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Claiming the Federal Adoption Tax Credit for Special Needs Adoptions *(Updated October 2009)*

Families who adopt a child with special needs from foster care can claim a federal adoption tax credit without needing to incur or document expenses. The per-child tax credit is \$12,150 for those finalized in 2009*, and families have six years to use the entire credit. (If you finalized your adoption between 2003 and 2008, read *What If We Finalized an Adoption before the Current Tax Year* below.)

Are We Eligible for the Credit?

To qualify for the credit without documenting expenses, families must:

- have adopted a child with special needs from foster care and
- have a modified adjusted gross income of a certain level.

Then to be able to use the credit, families must also have federal tax liability.

Does my child have special needs?

Children who are harder to place for adoption—older children, children of color, sibling groups, and children with medical conditions or disabilities—are often determined to have special needs. NACAC interprets the IRS instructions to mean that if a child receives adoption subsidy (assistance), the adoption subsidy agreement (or application and agreement) is evidence that the state has determined that child has special needs. (See Line 1, Column (d) of the 8839 instructions for the IRS's language.)

If your child does not receive an adoption subsidy, NACAC believes the state has not determined that your child has special needs and you will have to document adoption expenses to claim the credit.

Are we financially eligible for the credit?

How much, if any, of the credit you can use is based on:

- your income — Families with federal modified adjusted gross income above \$222,180 in 2009, cannot claim the credit at all; families with incomes above \$182,180 in 2009 can claim partial credit.
- your total federal tax liability (line 46 of form 1040) — In one year, you can use as much of the credit as the full amount of your federal income tax liability (which is your tax liability less any other credits). Even if you normally get a refund, you may still have tax liability and could increase the amount of your refund.

* The amount of the adoption tax credit and income restrictions here are based on 2009 amounts. There are cost of living adjustments each year, so for tax years 2010 and beyond the numbers will change. Form line numbers may change as well.

Sample Family Situations

Below are some examples of how the tax credit might benefit families who finalized adoptions in 2009 (these are simplified examples, which do not take into account the Child Tax Credit explained below).

- A couple adopted a sibling group of two children with special needs. They had \$6,500 in federal income tax withheld from their paychecks, and their tax liability is \$7,000, which means they would owe \$500 to the IRS. With the adoption tax credit, they have \$24,300 in credits, and this year they could use up to \$7,000 of the credit (the amount of their federal tax liability). They get a refund of the \$6,500 they had already paid, and can carry over \$17,300 of the tax credit for up to five more years.
- A single mother adopted a sibling group of three children with special needs. She had \$5,000 in federal income tax withheld from her paychecks, but her tax liability is only \$4,000, which means she would receive a refund of \$1,000. For the three children, she has \$36,450 in adoption tax credits. This year she could use \$4,000 of the credit. She will get a refund of the \$5,000 she paid, and can carry over \$31,450 of tax credit for up to five more years.
- A couple with five children adopted a sibling group of two children 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 \$24,300 in the Adoption Tax Credit, but they cannot use it this year since they have no federal tax liability. They should still file Form 8839 with their 2009 tax return so that they can then carry the credit forward for five additional years if their tax liability is greater than zero in those years.

How Do I Claim the Adoption Tax Credit?

To claim the credit you need to complete IRS Form 8839 in addition to filing your usual IRS Form 1040. You can find Form 8839 at www.irs.gov/pub/irs-pdf/f8839.pdf or by requesting it from 800-829-1040.

What do I do when the IRS asks for qualifying expenses on line 5?

Because you do not need to document expenses for children with special needs, simply enter \$12,150 for 2009 as long as your child receives adoption subsidy. If you claimed any credit for expenses associated with this adoption in previous years, you need to deduct those from the total credit. The IRS instructions for 2008 taxes state: "If you did not claim any adoption credit for the child in a prior year, enter \$11,650 on line 5 even if your qualified adoption expenses for the child were less than \$11,650 (and even if you did not have any qualified adoption expenses for this child)."

What if my tax liability is less than the Adoption Tax Credit?

To carry any part of the credit forward to future years, fill out the Credit Carryforward Worksheet in the Instructions for Form 8839. This documents the amount of the credit you can carry forward for up to five additional years or until it is used up, whichever is sooner. You do not need to submit this worksheet, but you will need to complete and submit Form 8839 for any year in which you claim the credit you carried forward.

How does the Adoption Tax Credit affect the Child Tax Credit?

If you can claim your child as a dependent, then you 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 you can claim. To determine

the amount of the Child Tax Credit you can use, you must complete the Child Tax Credit Worksheet in IRS Publication 972.

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

What If We Finalized an Adoption before the Current Tax Year?

If you finalized an adoption in 2003 or a later year for which you have already filed your taxes, you can amend your return to take advantage of the federal adoption tax credit.

If you finalized an adoption before 2003 you probably won't amend your return because:

- you can only get credit for expenses you paid and can document for the adoption process, and
- it has been more than three years since you filed your original return and the instructions for form 1040X state: "Generally, for a credit or refund, Form 1040X must be filed within 3 years after the date you filed the original return..."

In the rare case that you had significant expenses, you might be able to carry the credit forward to returns less than three years old as explained below.

How do I decide if I should amend my previous tax returns?

Your ability to benefit from the credit depends on your federal tax liability in any given year, so first you need to check if you could have benefited from the Adoption Tax Credit in the year you finalized the adoption or in later years.

If your tax liability minus your credits is greater than zero in the year you finalized the adoption—or in any of the next five years—you will benefit from the credit and should amend your taxes. The chart below shows where on your tax form (1040 or 1040A) you can find your tax liability, your credits, and your liability minus your credits. It also lists the maximum amount of the credit per child for that year.

Tax Year	Tax Liability	Total Credits	Liability minus Credits	Maximum Adoption Tax Credit
2003	1040 – Line 43 1040A – Line 28	1040 – Line 53 1040A – Line 35	1040 – Line 54 1040A – Line 36	\$10,160
2004	1040 – Line 45 1040A – Line 28	1040 – Line 55 1040A – Line 35	1040 – Line 56 1040A – Line 36	\$10,390
2005	1040 – Line 46 1040A – Line 28	1040 – Line 56 1040A – Line 35	1040 – Line 57 1040A – Line 36	\$10,630
2006	1040 – Line 46 1040A – Line 28	1040 – Line 56 1040A – Line 34	1040 – Line 57 1040A – Line 35	\$10,960
2007	1040 – Line 46 1040A – Line 28	1040 – Line 56 1040A – Line 34	1040 – Line 57 1040A – Line 35	\$11,390
2008	1040 – Line 46 1040A – Line 28	1040 – Line 55 1040A – Line 34	1040 – Line 56 1040A – Line 35	\$11,650

What if I finalized more than three years ago?

If you finalized before 2006, there is a complication. If you are seeking a refund, the Revenue Code only allows you to amend your tax returns for the last three years. (The three years is calculated based on the date

the taxes were due. A 2006 tax return is due by April 15, 2007, so you can amend 2006 taxes for a refund until April 15, 2010.)

If your tax liability minus credits was or will be greater than zero in any of the years from 2006 on, however, you should still amend your taxes, starting with the year you finalized your adoption. For example, if you finalized the adoption of one child with special needs from foster care in 2005, you should amend your 2005 taxes, figure out how much of the \$10,360 credit you *would* have been able to use that year (which you *cannot* get a refund for), and carry forward the remainder. You would then amend the 2006, 2007, and 2008 taxes (until you've used up the entire credit).

How does the Child Tax Credit affect amended returns?

As described above, you need to complete Publication 972 for each year you are amending to figure out the Child Tax Credit and how much of the Adoption Tax Credit you can claim in that year (and then how much you might carry forward). If you already claimed the Child Tax Credit, you will still need to work through Publication 972's Worksheet to figure out the proper amount of the Adoption Tax Credit you are able to use for a given year. Claiming the Adoption Tax Credit may affect whether you can claim the Child Tax Credit for the year for which you are amending. If your Child Tax Credit is reduced because you claim the Adoption Tax Credit, you should check to see if you can claim the Additional Child Tax Credit instead.

How do I amend my returns?

If you paid someone to prepare your taxes, you should ask them to amend your taxes for free since they failed to include the Adoption Tax Credit.

To amend your own taxes, complete Form 1040X, which can be found at www.irs.gov/pub/irs-pdf/f1040x.pdf or by calling 1-800-829-1040. You will need copies of the returns you filed for each year you amend, plus blank copies of Form 8839 (the Adoption Tax Credit form) for each year you amend. Access previous year's forms at www.irs.gov/formspubs/article/0,,id=98339,00.html.

If you are only amending the tax credits, you can start with line 6 of Form 1040X. The amounts on line 6 should remain the same, but you will note changes to the amounts on lines 7, 8, and 10 (Columns B and C). If you take the Child Tax Credit and/or Additional Child Tax Credit, you may have changes to line 14, Columns B and C, and line 18. Line 23 is the amount of your refund, which you should receive in four to six months.

What If I Have Additional Questions?

If you receive an adoption subsidy (assistance) 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), read NACAC's fact sheet, *Tax Issues Related to Adoption Assistance and Adoption*, which can be found at: <http://www.nacac.org/adoptionssubsidy/factsheets/taxes.html>.

If you have additional questions on the Adoption Tax Credit or adoption subsidy, contact the North American Council on Adoptable Children at 651-644-3036 or adoption.assistance@nacac.org.