State Taxation of Active-Duty Servicemembers' Personal Income
by Jessica Lynn Clark

Jessica Lynn Clark, a student at The George Washington University School of Law, reviews the states’ tax treatment of active-duty servicemembers’ income; she considers whether it is fair to give servicemembers special treatment.

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I. Introduction

Active-duty members of the U.S. armed forces receive both taxable and nontaxable compensation -- base pay, which is generally taxable, and a variety of other payments, including basic housing allowances and basic subsistence allowances, which are not taxable.1 In addition to these general distinctions, servicemembers are generally provided with special tax treatment, under both the federal tax system and many state tax systems.2 With the federal Soldiers’ and Sailors’ Civil Relief Act, Congress provided for special tax treatment for servicemembers in several ways.3 First, a servicemember's tax liability can be "deferred for a period not more than 180 days after termination of or release from military service, if a servicemember's ability to pay such income tax is materially affected by military service."4 No penalties or interest apply to these authorized deferments.5 Second, for servicemembers serving in combat zones or contingency zones, any military compensation earned while in the zone is exempt from income tax.6 Furthermore, federal statute provides for 180-day automatic filing and payment extensions to servicemembers serving in combat zones or contingency zones.7 For these servicemembers, the 180-day extension begins when the servicemember has completed service in the applicable zone or when the servicemember is released from hospitalization that resulted from service in one of those zones.8

The act also provides for how to determine a servicemember's residence for state tax purposes. Under the act, servicemembers do not "lose nor acquire a residence or domicile for purposes of taxation with respect to the person, personal property, or income of the servicemember by reason of being absent or present in any tax jurisdiction of the United States solely in compliance with military orders."9 Thus, no matter where stationed, servicemembers maintain their original residence, or home of record, unless the required steps are taken to officially change residence. The required steps may differ by state, but Maryland offers a typical list of steps.10 First, the servicemember must "intend to establish new residence in a specific jurisdiction."11 Second, the servicemember must move away "from the previously held jurisdiction."12 Third, the servicemember must "establish a new, permanent place of abode in the new jurisdiction."13 Finally, the servicemember must update his or her service record by completing a Form DD 2058.14

Furthermore, military compensation "for military service shall not be deemed to be income for services performed or from sources within a tax jurisdiction of the United States if the servicemember is not a resident or domiciliary of the jurisdiction in which the servicemember is serving in compliance with military orders."15 That means that servicemembers have state personal income tax liability for military compensation solely in their home state of record, and that nonresident states cannot use a servicemember's military compensation in calculating the amount of state tax due to the nonresident state.16

In addition to these federal statutory rules, most states have special policies and rules for servicemembers regarding personal income tax. These rules are discussed below. In discussing the state tax policies toward servicemembers, this report is separated into two main parts. First, I will provide a brief summary of each state's treatment of servicemembers' personal income. Second, I will discuss some of the policy issues regarding servicemembers' special tax treatment.

II. State by State

Alabama

Resident servicemembers are subject to Alabama income tax on personal income, regardless of its source and regardless of
where the servicemember was stationed during the tax year.\textsuperscript{18} If a servicemember is not a legal resident of Alabama but is stationed within Alabama, Alabama does not tax the servicemember's military compensation.\textsuperscript{19} However, Alabama does require nonresident servicemembers to pay state income tax on any "earned income from Alabama sources other than military pay," subject to minimum reporting requirements.\textsuperscript{20} Alabama does not provide any special filing or payment extensions to servicemembers who are required to file Alabama tax returns, but it does allow extensions to all taxpayers up to six months.\textsuperscript{21} Even if granted, these extensions do not apply to the due date for tax liability and penalties and interest may be applied to any tax liability.\textsuperscript{22}

Alaska

Alaska has no personal income tax.

Arizona

Arizona requires servicemembers who are legal residents of Arizona to pay state income tax on all income earned, regardless of its source and regardless of where the servicemember was stationed during the tax year.\textsuperscript{23} Also, servicemembers who are not legal residents of Arizona but are stationed within Arizona are subject to Arizona income tax on any nonmilitary income earned or received from Arizona sources, but are not subject to Arizona income tax on military compensation. Arizona also has provisions that allow extensions for both filing and payment without penalties or interest when a servicemember is stationed overseas or when "it is impossible or impractical to file or pay Arizona taxes by reason of being outside the country." Up to two extensions are possible, giving the servicemember up to October 15 of the year filing is required. For a waiver of interest or penalties, a servicemember must write to the Arizona Department of Revenue to request the waiver and justify the request.

Arkansas

Arkansas resident servicemembers are subject to Arkansas income taxes regardless of the source of income and regardless of where the servicemember was stationed during the tax year, but Arkansas allows servicemembers to subtract from taxable income the first $6,000 of military compensation.\textsuperscript{24} For servicemembers stationed within Arkansas who are not legal residents of Arkansas, the state does not tax military compensation.\textsuperscript{25} Arkansas does, however, tax any income received from Arkansas sources "while [] stationed in Arkansas, including [] pay from nonappropriated funds: i.e., exchange, clubs, commissary, etc."\textsuperscript{26} Arkansas allows only extensions that the IRS allows, and any extensions are for filing only. Therefore, even if servicemembers have valid extensions for filing, they may be subject to penalties and interest on any tax liability.

California

Servicemembers who are California residents with a permanent home in California and are stationed in California are subject to California income tax on all income, regardless of its source.\textsuperscript{27} Thus, for California resident servicemembers stationed outside California, military compensation is not subject to California income tax. California treats residents stationed outside California as nonresidents for tax purposes and they are taxed only on income from California sources. For nonresidents stationed within California, military compensation is not subject to California income tax, but any other California-source income earned or received is subject to California income tax.

Colorado

For tax purposes, Colorado treats servicemembers who are legal residents of Colorado "in the same manner as any other Colorado resident," which means resident servicemembers are subject to income tax on all income, regardless of its source.\textsuperscript{28} Colorado does provide a special exception for servicemembers who are legal residents of Colorado and "spend [] at least 305 days of the tax year outside of the 50 state boundary of the United States of America while stationed outside of the United States of America for active military duty" by treating those servicemembers as nonresidents for tax purposes. This treatment exempts from taxation the resident servicemember's military compensation as well as any other income not earned or received from a Colorado source.\textsuperscript{29}

Nonresident servicemembers stationed within Colorado are not subject to Colorado income tax, but nonresident servicemembers stationed in Colorado who earn income from Colorado sources are subject to Colorado income tax on that income. The specific sources of income subject to tax include nonmilitary Colorado salaries, wages, tips, and commissions; Colorado business income; and "income from rents, royalties and/or gains from the sale of tangible personal property or real property located in Colorado." The nonresident servicemember is not taxed by Colorado on interest or dividend income, regardless of source.

Connecticut

Servicemembers who are residents of Connecticut are subject to Connecticut income tax on all income, regardless of its source. Resident servicemembers may file as nonresidents if they meet certain exceptions. To qualify for the "Group A Exception," the servicemember must not have had "a permanent place of abode in Connecticut for the entire taxable year"; must have
"maintained a permanent place of abode outside Connecticut for the entire taxable year"; and must have "spent a total of 30 days or less in the aggregate in Connecticut during the taxable year." Servicemembers who meet these exceptions are treated as nonresidents for tax purposes and their military compensation is not subject to Connecticut income tax. To qualify for the "Group B Exception," a servicemember must have, during "any period of 548 consecutive days," been "present in a foreign country (or countries) for at least 450 days. During that 548-day period, the servicemember must not have been "present in Connecticut for more than 90 days" and must not have a "permanent place of abode in Connecticut." Also, the servicemember's presence in Connecticut is limited by a calculation based on the "number of days contained in the nonresident portion of the taxable year." Servicemembers who meet the Group B Exception may file as nonresidents and their military compensation is not subject to Connecticut income tax. Connecticut does not tax the military compensation of nonresident servicemembers stationed within Connecticut. If, however, the nonresident servicemember has Connecticut-source income, including nonmilitary wages earned from a Connecticut business and income earned from property in Connecticut, he or she must pay Connecticut state income tax.

In addition to the federal combat zone extensions, Connecticut also allows extensions for servicemembers serving in areas other than combat zones, but these extensions are only for filing and servicemembers must provide full payment of the tax due at the original due date. Also, Connecticut allows servicemembers to file tax returns up to three years late in order to receive an income tax refund.

**Delaware**

Servicemembers who are residents of Delaware are subject to Delaware income tax on military compensation and all other income, regardless of the source and regardless of where they were stationed during the tax year. Nonresident servicemembers stationed within Delaware are not subject to Delaware income tax on their military compensation, but they are subject to Delaware income tax for any income earned in Delaware. Delaware does not provide a special extension to servicemembers, but allows all taxpayers to apply for an extension ending August 15 of the year the tax return is due. The extension is for filing only and there may be penalties and interest applied to any tax liability.

**Florida**

Florida has no personal income tax.

**Georgia**

Servicemembers who are residents of Georgia are subject to Georgia income tax on all income, regardless of the source of income and regardless of where they were stationed during the tax year. Nonresident servicemembers stationed within Georgia are not subject to Georgia income tax on their military compensation, but may be subject to Georgia income tax for any "earned income from Georgia sources other than military pay." Resident servicemembers stationed overseas receive an automatic six-month extension for filing and no interest or penalties apply during the extension period. The six-month extension period begins when the servicemember returns to the continental United States.

**Hawaii**

For servicemembers who are legal residents of Hawaii, all income including military compensation and "income from sources in Hawaii and outside Hawaii" is subject to Hawaii income tax, regardless of where the servicemember was stationed during the tax year. For a nonresident servicemember stationed within Hawaii, "any income which is not related to the military duty" is subject to Hawaii state income tax. This excludes both military compensation and "income from intangibles," like savings account interest. Perhaps because of the particular attraction to servicemembers to retire in Hawaii, the state has a special provision for servicemembers who are "assigned to duty in Hawaii for 3 years," "will be discharged from military service in Hawaii," and "intend to establish residence in Hawaii upon discharge from the military." When servicemembers establish domicile in Hawaii, defined as "the place of an individual's true, fixed, permanent home and principal establishment and to which place the individual has the intention of returning whenever the individual is absent," they become legal residents of Hawaii and all income, regardless of source, is subject to Hawaii income tax. Hawaii does not provide any special extensions to servicemembers, but does provide an automatic four-month extension to all taxpayers.

**Idaho**

For servicemembers who are legal residents of Idaho and stationed in Idaho, all income, regardless of its source, is subject to Idaho tax. For Idaho resident servicemembers stationed outside Idaho, all income is "reportable," but "only military wages received while stationed in Idaho and all nonmilitary income, regardless of the source, will be subject to tax." Idaho also has a provision that allows a legal resident of Idaho to file as a "Special-Case Idaho Resident." A servicemember must meet all of the following requirements to qualify as a special case: "lived outside of Idaho for at least 445 days in a 15-month period"; "spent less than 60 days in Idaho during the year"; "did not have a personal residence in Idaho"; "did not claim Idaho as [his or her] federal tax home"; was "not employed on the staff of a U.S. senator or representative"; and "did not hold an elective or appointive office of the U.S. government other than the armed forces or a career appointment in the U.S. Foreign Service." Servicemembers who meet all of these requirements are treated as nonresidents and are required to file an Idaho income tax return only if "gross income from
Idaho sources exceeds $2,500." For servicemembers stationed within Idaho but not legal residents of Idaho, the state does not tax military compensation. If the servicemember has any nonmilitary income from Idaho sources, however, that income is subject to Idaho tax if the Idaho gross income is at least $2,501.

**Illinois**

Resident servicemembers stationed within Illinois are subject to Illinois income tax, but Illinois does not tax military compensation earned by servicemembers. A servicemember that is a resident of Illinois and was stationed outside of Illinois during the entire tax year, however, is "considered a nonresident for Illinois tax purposes," as long as the servicemember did not earn any Illinois-source income. Nonresident servicemembers stationed in Illinois, and resident servicemembers who are treated as nonresidents, are not subject to Illinois income tax unless they have nonmilitary Illinois-source income. Illinois does not have any special extensions for servicemembers, but all taxpayers can receive an automatic six-month extension for filing, and penalties and interest may apply.

**Indiana**

For resident servicemembers, all income is subject to Indiana tax, regardless of its source and regardless of where the servicemember was stationed during the tax year. Indiana also allows for a credit if the servicemember is subject to tax in both Indiana and the state where the servicemember is stationed. Indiana also provides that Indiana residents may deduct up to $2,000 of military compensation. For nonresident servicemembers stationed within Indiana, "all nonmilitary income received from Indiana sources" is taxable. Indiana allows an automatic 60-day filing extension for servicemembers stationed outside the United States or Puerto Rico. Servicemembers must provide a statement verifying that they were outside the United States or Puerto Rico on April 15.

**Iowa**

Servicemembers who are residents of Iowa are subject to Iowa income tax, regardless of the income source and regardless of where the servicemember was stationed during the tax year. Iowa does allow residents to receive a credit for tax paid to another state when the resident is required to file an income tax return in another state. Servicemembers who are not residents of Iowa but who are stationed in Iowa are required to file an Iowa income tax return only if they had Iowa-source income of $1,000 or more. Extensions are available to servicemembers, but they must pay at least 90 percent of the tax due as of April 30 in the year the tax is due in order to get the extension. If this is done, the deadline is automatically extended to October 31.

**Kansas**

Servicemembers who are residents of Kansas are subject to Kansas income tax on all income, regardless of its source and regardless of where the servicemember was stationed during the tax year. Nonresident servicemembers stationed within Kansas are subject to Kansas income tax only to the extent of any income earned from Kansas sources. There are no special extension provisions for servicemembers, but all taxpayers may request an extension. Extensions apply only to filing, and penalties and interest may apply to any tax liability.

**Kentucky**

Servicemembers who are Kentucky residents are subject to Kentucky income tax on all income, regardless of its source and regardless of where they were stationed during the tax year. For nonresident servicemembers stationed within Kentucky, Kentucky taxes all income from nonmilitary Kentucky sources. Kentucky also extends the federal combat zone extension to 12 months after the servicemember's combat zone duty is completed. For income tax due, however, interest may accrue from the original filing date, but servicemembers may pay at least 75 percent of the tax due by the original filing deadline to avoid a late-payment penalty.

**Louisiana**

For Louisiana-resident servicemembers, all military compensation in addition to any other income, regardless of its source and regardless of where the servicemember was stationed during the tax year, is subject to Louisiana personal income tax. However, Louisiana provides a credit for tax paid to another state by a servicemember, as long as the income is included on the Louisiana tax return. Louisiana also allows for an exemption of up to $29,999 of military compensation to servicemembers stationed outside of Louisiana for at least 120 consecutive days. Servicemembers who are not residents of Louisiana but who are stationed within Louisiana are subject to income tax only on any nonmilitary Louisiana-source income.

**Maine**

Servicemembers who are residents of Maine are subject to tax on all income, regardless of its source and regardless of where the servicemember was stationed during the tax year. Nonresident servicemembers stationed within Maine are subject to Maine
personal income tax for any income earned from nonmilitary Maine sources, not including interest and dividends received. Maine does not have any special extensions for servicemembers, but gives all taxpayers an automatic six-month extension. The extension is only for filing and the taxpayer must pay at least 90 percent of total tax liability by April 15 to avoid a penalty and interest.

Maryland

Maryland resident servicemembers are subject to Maryland income tax for all income earned or received, regardless of its source and regardless of where the servicemember is stationed. However, Maryland allows residents to "subtract up to $15,000 in military pay earned outside the U.S. boundaries or possessions, depending on the individual's total income." Nonresident servicemembers stationed within Maryland are not subject to tax on military compensation, but are subject to tax for any "income that was derived from any real or personal property that is located in Maryland as well as nonmilitary income earned in Maryland including income from Maryland lottery prizes."

Massachusetts

Servicemembers who are Massachusetts residents are subject to Massachusetts income tax on all income, regardless of its source and regardless of where the servicemember was stationed during the tax year. Massachusetts also addresses the possibility that a servicemember stationed in another state may have income subject to tax in two jurisdictions. In that situation, Massachusetts provides "a credit for taxes paid to the other jurisdiction." Nonresident servicemembers stationed in Massachusetts are subject to Massachusetts income tax only to the extent that they earn any nonmilitary Massachusetts-source income.

Michigan

Servicemembers who are residents of Michigan are subject to Michigan income tax on certain types of income, regardless of where the servicemember was stationed, but Michigan does not tax military compensation. Nonresidents stationed within Michigan are subject to Michigan income tax on any Michigan-source income.

Minnesota

For Minnesota residents stationed within Minnesota, all military compensation and other income, regardless of source, is subject to Minnesota income tax. Minnesota treats resident servicemembers stationed outside of Minnesota as nonresidents for tax purposes for the period of time they were stationed outside Minnesota. That means that all military compensation earned while stationed outside Minnesota is not subject to Minnesota income tax, but other types of nonmilitary Minnesota-source income may be subject to tax. Nonresidents stationed within Minnesota are subject to Minnesota income tax only for Minnesota-source income. In addition to the federal combat zone extension, Minnesota allows an extension for servicemembers stationed outside the United States, but who were not stationed in a combat zone. Those servicemembers have until October 15 to file, but penalties and interest may accrue on any tax liability not paid by April 15.

Mississippi

Mississippi resident servicemembers are subject to tax on all income earned, including military compensation, regardless of its source and regardless of where they were stationed during the tax year. For nonresidents stationed within Mississippi, servicemembers are subject to Mississippi personal income tax only to the extent of any income earned from Mississippi sources.

Missouri

For servicemembers who are residents of Missouri, all income regardless of source is subject to Missouri income tax. Missouri does allow servicemembers stationed outside of Missouri to be treated as nonresidents for tax purposes, as long as they "maintained no permanent place of abode in Missouri during the tax year"; "maintain[ed] a permanent place of abode elsewhere; and spent 30 days or less in Missouri during the year in which they are filing." If servicemembers meet all three requirements, their military pay is not subject to Missouri income tax. For nonresident servicemembers stationed within Missouri, military compensation is not subject to Missouri income tax, but any Missouri-source income earned while in Missouri is subject to Missouri income tax.

Montana

For Montana resident servicemembers, regardless of where they are stationed, Montana does not tax "basic, special, and incentive pay received for serving on active duty as a member of the regular Armed Forces." Any other income, regardless of source, is subject to Montana income tax. Nonresident servicemembers stationed within Montana are subject to Montana income tax only to the extent that the servicemember has any Montana-source income. Montana does not provide any special extensions to servicemembers, but all taxpayers may apply for an extension of up to six months. These extensions, however, are for filing
only, and penalties and interest may accrue on any tax liability.

Nebraska

Resident servicemembers, regardless of where they were stationed during the tax year, are subject to Nebraska income tax on all income, regardless of source. However, Nebraska allows a credit for income tax paid in another state. Nonresident servicemembers who are stationed in Nebraska are subject to Nebraska income tax only to the extent that they have Nebraska-source income.

Nevada

Nevada has no personal income tax.

New Hampshire

New Hampshire has no personal income tax on reported W-2 wages.

New Jersey

New Jersey resident servicemembers are subject to income tax on all income earned, regardless of source. New Jersey resident servicemembers may qualify for tax treatment as nonresidents if the servicemembers "did not maintain a permanent home in New Jersey"; "maintain[ed] a permanent home outside of New Jersey"; and spent 30 days or less in New Jersey during the tax year. Also, New Jersey resident servicemembers who are American Indians are exempt from taxation on their military compensation. Nonresident servicemembers stationed within New Jersey are subject to New Jersey tax only on income received from New Jersey sources. New Jersey allows an automatic extension for a servicemember who can't meet the April 15 deadline because of distance, injury, or hospitalization. To get the three-month automatic extension, servicemembers must include a written explanation with the tax return forms.

New Mexico

New Mexico resident servicemembers are subject to New Mexico income tax on all income, regardless of its source and regardless of where they were stationed during the tax year. New Mexico also has special rules for servicemembers who are enrolled members of an Indian nation, tribe, or pueblo. Military compensation for these enrolled members is exempt from taxation during "periods in which the member's home of record is on the lands of the member's Indian nation, tribe, or pueblo." Nonresident servicemembers stationed within New Mexico are not subject to New Mexico personal income tax for their military compensation, but are subject to New Mexico tax for any income earned from New Mexico sources. New Mexico allows servicemembers five types of extensions, including those allowed by the IRS. For each type of extension, there is no penalty, but the servicemember is required to pay interest on any tax liability.

New York

New York resident servicemembers are subject to New York income tax for military compensation and any other income. A New York resident servicemember, however, may be considered a nonresident for tax purposes if the servicemember "did not maintain any permanent place of abode in New York state during the tax year"; "maintained a permanent place of abode outside New York State during the entire tax year"; and "spent 30 days or less in New York State during the tax year." New York also allows resident servicemembers to file as nonresidents if the servicemember was in a foreign country for at least 450 days during any period of 548 consecutive days and spent 90 days or less in New York state during that 548-day period. The servicemember's presence in New York must be limited to the ratio that results from a calculation based on the number of days present during the nonresident portion of the tax year. New York does not tax any military compensation of nonresident servicemembers stationed within New York, but does tax any income received from a New York state source.

New York allows an automatic four-month filing extension to all taxpayers, and allows an additional two months for servicemembers stationed in a foreign country at the time of the filing deadline. Under the four-month extension, the due date for filing also extends the due date for payment of any New York state income tax liability, but interest accrues beginning April 15. Servicemembers can get the additional two months, with a final due date of August 15, but payments are due by June 15. New York's Department of Taxation and Finance has the discretion to waive penalties on late returns if servicemembers include a statement of their active duty and an explanation of why the return was filed late. New York also has provisions allowing servicemembers to defer payment of back taxes. To get a deferral, servicemembers must "show that their ability to pay the back taxes has been materially impaired" and must already have received a tax bill or have an existing installment plan.

North Carolina

North Carolina resident servicemembers are subject to North Carolina income tax on all income, regardless of source and
regardless of where they were stationed during the tax year. For nonresident servicemembers stationed within North Carolina, the state does not tax any military compensation, but any income from a North Carolina source is subject to North Carolina income tax. North Carolina does not provide any special extensions to servicemembers, but all taxpayers can request extensions up to six months. Even if granted, extensions do not prevent penalties and interest from accruing on any tax liability.

North Dakota

North Dakota resident servicemembers are subject to North Dakota income tax for all income, regardless of its source and regardless of where they were stationed during the tax year. Nonresident servicemembers stationed within North Dakota are subject to North Dakota income tax only to the extent of any North Dakota-source income received or earned. Servicemembers who don't qualify for the federal statutory combat zone extension may request the general extension available to all taxpayers.

Ohio

Ohio resident servicemembers are subject to Ohio income tax on the servicemember's entire federal adjusted gross income, regardless of source and regardless of where the servicemember was stationed during the tax year. Ohio does, however, allow credit for income tax paid to another state. For nonresident servicemembers stationed within Ohio, income received or earned from Ohio sources is subject to Ohio income tax.

Oklahoma

Oklahoma resident servicemembers are subject to Oklahoma income tax on all income regardless of its source and regardless of where they were stationed during the tax year, except for any "income from real and tangible personal property located in another state, income from business activities in another state, or the gains/losses from the sales or exchange of real property in another state." Oklahoma allows a resident servicemember to exempt from tax the first $1,500 of taxable military compensation. Oklahoma also provides that a servicemember who is both a resident of Oklahoma and an American Indian is not subject to Oklahoma income tax on any of the servicemember's military compensation. The servicemember must have "resided within his tribe's 'Indian Country' at the time of entering the Armed Forces of the United States, and the member has not elected to abandon such residence." A nonresident servicemember stationed within Oklahoma is not subject to Oklahoma income tax for military compensation, but any income earned by performing other services in the state is subject to Oklahoma income tax. Oklahoma also allows for extensions for servicemembers who cannot file a timely tax return when the reason for the inability to file a timely return is that the servicemember is absent from the state while on active duty or is confined to a hospital.

Oregon

Oregon resident servicemembers are subject to Oregon income tax on all income regardless of its source, but servicemembers stationed outside Oregon may be able to file as nonresidents to avoid paying tax on military compensation. If an Oregon resident servicemember has no permanent residence in Oregon during any part of the tax year and has a permanent residence outside Oregon during the entire tax year, and spent fewer than 31 days in Oregon during the tax year, the servicemember may file as a nonresident. That special nonresident status means that the Oregon resident servicemember is subject to Oregon income tax only to the extent that the servicemember has income from Oregon sources. Nonresident servicemembers stationed within Oregon are not subject to Oregon income tax except on income from an Oregon source.

Oregon also provides for certain exemptions of military pay. Servicemembers may "subtract active duty pay earned anywhere outside of Oregon until the date the president sets as the end of combat zone activities." That exemption does not require that the servicemember be stationed within the combat zone, but only that the servicemember be on active duty when there is a presidentially declared combat zone. Also, Oregon allows servicemembers to "subtract up to $3,000 of active duty pay earned inside Oregon." Oregon does allow a servicemember qualified for both exemptions to take both exemptions; however, the exemptions "cannot be more than the total active duty pay included in federal AGI."

Pennsylvania

For resident servicemembers, Pennsylvania does not tax the military compensation earned while stationed outside Pennsylvania, but it does tax military compensation of servicemembers who are residents of Pennsylvania and are also stationed within Pennsylvania. Pennsylvania also taxes any other income received by a Pennsylvania resident, regardless of the income source. For nonresident servicemembers stationed within Pennsylvania, only Pennsylvania-source earned or received income is subject to Pennsylvania income tax. In addition to the federal combat zone extensions, servicemembers may apply for the four-to-six-month extension that is available to all Pennsylvania taxpayers.

Rhode Island

Rhode Island residents who are servicemembers are subject to Rhode Island income tax for all income, regardless of its source and regardless of where they are stationed. Nonresident servicemembers stationed within Rhode Island are not taxed on their
military compensation, but any income earned or received from Rhode Island sources is subject to Rhode Island income tax. Rhode Island does not provide any special extensions for servicemembers, but all taxpayers may receive at least a four-month extension, and penalties and interest may accrue for any tax liability.

**South Carolina**

For South Carolina resident servicemembers, all income regardless of source and regardless of where the servicemember was stationed during the tax year is subject to South Carolina income tax. Nonresident servicemembers stationed in South Carolina are not subject to South Carolina income tax for their military compensation, but are subject to South Carolina income tax for any other earned income from a South Carolina source.

**South Dakota**

South Dakota has no personal income tax.

**Tennessee**

Tennessee does not have a personal income tax.

**Texas**

Texas has no personal income tax.

**Utah**

Utah resident servicemembers are subject to Utah income tax on all income, regardless of source and regardless of where the servicemember is stationed. Utah allows resident servicemembers to credit income tax paid to another state. Nonresident servicemembers stationed within Utah are subject to Utah income tax only to the extent of any Utah-source income earned or received. Utah provides for an automatic extension of up to six months for resident servicemembers stationed outside the United States. Utah allows an additional extension of up to four months after the servicemember "return[s] to the United States or his discharge date, whichever is earlier." Although there is no penalty, interest accrues on any tax liability from the original due date.

**Vermont**

Vermont resident servicemembers are subject to Vermont income tax on all income, regardless of source. However, Vermont allows an exemption for any "military pay for full-time active duty with the armed services when the pay is earned outside of Vermont." Nonresident servicemembers stationed within Vermont are not subject to income tax on their military compensation, but may be subject to Vermont income tax on other income earned or received from Vermont sources.

**Virginia**

Resident servicemembers are subject to Virginia income tax regardless of where they are stationed and regardless of source of income, but Virginia allows servicemembers to deduct up to $15,000 of military basic pay as long as the servicemember was on extended duty for more than 90 days. The deduction is limited, however, so that "for every $1.00 of income over $15,000, the maximum subtraction is reduced by $1.00," and no deduction is allowed if the servicemember's basic military pay is $30,000 or more. Nonresident servicemembers stationed within Virginia are not subject to Virginia income tax on military compensation. Nonresident servicemembers are subject to tax, however, to the extent that they have any income from Virginia sources, not including interest earned on Virginia bank accounts. Virginia provides an automatic extension to July 1 for servicemembers stationed outside the United States and Puerto Rico. To get the extension, servicemembers must simply write "Overseas Rule" at the top of the tax return and attach an explanatory statement.

**Washington**

Washington has no personal income tax.

**West Virginia**

Resident servicemembers are subject to West Virginia income tax on all income, regardless of its source, unless the servicemember did not maintain a physical presence in West Virginia for more than 30 days during the tax year. Resident servicemembers who meet this condition are treated as nonresidents and may be subject to West Virginia income tax only to the extent that they have any West Virginia-source income. A nonresident servicemember stationed within West Virginia is not subject to West Virginia income tax on the servicemember's military compensation. The nonresident servicemember may, however, be subject to West Virginia income tax on any West Virginia-source income earned or received while stationed in West Virginia.
Wisconsin

Wisconsin resident servicemembers, no matter where they are stationed, are subject to income tax on all income, regardless of source. Also, Wisconsin provides that servicemembers may be eligible for a credit of up to $200 against Wisconsin income tax for military pay received while stationed outside the United States. Wisconsin also provides that resident servicemembers subject to another state income tax may receive a credit toward their Wisconsin income tax for tax paid to the other state. Nonresident servicemembers stationed within Wisconsin are not subject to Wisconsin income tax on their military compensation, but may be subject to Wisconsin income tax for any Wisconsin-source earned or received income, including winnings from Wisconsin lottery tickets and "winnings from a Native American casino or bingo hall located in Wisconsin."

Wyoming

Wyoming has no personal income tax.

District of Columbia

Resident servicemembers are subject to District of Columbia income tax on all income, regardless of its source and regardless of where they are stationed. The instructions for Form DC-40 state that an individual must file a D.C. individual income tax return if the person "lived in D.C. for 183 days or more during [the tax year], even if [the] permanent residence was outside D.C." This suggests that nonresident servicemembers stationed within the district are subject to D.C. income tax; however, according to federal statute, the district could tax only D.C.-source income, not the military compensation of a nonresident. The district does not provide any special extensions for servicemembers, but all taxpayers are eligible for an extension up to six months, and penalties and interest may accrue on any tax liability.

III. Policy Issues and Concerns

Reasons for giving servicemembers special tax treatment include recognition of and reward for the service they give to the United States; recognition of and an attempt to temper the relatively low pay; and to encourage people to join the armed forces. One way to evaluate state tax policies for servicemembers is to consider how the policies fit into the five principles of sound tax policy:

- it provides appropriate revenues;
- it's neutral;
- it's fair and equitable;
- it's easy and economical to administer; and
- it allows accountability.

Although I am neither advocating nor opposing the special tax treatment many states provide to servicemembers, these principles present some of the issues to consider in deciding whether the special tax treatment of servicemembers should continue, and whether special tax treatment should be extended to more states.

Provision of Appropriate Revenues

This principle holds that a state tax system "must raise the requisite revenue to pay for those services that the public demands." In the taxation of servicemembers, there are two points related to this principle. First, many states do tax servicemembers' military compensation and other income, which means that the states are receiving tax revenue from the servicemembers. Thus, servicemembers are contributing to the state's requisite revenue. Second, and more significant, is that servicemembers often are not stationed within their state yet still pay income tax to the state. For example, an active-duty Navy petty officer from North Dakota has little chance of being stationed in North Dakota, yet as long as he maintains residence in North Dakota, he will continue to pay North Dakota income tax. The fact that the servicemember is not in North Dakota, though, means that he or she is unable to take advantage of the services provided by North Dakota. Similarly, a servicemember stationed outside North Dakota is unlikely to demand North Dakota services. Therefore, although most states continue to raise part of their tax revenue through the taxation of servicemembers' military compensation, few to no public services may ever reach the servicemember stationed outside the state. That principle, therefore, supports special tax treatment for servicemembers.

Neutrality

The principle of neutrality holds that "taxes should have as little effect on market decisions as possible." In this context, neutrality means that servicemembers should not make residency decisions or requests for duty assignments based on state tax systems.

Decisions based on state taxation policies, however, are likely among servicemembers, especially considering that several states have no personal income tax and many others provide specific exemptions for military pay. Servicemembers may be motivated to seek an assignment in Texas or Florida, for example, in an effort to purchase a home and establish a new residence. Then, even if the servicemember continues in active duty, he or she will no longer be subject to personal income tax after successfully changing residency. In an informal survey of 61 active-duty servicemembers, 18 said they changed their residency in order to get
better tax treatment. All 18 changed their residency to a state without income tax or with an exemption for military compensation, and they responded that they changed their residencies to avoid paying state income tax. This clearly suggests that the servicemembers' market decisions were affected by the state tax systems. Thus, there is a strong argument, and at least some evidence, that servicemembers' special tax treatment fails to meet the principle of neutrality.

**Fair and Equitable**

Although the words "fair" and "equitable" can be difficult to define, there are at least two standards by which to measure this principle: horizontal equity and vertical equity. In terms of horizontal equity, this principle holds that all similarly situated taxpayers should be treated similarly. Whether special treatment of servicemembers' income meets the principle of horizontal equity depends on the state. There are definite horizontal equity issues with the states that exempt portions of a servicemember's military compensation, while a nonservicemember with a similar income amount does not receive the exemption. For states that tax servicemembers' income just as any other resident's income, there are fewer horizontal equity concerns. Even in those states, fairness and equity remain issues because servicemembers are not taxed on many of the monetary benefits they receive, like basic housing and food allowances. Those amounts are not included in a servicemember's taxable income, and therefore a nonservicemember within the state will never be treated exactly, or even close to exactly, as a servicemember is treated for tax purposes. Still, under a broader interpretation of fairness and equity, there is a good argument that it is fair to give servicemembers tax advantages that other taxpayers do not receive because of the sacrifices that servicemembers make for the good of the country. Also, even though there are some horizontal equity problems, most states have horizontal equity problems anyway, and additional problems in that context are not a compelling reason to eliminate the special tax treatment of servicemembers.

Regarding vertical equity, taxpayers should pay tax based on their ability to pay, as in "taxpayers should bear a greater burden of paying for government services as their income grows." This principle, although contested, supports special tax treatment for servicemembers because of the historically low pay compared with other similar private-sector jobs. Regressivity problems, however, are an issue because servicemembers' income is relatively low compared with similar private-sector jobs. With their lower income, servicemembers may "spend a larger percentage of their income on goods subject to tax than do high-income individuals." As with horizontal equity, vertical equity remains a problem for many state tax systems generally, and even if states abandoned the special tax treatment of servicemembers, that would not eliminate the fairness and equity problems.

**Easy and Economical to Administer**

This principle holds that there should be minimal administrative costs on the state government and on the taxpayer. In most states, the costs of compliance are probably the same for servicemember taxpayers as they are for any other taxpayer. In some states, however, the costs of compliance, even when the compliance is favorable to the servicemember taxpayer, may be high. The compliance costs may be higher for servicemembers because most servicemembers are not stationed in the state in which they are subject to tax on their military compensation. Although all state income tax forms and instructions are available online, not all servicemembers have Internet access, which could make it difficult for servicemembers to know or access the rules for their state. Also, servicemembers who are stationed overseas may have difficulty getting in touch with a person in the states if they have questions. Complications like these are dealt with, or at least attempted to be dealt with, via tax assistance sites available on many military installations both in the United States and overseas. The tax assistance centers, however, are generally set up to provide only federal income tax assistance, and servicemembers may be on their own in figuring out complicated state tax forms. Thus, the states that have no personal income tax are the best at meeting this easy and economical goal, while servicemember residents of other states with personal income tax may have compliance challenges. Servicemembers may also be responsible for paying income tax to a nonresident state, which could present additional compliance challenges. Still, even though some of the state tax rules may be complicated, most of the complications are due to the state's favorable treatment of servicemember taxpayers, and therefore, it is in the taxpayer's best interests to learn and follow the state rules.

**Accountability**

The principle of accountability requires a state to "ensure[ ] that those charged with the administration and enforcement of the tax laws are performing their duties efficiently and fairly." Accountability also requires state governments to enforce their tax laws by collecting taxes and by having an open, transparent tax policy. Accountability, although no doubt an issue for many states, is not really an issue for servicemember taxation. Most special rules for servicemembers follow the federal taxation rules, and it is unlikely that state lawmakers are making secret deals with servicemembers to give them special benefits, compared with the likelihood of special tax breaks to encourage a corporation to move to a particular state location. One area of accountability that could implicate servicemember taxation issues is that states should continue to "review existing laws and determine whether they are serving the needs of the citizens." This presents the question of whether it is good policy to tax a servicemember's income in order to increase the state revenue to satisfy the public's needs, when the servicemember may be in Japan or even just across the country in another state, where he is unable to take advantage of any of the state benefits for which he is paying taxes. This is an interesting question because it does not seem likely that lawmakers would want to completely exempt resident servicemembers serving outside the state, although some states do that, because that means a decrease in tax revenue for the state. However, from a practical standpoint, it does not seem fair that servicemembers should be required to pay taxes to support services they may never be able to take advantage of. Lawmakers should rethink the rules of taxation of servicemembers serving
outside their state to determine whether such taxation meets the goals of sound tax policy.

**IV. Conclusion**

Even though special tax treatment for active-duty servicemembers does not fully satisfy all of the principles of sound tax policy, the tax benefits are generally designed to compensate the servicemembers for their service to the United States and meet the goals of the federal Soldiers’ and Sailors’ Civil Relief Act. Also, from a political perspective, lawmakers are not likely to find much support for taking away benefits currently provided to servicemembers. If anything, lawmakers in states that currently have neutral treatment of servicemember taxpayers might be pressured to consider adding special tax treatment in their states. Thus, even though special tax treatment may not satisfy the principles of sound tax policy, these types of state tax policies are likely to continue.

<table>
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<tr>
<th>Most Favorable</th>
<th>(No Personal Income Tax)</th>
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<tbody>
<tr>
<td>Alaska</td>
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<td>Wyoming</td>
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<tr>
<th>Favorable*</th>
<th>(Special Exemptions, Subtractions, Deductions, or Extensions)</th>
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</thead>
<tbody>
<tr>
<td>Arizona</td>
<td>(filing and payment extension)</td>
</tr>
<tr>
<td>Arkansas</td>
<td>(first $6,000 of military compensation exempt from taxation)</td>
</tr>
<tr>
<td>California</td>
<td>(military compensation exempt unless servicemember has a permanent residence in California and is stationed in California)</td>
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<tr>
<td>Colorado</td>
<td>(treatment as nonresidents under certain conditions that exempts both military compensation and other non-Colorado income)</td>
</tr>
<tr>
<td>Connecticut</td>
<td>(treatment as nonresidents under certain conditions that exempts both military compensation and other non-Connecticut income)</td>
</tr>
<tr>
<td>Georgia</td>
<td>(filing and payment extension)</td>
</tr>
<tr>
<td>Idaho</td>
<td>(treatment as nonresidents under certain conditions that exempts both military compensation and other non-Idaho income)</td>
</tr>
<tr>
<td>Illinois</td>
<td>(military compensation is exempt from taxation)</td>
</tr>
<tr>
<td>Indiana</td>
<td>(up to $2,000 military compensation is exempt from taxation)</td>
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<tr>
<td>Iowa</td>
<td>(filing extension)</td>
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<tr>
<td>Kentucky</td>
<td>(filing extension)</td>
</tr>
<tr>
<td>Louisiana</td>
<td>(taxation exemption up to $29,999 of military compensation)</td>
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</table>
Maryland (taxation exemption up to $15,000 of military compensation)

Michigan (military compensation is exempt from state taxation)

Minnesota (treatment as nonresidents under certain conditions that exempts both military compensation and other non-Minnesota income; filing extension)

Missouri (treatment as nonresidents under certain conditions that exempts both military compensation and other non-Missouri income)

Montana (military compensation is exempt from state taxation)

New Jersey (treatment as nonresidents under certain conditions that exempts both military compensation and other non-New Jersey income; military compensation is exempt from taxation for Native Americans; filing extension)

New Mexico (military compensation is exempt from state taxation for enrolled members of an Indian tribe; penalty-free filing and payment extension)

New York (treatment as nonresidents under certain conditions that exempts both military compensation and other non-New York income; filing extension)

Oklahoma (taxation exemption of first $1,500 of military compensation; military compensation is exempt from taxation for American Indians; filing extension)

Oregon (exemption up to $3,000 for military compensation earned within Oregon; exempts all military compensation when there is an existing combat zone; treatment as nonresidents under certain conditions that exempts military compensation and other non-Oregon income)

Pennsylvania (exemption for military compensation earned while stationed outside of Pennsylvania)

Utah (filing extension)

Vermont (exemption for military compensation earned while stationed outside of Vermont)

Virginia (exemption up to $15,000 of military compensation)

West Virginia (treatment as a nonresident under certain conditions that exempts both military compensation and other non-West Virginia income)

Wisconsin (up to $200 tax credit for servicemembers who were stationed outside the United States)

Neutral**
(No Special Treatment for Servicemember Taxpayers)

Alabama

Delaware

Hawaii

Kansas

Maine

Massachusetts

Mississippi
Nebraska
North Carolina
North Dakota
Ohio
Rhode Island
South Carolina
District of Columbia

*From the perspective of the servicemember taxpayer. These benefits are in addition to any federal statutory benefits and benefits to a servicemember from nontaxable payments, such as the housing allowance.

**Neutral only in terms of state tax policies. These servicemembers still receive the federal income tax benefits and corresponding impact on state income tax returns by excluding certain income from the federal income tax return.

FOOTNOTES

1 Government Accountability Office, "Active Duty Military Compensation and Its Tax Treatment," GAO-04-72IR (2003), at 1-2; see also id. at 9-10.

2 In this report, I will limit my discussion to the tax treatment of full-time active-duty single servicemembers.

3 Soldiers' and Sailors' Civil Relief Act -- Amendment, Pub. L. No. 108-189, section 2, 117 Stat. 2835 (2003). The purposes of the act are as follows:

   (1) to provide for, strengthen, and expedite the national defense through protection extended by this Act to servicemembers of the United States to enable such persons to devote their entire energy to the defense needs of the Nation; and (2) to provide for the temporary suspension of judicial and administrative proceedings and transactions that may adversely affect the civil rights of servicemembers during their military service. Id.

4 Soldiers' and Sailors' Civil Relief Act -- Amendment section 510.

5 Id.

6 IRC section 112; see also IRS, "Military Pay Exclusion -- Combat Zone Service," at http://www.irs.gov/newsroom/article/0, id=101262,00.html. An exclusion like this generally applies automatically to states because income tax returns usually start with a taxpayer's federal adjusted gross income. If the income was excluded in the federal return, it is therefore automatically excluded in the state return, unless otherwise provided by the state. Unless otherwise noted in Part II, all states with income tax follow these federal guidelines on servicemembers serving in a combat or contingency zone.


8 IRC section 7508.

9 Soldiers' and Sailors' Civil Relief Act -- Amendment section 511(a).


11 Id.
12 Id.
13 Id.
14 Id.
15 Soldiers' and Sailors' Civil Relief Act -- Amendment section 511(b).
16 Id.
17 See table on pages 608-609 for a brief state-by-state breakdown.
19 Id.
20 Id.
22 Id.
25 Id.
26 Id.
Ill. Department of Revenue, “Filing Requirements for Military Personnel,” Publication 102, at 1-2, http://www.revenue.state.il.us/publications/pubs/pub-102.pdf. Military compensation not taxed includes military compensation received during basic training, compensation received for Reserve duty or an Illinois National Guard unit, including ROTC, and compensation for duty as a cadet or midshipman at certain military academies. Id. at 2.


Iowa Department of Revenue, "Iowa Tax Responsibilities of Military Personnel," at http://www.state.ia.us/tax/1040EI/GenInfo/04Military.html.


2004 Maine Resident Nonresident or Part-Year Resident Individual Income Tax Booklet, supra note 45, at 5.


Id. This subtraction is allowed only if the servicemember’s total military pay is $30,000 or less. Comptroller of Maryland, Overseas Pay, at http://individuals.marylandtaxes.com/incometax/military/overseas.asp.


58 Id. The servicemember must file a sworn statement of this information. Id.


63 N.M. Taxation and Revenue, General Information, at 1, http://www.state.nm.us/tax/forms/year03/2004PIT1INST.pdf.


67 N.C. Department of Revenue, Active Military, at http://www.dor.state.nc.us/taxes/individual/military.html.

68 N.C. Department of Revenue, Extensions, at http://www.dor.state.nc.us/taxes/individual/extension.html.


72 Okla. Tax Commission, Income Tax: Military FAQs, at http://www.oktax.state.ok.us/faq.html#Incomepercent20Tax: percent 20 percent 20Military percent 20FAQs.


74 Okla. Tax Commission, Income Tax: Military FAQs, supra note 72.

75 Oregon Department of Revenue, Military Personnel Filing Information, at http://egov.oregon.gov/DOR/PERTAX/IC-101-


D.C. Office of Tax and Revenue, 2004 D-40 Individual Income Tax Forms and Instructions, supra note 86.


Id. at 15.

With assistance from my husband Jeremiah Clark, an active-duty Navy petty officer stationed at Fort Meade, Maryland, I conducted an informal survey of 61 active-duty servicemembers. Respondents were asked the following questions:

1. At the time you entered the armed forces, what was your home of record (state only)?

2. What state is listed on your 2004 W-2?

3. What state do you live in currently?

4. Have you changed your home of record since entering the armed forces?

5. If yes, why did you change your home of record?

See Brunori, supra note 89, at 19.