

What is the adoption tax credit?

The tax code provides an adoption credit of up to \$13,400 of qualified expenses (in 2015) for each child adopted, whether via public foster care, domestic private adoption, or international adoption. The tax expenditure on the credit in 2014 totaled approximately \$260 million.

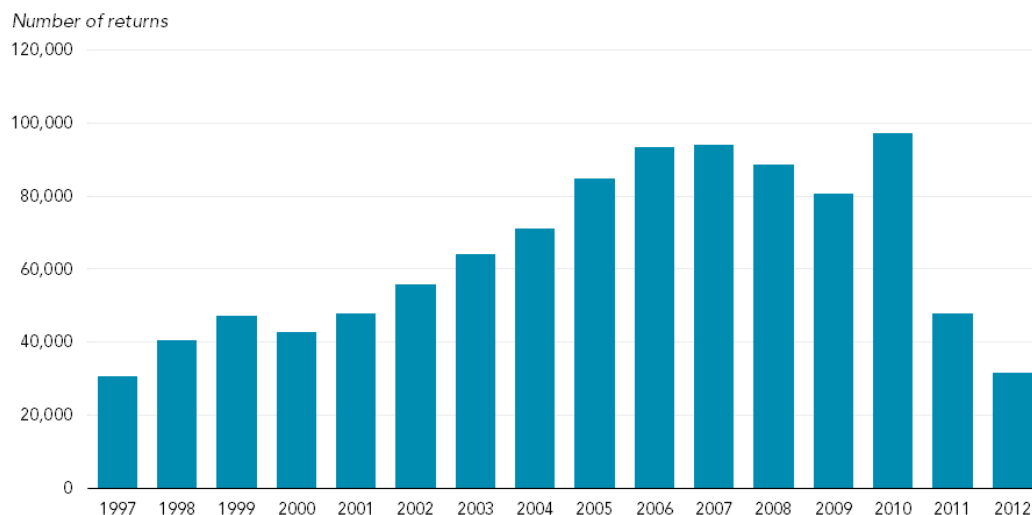
CREDIT AMOUNT

The adoption credit covers all qualifying expenses up to \$13,400 in 2015. The maximum credit and income eligibility thresholds are indexed for inflation. "Special needs" adoptions automatically qualify for the maximum credit regardless of actual out-of-pocket expenses. For purposes of the credit, a child has special needs if a state's welfare agency determines that the child cannot or should not be returned to his or her parents' home and that the child probably will not be adoptable without assistance provided to the adoptive family. This provision is designed to encourage parents to adopt children who would otherwise be hard to place, even if most of the adoption expenses are covered by someone else (such as a public foster care program).

ELIGIBILITY

The adoption credit is available to most adoptive parents, with some exceptions. The 2015 credit begins to phase out at \$201,010 of modified adjusted gross income and phases out entirely at \$241,010. The credit is also not available for adoptions of stepchildren. Finally, any expenses reimbursed by an employer through an adoption assistance program are ineligible for the credit.

FIGURE 1
Tax Returns Claiming Adoption Tax Credit
1997 – 2012



Source: Internal Revenue Service, Statistics of Income: Individual Income Tax Returns, Publication 1304, Table A.

REFUNDABILITY

The adoption tax credit is nonrefundable but can be carried forward for up to six years. The credit is thus of little or no value to low-income families who pay little or no income tax. The Patient Protection and Affordable Care Act of 2010 made the adoption tax credit refundable for 2010 and 2011. However, concerned about the potential for fraud, the Internal Revenue Service (IRS) stepped up compliance efforts. The result, according to the National Taxpayer Advocate, was substantial delays for taxpayers, with 69 percent of all adoption credit claims during the 2012 selected for audit. The IRS ultimately disallowed only 1.5 percent of claims, and 20 percent of those savings were spent on interest owed to taxpayers with delayed refunds. The credit reverted to nonrefundability in 2013.

TAX EXPENDITURE

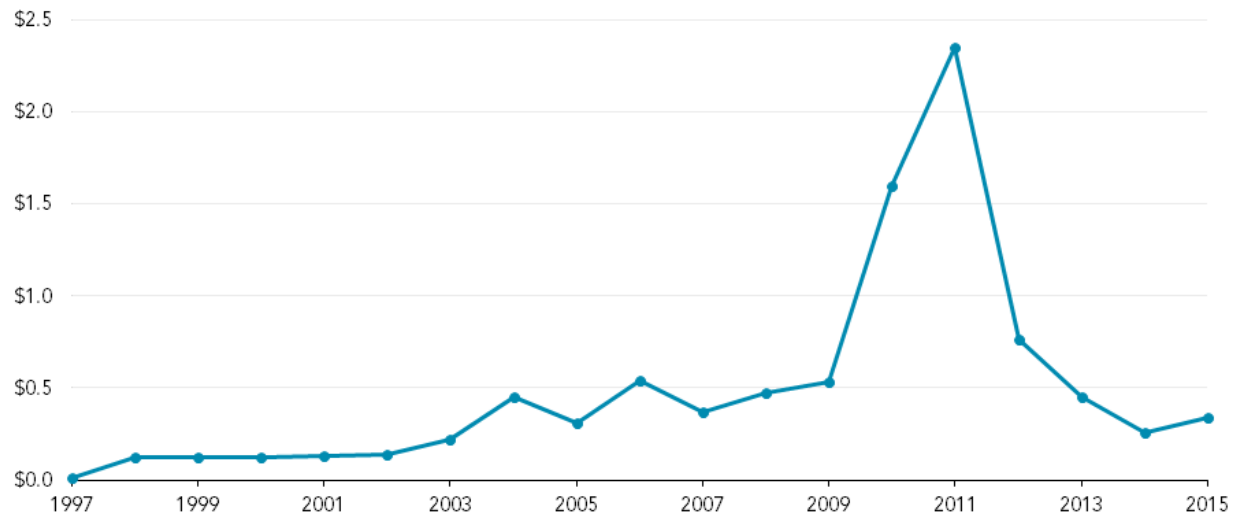
The credit has been repeatedly expanded, from an initial maximum value of \$5,000 in 1997 to \$13,400 in 2015. In fiscal year 2014, credit claims reduced tax liability by \$260 million, according to the US Department of Treasury. The temporary availability of a refundable credit pushed the tax expenditure up to the dramatically higher figures of \$1.6 billion 2010 and \$2.35 billion in 2011 (including the refundable portion) (figure 2).

FIGURE 2

Tax Expenditures for Adoption Fiscal years 1997–2015



Billions of dollars



Source: Treasury tax expenditure budget, various years.

Notes: Includes outlay (refundable) portion in years 2010-12. Tax Expenditure estimate includes the value of tax-free employer adoption programs, which are likely 1-2 percent of the total.

WHO GETS IT

The distribution of the credit across income groups ranges from small amounts for the lowest earners (because of their minimal tax liability and the credit's nonrefundability) and the highest earners (because of the income cap) to substantial amounts to those with middle and higher incomes. For example, in 2005, those with incomes under \$50,000 made up 23 percent of claimants and averaged \$1,366 in benefits per adoption, while those in the \$75,000–\$150,000 range obtained credits averaging \$6,000 per adoption. Few households with incomes above \$150,000 reported adoption expenses, probably because few were ineligible for the credit (table 1).

The most recent year with data available by adoption type (2004) indicates that nearly half of adoptions for which the credit was claimed were for domestic children without special needs, with only 18 percent classified as special needs and the remainder reflecting international adoptions.

TABLE 1

Distribution of Adoption Tax Credit
By total income, 2005



Total income (dollars)	Number of returns with adoption expenses	Total tax benefit (thousands of dollars)	Mean credit (dollars)
Less than 25,000	2,368	810	802
25,000 – 49,999	10,876	27,720	1,489
50,000 – 74,999	15,495	88,853	3,174
75,000 – 99,999	12,038	97,377	4,899
100,000 – 149,999	12,043	122,886	7,387
150,000 – 189,999	2,517	19,108	6,048
More than 190,000	1,066	4,792	6,230
All	56,423	361,527	4,095

Source: US Department of Treasury, 2007.

DATA SOURCES

Department of the Treasury. 2007. *Federal Income Tax Benefits for Adoption: Use by Taxpayers 1999–2005*. [Table 1. “Summary of Adoption Benefits Reported on Income Tax Returns 1999–2005.”](#)

Department of the Treasury, and Internal Revenue Service. *Individual Income Tax Returns Publication 1304*. [Table A. “All Returns: Selected Income and Tax Items in Current and Constant 1990 Dollars, Tax Years 1990–2012.”](#)

FURTHER READING

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