

Important Information about the Adoption Tax Credit

Beginning in tax year 2003, families adopting children from foster care may benefit from the federal adoption tax credit without needing to document expenses. For tax year 2007, parent(s) who adopt a child from foster care and whose adjusted gross income is less than \$210,820 qualify for an \$11,390 tax credit, even if you incurred zero expenses related to the adoption. A tax credit is an amount that can be subtracted dollar for dollar from the taxes you owe. Previously, adoptive parents could take the tax credit only to offset “qualified” adoption expenses. You have this year and up to the next five additional years in which to use it.

What is an Adoption Tax Credit?

Congress has made an adoption tax credit available since tax year 1997. Until 2003, the adoption credit allowed families earning less than \$115,000 to subtract from their tax liability “qualified adoption-related expenses,” as defined by the IRS -- up to \$5,000 for each private adoption, or \$6,000 for each adoption of a child with special needs. A “child with special needs” is any child that a state child welfare agency determines cannot be returned home to his/her parents and a specific factor makes it reasonable to conclude the child cannot be placed with adoptive parents unless adoption assistance is provided. Most children adopted from foster care (and for whom adoptive parents are receiving AAP benefits) qualify as a child with special needs. “Qualified” expenses are expenses directly related to the adoption, such as adoption agency fees, attorney fees, court costs, medical expenses, and travel expenses.

However, most families adopting a foster child saw limited benefit from the adoption tax credit because they incur few expenses directly related to the adoption. For families who adopt from public agencies, costs for home studies and agency fees are often waived or reimbursed through the nonrecurring costs provision of the adoption assistance program. These families’ adoption-related costs are more likely to include ongoing medical services and counseling, larger vehicles, and housing modifications that occur before and after a child or sibling group is placed. Such costs do not count as “qualified adoption-related expenses” for purposes of the adoption tax credit.

Adoption Tax Credit Changes Effective in 2003

In June 2001, Congress revised the adoption tax credit by increasing the amount of the credit to \$10,000 for all adoptions (plus an annual cost-of-living adjustment or COLA) and increasing the upper limit on the amount of income parents may earn in order to use the credit to \$150,000 (plus COLA), phased out at \$190,000 (plus COLA). You can take the full amount of the credit if your adjusted gross income is less than \$150,000. The amount you can take decreases as your income approaches \$190,000. If your income exceeds \$190,000, you are not eligible for the credit. For the 2007 tax year, adoptive parents with adjusted gross incomes less than \$210,820 can access a portion of the credit.

Congress also addressed the special circumstances of families who adopt foster children by making the adoption tax credit a flat tax credit. A “flat” tax credit means that a family who finalizes the adoption of a foster child and earns less than \$190,000 can take the tax credit without having to document that they incurred a specific level of qualified adoption expenses. The flat tax credit for foster child adoptions was created in recognition of the many costs associated with these adoptions that are not included in the IRS list of “qualified” adoption expenses.

When Can the Adoption Tax Credit Be Claimed?

The adoption tax credit must be claimed in the same year a child’s adoption finalizes. However, the adoption tax credit can be claimed over five years. This means that if you do not owe enough tax to take the full amount of the credit for the year in which your child was adopted, you should still submit a claim for the tax credit, because you might have a federal income tax liability in the ensuing four years; and you can apply the remaining amount of the credit to the next four years’ taxes. In other words, if you reduce your tax bill to zero and have not used the entire credit, the unused credit amount can be carried forward five tax years, or until it is completely used, whichever comes first. If you finalized your adoption before 2007 and failed to claim the adoption tax credit, you can still file an amended tax return to qualify for the credit.

Forms

Form 8839 is the form you need to file. To take the credit, complete [Form 8839 \(PDF\)](#), *Qualified Adoption Expenses*. You will attach Form 8839 to [Form 1040 \(PDF\)](#) or [Form 1040A \(PDF\)](#) and report the credit on line 52 of Form 1040 or line 34 of Form 1040A. The IRS Instructions for Form 8839 are at <http://www.irs.gov/pub/irs-pdf/i8839.pdf>.

Important Note: You should consult your accountant or a tax preparer or the IRS at (800) 829-1040 or www.irs.gov for information on how the tax credit will affect your individual tax situation and whether you will actually be able to claim the tax credit. Some helpful websites with further information on the adoption tax credit are: <http://www.nacac.org/policy/taxcredit.html>; www.adoptiontaxcredit.com.

Finally, if you receive AAP for your child and have questions on whether it is taxable income or if you can claim that child as a dependent (and receive the child tax credit), you should North American Council on Adoptable Children’s fact sheet *Tax Issues Related to Adoption Assistance and Adoption*.

If you have any questions about the adoption tax credit, please call Alliance Adoption Program Senior Staff Attorney Cynthia Billey at (213) 368-6010.