

Summary of Combat Zone Tax Benefits



If you are a member of the U.S. Armed Forces who serves in a combat zone (defined below), you can exclude certain pay from your income when determining your taxes as well as postpone certain tax related actions during and following your service in the combat zone. The following is a summary of combat zone tax exclusions (CZTE). IRS Publication 3, *Armed Forces' Tax Guide*, can provide additional information. These rules DO NOT apply to DoD or non-DoD civilian personnel, nor for members of the Merchant Marine, Public Health Service or other uniformed services. Coast Guard members **do** qualify.

What Can be Excluded

Enlisted personnel, warrant officers, and commissioned warrant officers can exclude **all** normally taxable pays from their income during months of service in a combat zone.

Commissioned officers can exclude the amount of **\$6875.10** per month of normally taxable pays. This amount is the highest enlisted pay grade (MCPON's pay for Navy) plus the **\$225** imminent danger or hostile fire pay for a total of **\$7100.10** per month. Note that tax-free allowances (BAH/BAS, etc.) continue to be tax-free for all military personnel and do not factor into the officer pay cap exclusion.

Excludable income includes:

- Active duty pay earned in any month you served in a combat zone

- Imminent danger/hostile fire pay
- A reenlistment bonus if the voluntary extension or reenlistment occurs in a month you served in a combat zone.
- Pay for accrued leave earned in any month you served in a combat zone. The DoD must determine that the unused leave was earned during that period.
- Pay received for duties as a member of the Armed Forces in clubs, messes, post and station theaters, and other non-appropriated fund activities. The pay must be earned in a month you served in a combat zone.
- Awards for suggestions, inventions, or scientific achievements you are entitled to because of a submission you made in a month you served in a combat zone.
- Student loan repayments that are attributable to your period of service in a combat zone (provided a full year's service is performed to earn the repayment).

One Day = One Month Rule. If you serve in a combat zone for one or more days in any month, you are entitled to an exclusion for that entire month.

W-2's. DFAS is charged with accounting for CZTE amounts and reports them to you on your W-2. The wages shown in box 1 of your Form W-2 should not include military pay excluded from your income under the combat zone exclusion provisions. If it does, you will need to get a corrected Form W-2 from your finance office. CZTE amounts are shown on your W-2 in box 12 as a "Q" amount. You cannot exclude as combat pay any wages shown in box 1 of Form W-2. The IRS does not permit "pen and ink" changes to W-2's! But you can file a return with the erroneous W-2 to get your refund, and then file an amended return later when you get a corrected W-2.

Definition of Combat Zone

A combat zone is any area the President of the United States designates by Executive Order as an area in which the U.S. Armed Forces are engaging or have engaged in combat. Certain areas in the Balkans region have been declared by Congress in a Public Law as "Qualified Hazardous Duty Areas" or QHDAs, which have the same tax benefits as combat zones.

Designated Combat Zones

Afghanistan, the Persian Gulf area (including Iraq, Kuwait, Saudi Arabia, Oman, Bahrain, Qatar, UAE, as well as the Persian Gulf, Gulfs of Aden and Oman, Red Sea, and parts of the Arabian Sea), and certain areas in the Balkans region are currently designated as CZs or QHDAs. Specific locations are listed in Publication 3.

Serving in a Combat Zone

- Service in a combat zone includes any periods you are absent from duty because of sickness, wounds, leave, or TAD/TDY, unless leave, TAD/TDY includes the full calendar month.
- If, as a result of serving in a combat zone, a person becomes a prisoner of war or is missing in action, that person is considered to be serving in the combat zone so long as he or she keeps that status for military pay purposes.
- You are considered to be serving in a combat zone if you are either assigned on official temporary duty to a combat zone or you qualify for hostile fire/imminent danger pay while in a combat zone.
- There are special rules for hospitalization related to CZ injuries. See Publication 3.

Non-Qualifying Presence in Combat Zone

The following military service does not qualify as service in a combat zone:

- Presence in a combat zone while on leave from a duty station located outside the combat zone,
- Passage over or through a combat zone during a trip between 2 points that are outside a combat zone, and
- Presence in a combat zone solely for your personal convenience.

Qualifying Service Outside Combat Zone [“In Direct Support”]

Military service outside a combat zone is considered to be performed in a combat zone if:

- The service is in direct support of military operations in the combat zone, **and**
- The service qualifies you for special military pay for duty subject to hostile fire or imminent danger.

“In Direct Support” designation is made by DoD and military pay received for this service will qualify for the combat zone exclusion if the designation is made **and only if** you receive IDP or HFP.

Other Combat Zone Tax Benefits

Filing and Payment of Taxes Extension.

The deadline for filing tax returns, paying taxes, filing claims for refund, and taking other actions with the IRS is automatically extended if you are serving in a combat zone/QHDA or are considered “in direct support.” These rules apply to your stateside spouse as well, if you will be filing a joint return.

The duration of this extension can be a bit complicated to calculate but put simply it is:

1. The duration of your service in the combat zone (or while hospitalized due to injuries received in the combat zone); plus
2. 180 days after you leave the combat zone; plus
3. The number of days that you had to take the action (e.g., file the return) when you entered the combat zone.

If for example, you entered the combat zone on April 1st, your tax return was due on April 15th. But you can add to your time in 1. and 2. above the 15 days that you had left to file the return on time. If you entered the combat zone on December 25th, you can add 105 days (1 January to 15 April) to the other extension times.

Publication 3 and the IRS web site have other examples.

Note: Just because you can extend the filing of your tax return does not make it a good idea! If you are due a refund, Uncle Sam will pay you a modest interest rate on returns filed under these provisions, but wouldn't you rather have the money now? File when you are able to, rather than waiting until years later. It will make things much simpler!

Signing of Returns.

The non-military spouse can file a joint return without the necessity of the service member's signature. This can be done by use of an IRS power of attorney (Form 2848), a military power of attorney that authorizes tax actions, or by simply submitting a signed statement indicating that the spouse is currently serving in a combat zone. These returns can be e-filed, but the tax preparer will need to attach the power of attorney or signed statement to a Form 8453 and send it to IRS.

Earned Income Tax Credit Qualification.

Servicemembers who may qualify for the EITC except for the fact that they have little or no earned income due to the CZ income exclusion, can now make an election on their tax return to consider otherwise excluded pay as taxable **solely** for EITC purposes. The W-2 box 12, Q amount is used instead of box 1, gross income. This election does not increase taxes owed and will almost always mean a larger refund.

Special Rules for IRAs, TSP Contributions, and Reserve Personnel.

Publication 3 has very helpful information on combat zone tax benefits related to these topics and should be consulted early and often. Reserve personnel receiving compensation from their civilian employer (“differential pay”) in particular need to consult Pub 3 to ensure they understand their tax liability.

Questions regarding combat zone tax benefits can be addressed to your local military tax center, your Unit Tax Advisor, or a JAG legal assistance attorney. The IRS web page at www.irs.gov also has a wealth of information for military taxpayers including a very useful Q&A section that may address your particular issue.



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