tangible personal property for use in Maryland and tax does not appear on the invoice, you would be expected to accrue and remit Maryland use tax of 5% to the state. To learn more about Maryland use tax obligations and forms, call Taxpayer Services at 410-767-1300 (Baltimore area) or 800-492-1751 (outside Baltimore). You can also visit the Maryland Comptroller’s Web site at <http://www.marylandtaxes.com>.

