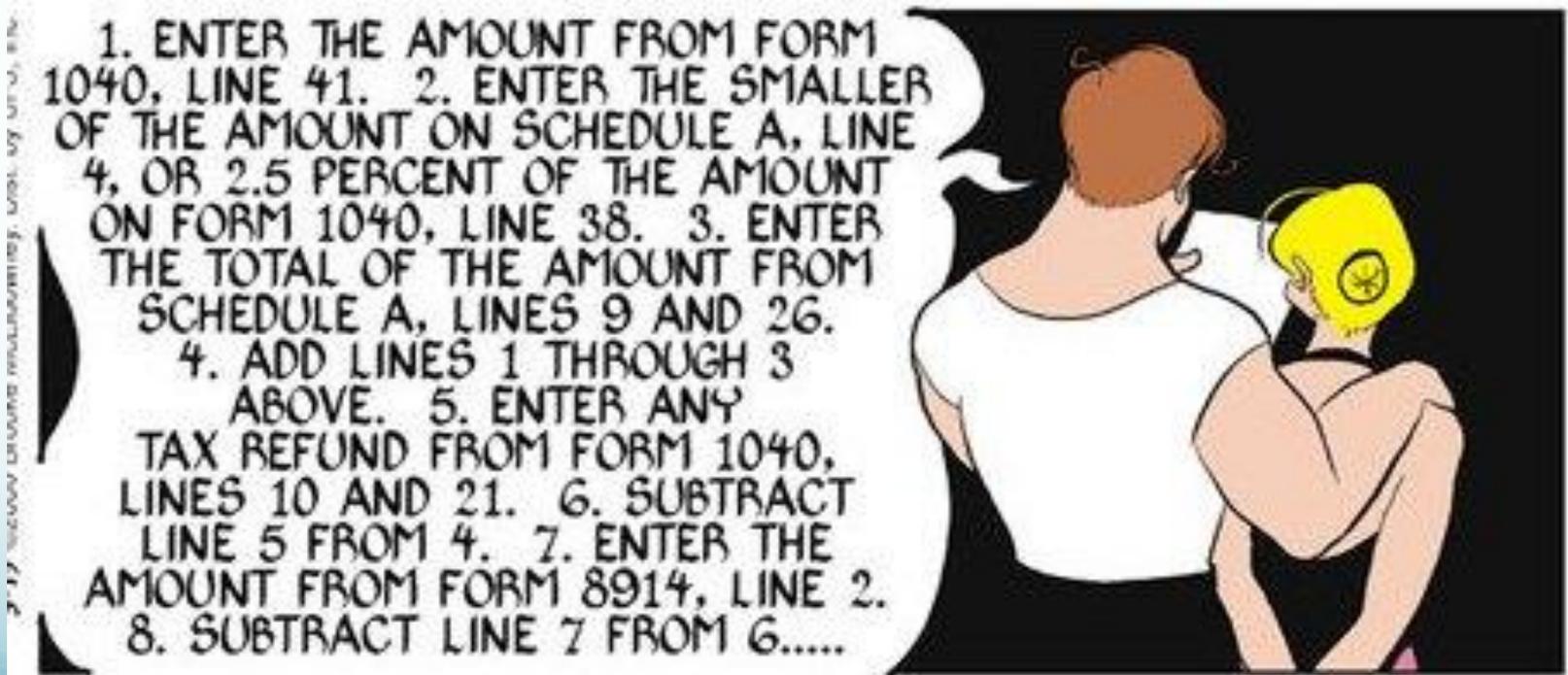


Federal Adoption Tax Credit

Welcome to NACAC's workshop on the federal adoption tax credit. This workshop is intended to provide you with basic information on the tax credit. It is not intended as tax advice.



Presented by Josh Kroll

Agenda

The agenda today will cover:

- Basic information about the federal adoption tax credit
- Specific information about adoptions completed in the following years:
 - 2021-2012
 - Other tax issues related to adoption

Eligibility

To be eligible for the federal adoption tax credit, you must:

- Have adopted a child (other than a step-child)
- The child must be under 18 years old at the time of adoption
- Have a modified adjusted gross income within certain guidelines
- Either have adopted a child determined by the state to have special needs OR have qualified adoption expenses; children who have special needs qualify for the maximum tax credit.

Maximum Credit and Income

| | Maximum Adoption Credit | Lower Income Limit (can get partial credit) | Upper Income Limit |
|------|-------------------------|---|--------------------|
| 2021 | \$14,440 | \$216,660 | \$256,660 |
| 2020 | \$14,300 | \$214,520 | \$254,520 |
| 2019 | \$14,080 | \$211,160 | \$251,160 |
| 2018 | \$13,810 | \$207,140 | \$247,140 |
| 2017 | \$13,570 | \$203,540 | \$243,540 |
| 2016 | \$13,460 | \$201,920 | \$241,920 |
| 2015 | \$13,400 | \$201,010 | \$240,010 |
| 2014 | \$13,190 | \$197,880 | \$237,880 |
| 2013 | \$12,970 | \$194,580 | \$234,580 |
| 2012 | \$12,650 | \$189,710 | \$229,710 |

The credit is a one-time credit **per child**. The income limit is based on the modified adjusted gross federal income in the year of the adoption. Families who earn between the lower income limit and the upper can take partial credit. Those who make below the lower limit are eligible for the full credit.

Income test and filing status

- The income test is only applied in the year you are claiming the credit. It does not apply if you are only carrying forward credit from a previous year.
- You cannot file Married Filing Separately (MFS) in the year you claim the credit. If you are Married but separated:
 - You lived apart from your spouse during the last 6 months of the year
 - The eligible child lived in your home more than half of the year
 - You provided over half the cost of keeping up your home
- Then you must file Head of Household, not MFS, in the year you claimed the credit.

When to file for adoption credit

- For international adoptions, in the year the adoption is final.
- For special needs adoptions without expenses, in the year the adoption is final
- For private domestic adoptions, either the year the adoption is final OR if not final, the year after the expenses were paid.

Not finalized adoptions

- For private domestic adoptions that aren't finalized.
- You can claim the credit the year after you paid the expenses. So 2019 expenses can be claimed as a credit on 2020 taxes.
- You will have to paper file, or file without the credit and amend (also paper filing).
- Any credit claimed will count against available new credit in the next year. If you don't use up all the credit, you will carryforward any unused credit.

Attempted Adoptions

- Sometimes private domestic adoptions do not happen.
- If you continue to pursue adoption, then any expenses and credit for previous adoption attempt will factor into the one adoption attempt, even if it is two different identified expectant mothers and their respective infants.
 - Families that pay and claim \$5,000 in expenses for baby A, which does not finalize. Later they pay \$20,000 for baby B that does finalize. They be able to claim all \$25,000 in expenses, but will be limited to the amount of credit for one child in the year finalized (\$14,080—2019)

Children with Special Needs

How do I know if my child is considered a child with special needs for the adoption tax credit?

- The definition of special needs for the tax credit is almost identical to the definition for federal adoption subsidy. **Therefore, if you adopted a child from foster care who receives adoption subsidy, your child should be considered a child with special needs.**

Why does it matter if my child is special needs?

- If you adopted a child with special needs, you qualify for the maximum amount of the adoption tax credit, even if you did not pay anything for the adoption.

IRS instructions

- **Line 1(d) Example 1.**
- Agency A is the child welfare department of State V. Mark, Rachel, and Janet, brother and sisters, are U.S. children residing in State V. When Mark was 10, Rachel 8, and Janet 6, Agency A removed the children from the home of the biological parents.
- After Agency A placed the children in foster care, Agency A determined it would be difficult to place the children for adoption without providing assistance to the adoptive family because of the ages and sibling relationship of the children.

IRS instructions continued

- Agency A provided the adoptive parents with monthly subsidy payments on behalf of each child. **The adoption assistance agreements entered into between Agency A and the adoptive parents are evidence that State V has determined that Mark, Rachel, and Janet are children with special needs and may be used to support the adoptive parents' claim to the adoption tax credit.**
- Mark, Rachel, and Janet are U.S. children who State V has removed from their biological parents. State V also has determined that each child has special needs. Their adoptive parents may claim an adoption tax credit for each child, even if the adoptive parents paid no qualifying adoption expenses, if all other requirements of the credit are met.

Children with Special Needs

- The single most important thing you need to know is that **a child with special needs qualifies for the full amount of the credit regardless of expenses paid for the adoption.**
- If your tax preparer does not believe you, show him or her the instructions for IRS Form 8839, line 5. The instructions are very clear.

Children with Special Needs

(continued)

- Special needs adoption.
- If you adopted a U.S. child with special needs and the adoption became final in 2020, enter on line 5:
 - \$14,300, minus
 - Any qualified adoption expenses you used to figure any adoption credit you claimed for the same child in a prior year. This is the amount you entered on line 3 of Form 8839 for this child.
- If you didn't claim any adoption credit for the child in a prior year, enter \$14,300 on line 5 even if your qualified adoption expenses for the child were less than \$14,300 (and even if you didn't have any qualified adoption expenses for this child).

Filing and record keeping

- Beginning with 2013 families could e-file their returns. They did not have to file a paper return.
 - For domestic private adoptions without a taxpayer ID number for the child or a child isn't known yet, they will have to paper file.
- Families do not have to send in supporting documentation like they had to for 2010 and 2011. However, families should keep these documents handy in case the IRS audits them.

Documenting the Adoption

- For all domestic adoptions, **a court decree** (the papers from the judge/court that shows you adopted)
- For international adoptions, foreign adoption decree translated into English, Hague Adoption Certificate, some Visas.
- For special needs adoptions, you need proof that the state has determined that the child has special needs. Your **adoption assistance agreement** (adoption subsidy agreement) is the proof.
- For private domestic and international adoptions that are not determined special needs, you should keep copies of bills, receipts and proof of payment to show that you had qualified adoption expenses and that you paid them.

Definitions

- Claim — This means that you are filing that you are eligible to get the credit.
- Use — Once you claim the credit, you have to be able to use it. Your ability to use the credit will be limited by your tax liability for the year.
- Tax liability — This is the amount you are responsible for in federal income tax for the year.

Base example

- NACAC withholds \$4,000 from my paychecks to pay my federal income tax.
- When I complete my taxes, the tax tables say I owe \$3,000 in income tax.
- I have no credits, and no other taxes.
- I get a refund of the \$1,000 I overpaid. So even though I get a refund, I owed \$3,000 in income tax.

New Twist

- With the passage of tax reform starting in 2018, there are some changes that impact a family's ability to use the adoption tax credit.
- Previously all \$1,000 of the child tax credit (children under 17 at end of year) could become the refundable Additional Child Tax Credit (provided enough earned income)
- Currently only \$1,400 of the \$2,000 available Child Tax Credit can be made refundable. That leaves \$600 per child that will be used before the adoption tax credit. Children 17 and over would also have \$500 used before the adoption tax credit.
- So from previous page example. Would owe \$3,000 which would be reduced to \$0 by \$600 in child tax credit and \$2,400 in adoption tax credit (of \$14,300)
- Payment would be \$4,000 withheld plus \$1,400 in additional child tax credit.
- Total refund would be \$5,400. Carryforward \$11,900 to the next year.

Save the Adoption Tax Credit

- NACAC has worked with other national groups to extend the adoption tax credit (successful) and make it refundable (not successful)
- We are advocating for it to be refundable in 2020 and going forward.
- Join our Facebook page:
<https://www.facebook.com/AdoptionTaxCredit>
- Get connected to News from NACAC e-newsletter.
- See our webinar on advocacy at www.adoptiontaxcredit.org
- If you Adjusted Gross Income is below \$30,000 the adoption tax credit probably won't help you one cent if it isn't made refundable (based on pre Tax Reform data—which seems to still be accurate)

Families who adopted in 2020

- It is still not refundable
- Special needs adoption do not have to have qualified adoption expenses.
- They will be able to e-file (domestic private without an identified child will probably have to paper file because of lack of taxpayer id for the child).
- Families should keep their records as mentioned earlier

Amending your returns

- If you paid someone to do your taxes, you should ask that person to amend the returns for free. They should have had you claim the adoption tax credit.
- If you used tax return software (such as TurboTax), see if you can amend it using that software.
- If you filed your return by hand, you will need to fill out Form 8839 and Form 1040x for the year you adopted—plus any subsequent years you are amending.
- For families that don't file taxes, you will have to file an original tax return with a form 8839 for the years you need to (just like which ones we say must be amended on the next slide).

If You Adopted in 2017-2019

- Special needs adoption do not need to document qualified adoption expenses.
- It is not refundable
- 2017 must be amended by April 15, 2021 to not lose any refund you may be due
- 2017 and 2018-19 interact very differently with the Child Tax Credit
- You must keep documentation in case the IRS asks for it, but are not required to submit it to the IRS when you file.
- Any unused credit is carried forward to the next year, up to a total of six years (year claimed and five additional years)—so if you amend 2017, any carry forward credit will be on your 2018 which you will need to amend too.

If You Adopted in 2016 or earlier

- If you adopted in 2011 or earlier it is too late. The IRS only allows for a refund within three years. Tax returns for 2011 are due by April 15, 2012—three years later is April 15, 2015.
- Because 2011 was refundable, there is no carryforward to 2012.
- If you adopted in 2012-2016, you are unable to receive a refund for 2012-2015, but you claim the credit, use what you would have (no refund) and carryforward unused credit to 2017 (through April 15, 2021) which you can still amend for a refund.

Claiming a child as a dependent

Relationship Test

- To meet this test, a child must be:
- Your son, daughter, stepchild, foster child, or a descendant (for example, your grandchild) of any of them, or
- Your brother, sister, half brother, half sister, stepbrother, stepsister, or a descendant (for example, your niece or nephew) of any of them.
- **Adopted child.** An adopted child is always treated as your own child. The term “adopted child” includes a child who was lawfully placed with you for legal adoption.
- **Foster child.** A foster child is an individual who is placed with you by an authorized placement agency or by judgment, decree, or other order of any court of competent jurisdiction.

Claiming a child as a dependent

Age Test

- To meet this test, a child must be:
- Under age 19 at the end of the year and younger than you (or your spouse if filing jointly),
- A student under age 24 at the end of the year and younger than you (or your spouse if filing jointly), or
- Permanently and totally disabled at any time during the year, regardless of age.

Residency Test

- To meet this test, your child must have lived with you for more than half the year. There are exceptions for temporary absences, children who were born or died during the year, kidnapped children, and children of divorced or separated parents.
- *Death or birth of child.* A child who was born or died during the year is treated as having lived with you more than half the year if your home was the child's home more than half the time he or she was alive during the year. The same is true if the child lived with you more than half the year except for any required hospital stay following birth.

Claiming a child as a dependent

Support Test (To Be a Qualifying Child)

- To meet this test, the child can't have provided more than half of his or her own support for the year.
- *Foster care payments and expenses.* Payments you receive for the support of a foster child from a child placement agency are considered support provided by the agency. Similarly, payments you receive for the support of a foster child from a state or county are considered support provided by the state or county.

Joint Return Test (To Be a Qualifying Child)

- To meet this test, the child can't file a joint return for the year.

Other Tax Issues

- Taxability for adoption subsidy payments — Adoption subsidy payments are not taxable income for federal income tax purposes.
- The child tax credit — the amount of the adoption tax credit you could CLAIM/USE was related to the child tax credit. As mentioned earlier this has gotten more complicated than prior to 2018 as not all of the child tax credit can become refundable.
 - Software and tax preparers will fill out the Child Tax Credit worksheet in Publication 972 to see how much of each credit you will use.

Questions on Tax Credit?

- Ask now!
- Look on our web site: www.nacac.org
- Call our office: 651-644-3036 x115
- E-mail me: joshk@nacac.org