

Federal Adoption Tax Credit for 2014

Updated April 2014

For adoptions finalized in 2014, there is a federal adoption tax credit of up to \$13,190 per child. The 2014 adoption tax credit is NOT a refundable credit, which means taxpayers can only get the credit refunded if they have federal income tax liability (see *below*).

The credit is paid one time *for each adopted child*, and should be claimed when taxpayers file taxes for 2014 (typically in early 2015).

To be eligible for the credit, parents must:

- ***Have adopted a child other than a stepchild*** — A child must be either under 18 or be physically or mentally unable to take care of him or herself.
- ***Be within the income limits*** — How much of the credit parents claim is affected by income. In 2014, families with a modified adjusted gross income below \$197,880 can claim full credit. Those with incomes above \$237,880 cannot claim the credit; those with incomes from \$197,880 to \$237,880 can claim partial credit.

The Amount of Credit to Be Claimed

Families who finalize the adoption of a child with special needs in 2014 (see *details below*) can claim the full credit of \$13,190 on the line that asks for expenses—whether or not they had any expenses.

Example — A woman adopts three of her grandchildren from foster care and the state paid all of the fees. All three children receive monthly adoption assistance benefits and thus are considered special needs. The grandmother earns less than \$197,880 so can claim the full credit of \$13,190 per child for a total of \$39,570. How much the grandmother actually receives, however, will depend on her tax liability (explained below).

Other adopters can claim a credit based on their qualified adoption expenses, which are the reasonable and necessary expenses paid to complete the adoption as long as those expenses are not reimbursed by anyone else. If the expenses are less than \$13,190, the adopters claim only the amount of the expenses. If expenses exceed \$13,190, the maximum to be claimed is \$13,190 per child.

Example — A couple adopted two children from China and had \$40,000 in legal, travel, and agency fees. They received a grant of \$20,000, leaving them with \$20,000 in qualified adoption expenses. They can claim only \$20,000 (not the full \$26,380 they might have been eligible for had their expenses been higher). If their modified adjusted gross income was between \$197,880 and \$237,880, they would receive only a portion of the credit, since the credit begins to phase out at incomes of \$197,880.

When to Claim the Credit

Parents who adopt a child with special needs claim the credit the year of finalization. Parents who adopt internationally cannot claim the credit until the year of finalization. Parents who are adopting from the U.S. and claiming qualified adoption expenses can claim the credit the year of finalization or the year after they spent the funds.

Example — A family begins adopting a U.S. infant in 2012 and pays \$4,000 in expenses in 2012, \$5,000 in 2013, and \$3,000 in 2014. The adoption finalizes in 2014. The parents must file for the \$4,000 spent in 2012 on their 2013 taxes. They cannot claim the \$5,000 and \$3,000 until they file their 2014 taxes.

Qualifying as Special Needs

Families who finalized in 2014 the adoption of a child who has been determined to have special needs can claim the full credit of \$13,190 as their expenses, regardless of their actual adoption expenses. The credit for all other adopted children is based on the family's qualified adoption expenses.

Basically, a child with special needs is a U.S. foster child who receives adoption subsidy or adoption assistance program benefits (which can include a monthly payment, Medicaid, or reimbursement of nonrecurring expenses). The instructions for the 2013 tax credit explain that to be considered a child with special needs, the child must meet all three of the following characteristics:

- “The child was a citizen or resident of the United States or its possessions at the time the adoption effort began (US child).
- A state (including the District of Columbia) has determined that the child cannot or should not be returned to his or her parents' home.
- The state has determined that the child will not be adopted unless assistance is provided to the adoptive parents. Factors used by states to make this determination include:
 - The child's ethnic background and age,
 - Whether the child is a member of a minority or sibling group, and
 - Whether the child has a medical condition or a physical, mental, or emotional handicap.”

Just because a child has a disability does not mean the child is special needs under the tax credit. No child adopted internationally is considered special needs for the adoption tax credit. Not even every child adopted from foster care is considered special needs (about 10 percent of children adopted from care do not receive adoption assistance support). **Those who do not receive any support from the adoption assistance program are likely not to have been determined to have special needs.**

Bottom line, if your child does not receive adoption subsidy/adoption assistance benefits, you will likely have to have qualified expenses to claim the credit.

How Much Taxpayers Will Benefit

How much, if any, of the adoption tax credit a parent will receive depends on their federal income tax liability in 2014 (and the next five years). In one year, taxpayers can use as much of the credit as the full amount of their federal income tax liability, which is the amount on line 46 of the Form 1040 less certain other credits (see Child Tax Credit below). Even those who normally get a refund may still have tax liability and could get a larger refund with the adoption tax credit. Taxpayers have six years (the year they first claimed the credit plus five additional years) to use the credit.

People who do not have federal income tax liability will not benefit. We encourage them to file a Form 8839 with their taxes to document the credit. They will then be able to carry the credit forward to future years in case the credit becomes refundable again in the future or their tax situation changes. (If a tax preparer wants to charge extra to file the Form 8839 and you won't benefit at all with your 2014 taxes, you might want to wait and amend your taxes if the credit is ever made refundable.)

Below are a couple of examples of how the tax credit might benefit families who finalized adoptions in 2014 (these are simplified examples, which do not take into account the Child Tax Credit explained below).

Example 1 — A couple adopted two brothers who had been determined to have special needs. The parents had \$6,500 in federal income tax withheld from their paychecks, and their tax liability is \$7,000, which means they would normally owe \$500 to the IRS. Their adoption tax credit is \$26,380, and they can use \$7,000 (their tax liability) of that with their 2013 taxes. They get a refund of the \$6,500 they had already paid, and can carry over \$19,380 for up to five more years.

Example 2 — A couple adopted three siblings with special needs. They had \$1,000 in federal income tax withheld from their paychecks, and their tax liability is \$0, which means they would receive a refund of \$1,000. They have \$39,570 in the adoption tax credit, but they cannot use it with their 2014 taxes since they have no federal income tax liability. They should still file Form 8839 with their 2014 tax return so that they can establish the credit, and carry it forward for up to five additional years in case their tax liability goes up in the future or the credit becomes refundable.

Interaction with the Child Tax Credit

If parents can claim their child as a dependent, then they should also look into the Child Tax Credit. The Child Tax Credit and the Adoption Tax Credit interact and may reduce the Child Tax Credit a family can claim. To determine the amount of the Child Tax Credit they can use, a family must complete the Child Tax Credit Worksheet in IRS Publication 972.

Taxpayers who can answer Yes on the last line of the Child Tax Credit Worksheet may be eligible for the Additional Child Tax Credit, which is a refundable credit (meaning they can claim the credit regardless of their tax liability). To claim the Additional Child Tax Credit, parents must complete IRS Form 8812.

Claiming the Credit

To claim the credit, taxpayers will complete a 2014 version of IRS Form 8839 and submit it with their Form 1040 when they file their 2014 taxes. Before filing, taxpayers should review the 2014 Form 8839 instructions carefully to be sure they apply for the credit correctly. The instructions will likely contain a worksheet needed to calculate tax liability and thus how much of the credit will be received. The form and instructions will be available around January 2015 at irs.gov and in the [Forms section](#) of this web site.

What If I Have Additional Questions?

If you have additional questions on the adoption tax credit, contact the North American Council on Adoptable Children at 651-644-3036 or taxcredit@nacac.org or discuss this with your accountant or tax preparer.