

# Adoption Tax Credit and Exclusion

Provided by the  
Legal Assistance Branch MLCPAC (II)  
Bldg. 54C Coast Guard Island  
Alameda, California 94501  
(510) 437-5891

## Tax Credit

Public Law 104-188 authorized tax credits for qualifying adoption expenses beginning in 1997. The tax credit is up to \$5,000 for qualifying expenses paid to adopt an eligible child, and as much as \$6,000 if the expenses are for the adoption of a child with special needs. The adoption credit is an amount that you subtract from your tax liability. After 2001, the adoption credit applies only to the adoption of a child with special needs as defined below.

## Tax Exclusion for Expenses Reimbursed by Employer

Through 2001, up to \$5,000 (\$6,000 for a child with special needs) paid or reimbursed by your employer for qualifying adoption expenses under an adoption assistance program may be excludable from your gross income. For purposes of the exclusion, an adoption assistance program includes the DOD/CG reimbursement to members of the Armed Forces and Coast Guard. After 2001 you cannot take an exclusion for any employer or DoD/CG reimbursement payment.

After 1997 and before 2002, you may claim both a credit and an exclusion for expenses of adopting an eligible child, *e.g.* if you have expenses in excess of those reimbursed you could claim an exclusion for the amount of reimbursement and a credit for those expenses not reimbursed but which qualify for the tax credit. However, you cannot claim both a credit and exclusion for the same expense. If you adopt a foreign child you cannot take a tax credit or exclusion until the adoption becomes final.

## Expenses that Qualifying for the Tax Credit

Qualifying adoption expenses are reasonable and necessary adoption fees, court costs, attorney fees, traveling expenses (including amounts spent for meals and lodging) while away from home, and other expenses directly related to, and whose principal purpose is for, the legal adoption of an eligible child.

Qualifying adoption expenses do not include expenses:

- That violate state or federal law,
- For carrying out any surrogate parenting arrangement,
- For the adoption of your spouse's child (**a Stepparent Adoption**)
- Paid using funds received from any federal, state, or local program,
- Allowed as a credit or deduction under any other federal income tax rule, or
- Paid or reimbursed by your employer or otherwise (except that amounts paid or reimbursed under an adoption assistance program may be qualifying expenses for the exclusion), *e.g.* DoD/CG Reimbursement Program.

**Eligible Child.** An eligible child must be:

- Under 18 year old, or
- Physically or mentally incapable of caring for himself or herself

After 2001, the adoption credit applies only if the eligible child is a child with special needs.

### **Child with Special Needs**

An eligible child is a child with special needs if he or she is a citizen or resident of the United States (including the District of Columbia and U.S. possessions) and a state determines that the child cannot or should not be returned to his or her parents' home and probably will not be adopted unless adoption assistance is provided to the adoptive parents. A foreign child cannot be treated as a child with special needs. Factors used by states to determine if a child has special needs could include:

- The child's ethnic background,
- The child's age,
- Whether the child is a member of a minority or sibling group or
- Whether the child has a medical condition or physical, mental, or emotional handicap.

If your state has determined that the child you are adopting is a child with special needs, you should keep evidence of that fact for your records.

### **Dollar Limit**

The amount of your adoption credit or exclusion is limited to \$5,000 for each effort to adopt an eligible child or \$6,000 for each effort to adopt an eligible child with special needs. If you take both a credit and an exclusion, this dollar limit applies separately to each.

The \$5,000 (or \$6,000) amount is the maximum of qualifying expenses taken into account over all taxable years. Therefore, it must be reduced by the amount of qualifying expenses taken into account in previous years for the same adoption effort.

### **When to Take the Credit or Exclusion**

An effort to adopt a child does not require that the adoption be finalized, unless the child is foreign (not a U.S. citizen or resident of U.S.) at the time the adoption begins. A final adoption is required if the child is foreign and for reimbursement of adoption expenses under the DoD/CG adoption reimbursement programs. See IRS Pub 968 for an easy to use chart regarding when to claim the tax credit or exclusion.

**Income Limit**

There is an income limit on the adoption credit or exclusion and that is based on modified adjusted gross income (modified AGI) more than \$75,000. See IRS Pub 968 for instruction regarding calculating the reduced credit or exclusion.

**How To Take the Credit Exclusion**

You must file Form 8839 with either Form 1040 or Form 1040A to take the credit or exclusion. You should maintain records to support any adoption credit or exclusion claimed.

**Joint Return Required**

If you are married, you must file a joint return to take the adoption credit or exclusion. However, you can take the credit or exclusion on a separate return if you are legally separated under a decree of divorce or separate maintenance, or if you lived apart from your spouse for the last six months of the tax year and:

- your home is the eligible child's home for more than half the year,
- You pay more than half the cost of keeping up your home for the year.

**Child's Identifying Number**

You must provide an identifying number for the child on Form 8839. This number is the child's:

- Social security number (SSN) if the child has one or you will be able to obtain one in time to file your tax return. Apply for an SSN on Form SS-5
- Individual taxpayer identification number (ITIN) if the child is a resident or nonresident alien and not eligible for an SSN. Apply for an ITIN on Form W-7A.
- Adoption taxpayer identification number (ATIN) if you are in the process of adopting a child who is a U.S. citizen or resident and cannot get an SSN for the child until the adoption is final. Apply for an ATIN on Form W-7A.

**Tax Assistance**

For free tax assistance, contact your installation VITA tax advisor, or the IRS at 1 (800) 829-1040. Also see IRS Publication 968 and IRS Form 8839. MLCP Tax Assistance Program can be reached at (510) 437-2762.

**Adoption Reimbursement, Citizen for a Adopted Child and Other Benefits**

For additional information regarding the DoD/CG programs for reimbursement of adoption expenses, obtaining citizenship for a foreign-born child, and other benefits related to adoption see MLCP (II) fact sheet, Adoption Reimbursement, Citizenship for a Adopted Child and Other Benefits.

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