

The Adoption Tax Credit: An Ethical Dilemma

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Since 1997, many adoptive families have been able to use the federal adoption tax credit. The credit, however, is due to end in 2010 and some legislators are already proposing to extend the credit indefinitely. New evidence suggests that we must not renew the credit without first ensuring that it furthers the goal of promoting and supporting adoptions from foster care.

What the Numbers Tell Us

A recent Child Trends research brief¹ uses 1999–2005 data from the U.S. Treasury Department to determine who most benefits from the credit. In his report summary, author Rob Geen reveals that:

- “The vast majority of adoption tax credit recipients completed private or foreign adoptions rather than adoptions from foster care.”
- “The tax credit disproportionately supports higher-income families.”
- “The tax credit primarily supports the adoption of younger children.”
- “Nearly all foreign adoptions were supported by the...tax credit, but only one in four foster care adoptions were.”

Children adopted from foster care in 2004 represented just 18 percent of children supported by the credit and 17 percent of money spent. In 2005, about two-thirds of the money spent on the tax credit went to tax filers whose annual incomes surpassed \$74,999. Nearly 90 percent of filers with incomes above \$100,000 adopted internationally or privately, and 71 percent of all families adopted children under age five. Only about 10 percent of higher-income families adopted from foster care, and very few adopted older children.

Parents who adopted foreign children used the tax credit at the highest rate. State Department data indicate that 22,884 children were adopted internationally in 2004. Tax returns suggest that filers claimed 2004 adoption tax credit benefits for 23,296 foreign children.² Roughly 52,000 children were adopted from foster care in 2004, but taxpayers claimed a credit for just 12,432 of those adoptees—less than a quarter of the children adopted from foster care that year.

In NACAC's experience, the low rate of tax credit use by those who adopt children with special needs is linked to two main factors. First, many of these adoptive parents simply do not earn enough taxable income or generate enough tax liability to take advantage of a tax credit. Others who adopt from foster care lack accurate information about the credit and thus never use it.

The Adoption Credit in Perspective

When adoption tax credit legislation was first enacted in 1996 (in H.R. 3286, the Small Business Job Protection Act), Senate Report 104-279 explained the reasoning behind the credit as follows:

The Committee believes that the financial costs of the adoption process should not be a barrier to adoption. In addition, the Committee wishes to encourage further the adoption of special needs

children....

The law set a tax credit limit of \$6,000 per child adopted from foster care versus a \$5,000 credit per child for other types of adoption, and set an income eligibility limit of \$115,000 (\$75,000 for the full credit). The special needs tax credit was exempted from the sunset provision, a clear indication that promoting adoption from foster care was a priority.

Under the Economic Growth and Tax Relief Reconciliation Act of 2001, the credit amount rose to \$10,000 for all adoptions (plus an annual cost-of-living adjustment or COLA). The income eligibility limit doubled to an adjusted gross income of \$150,000 plus COLA for a full credit; the credit phases out at \$190,000 plus COLA. For the 2006 tax year, adoptive parents with adjusted gross incomes of up to \$204,410 could still access a portion of the credit.

Starting in 2003, parents who adopted U.S. children with special needs no longer had to document adoption-related expenses and gained greater access to the credit. In all, between 1999 and 2004, claims on behalf of children with special needs rose 138 percent and dollars spent increased by 613 percent. Despite this upswing, more than 82 percent of adoption tax credit dollars in 2004 still went to support children who were adopted internationally and privately.

Today's reality is that the original intent of the adoption tax credit legislation has been turned upside down. Those who most need support to adopt (lower-income families who are adopting children from foster care) are receiving the least benefit, and those for whom the financial outlay is not a barrier to adoption benefit the most.

Individuals who adopt from foster care often face a different economic situation than others who adopt. Many have a lower taxable income and a comparatively small tax burden. For the adoption tax credit to work, parents must have a substantial tax burden from which they can subtract the credit. The lower the tax owed, the less parents can use. Tax credits are, in fact, better suited to help families who earn enough to owe thousands of dollars in taxes.

It Is Time for Dialogue

The adoption tax credit is clearly not fulfilling a primary goal—that of promoting adoption from foster care. Before we make the credit permanent, members of the adoption community must have an open dialogue about the credit—its intent, its reality, its value for children in foster care who need permanent families. What should the government's role be in helping families privately adopt healthy infants or adopt from other countries? How can we best meet the needs of children who have endured abuse and neglect?

As part of this discussion, we must consider possible answers to key questions:

- **How can we better help those who adopt children with special needs to access the adoption tax credit?** If workers inform parents who adopt children with special needs about the credit and explain that they do not have to document expenses, more may access the benefit.
- **How can we make the credit more available to lower-income families?** A refundable credit, through which parents can receive the entire credit regardless of income, would greatly benefit those who have little or no tax liability. To make the option affordable, however, policy makers may need to revisit the credit amount and income limits.
- **Should the credit be restricted to those who adopt children with special needs?** Should the government, as the legal parent of children in foster care, prioritize the goal of finding homes for foster children over children from other countries and infants for whom demand far outstrips

supply?

- **Are there better ways to promote adoption from foster care?** Instead of assuming that the tax credit is part of a successful adoption promotion strategy, perhaps the federal government should fund proven programs to recruit and retain adoptive families for children in care. Such programs could focus on best practices for promoting adoptions and ensuring their success. As a first step, the government could study which strategies—the tax credit, specialized recruitment programs, post-adoption supports, etc.—truly result in increased adoptions from foster care.
- **Is there a better way to support adoptive families?** In 2005, tax credits used for adoption rose to \$355 million; another \$414 million of credit was carried forward to future tax years. At this rate, the adoption tax credit annually costs the treasury more than it spends on Title IV-B, part 2—the Promoting Safe and Stable Families program. Might not that money be better spent on post-adoption services—crisis mental health services, parent and child support groups, etc.—for all adoptive families who needs support?

The adoption tax credit is the most generous individual tax credit in U.S. tax code today. As an editorial in *The Columbus Dispatch* declared in August, “The tax credit was meant to be a tool to encourage and enable public adoptions, not an entitlement to anyone who adopts.” If we are to move ahead with the best interests of waiting children in mind, the adoption tax credit conversation needs to start now.

1 “The Adoption Tax Credit: Is It an Effective Approach to Promote Foster Care Adoption?”

2 Because parents who adopt internationally can claim expenses even when an adoption falls through, the number of credits claimed can legally exceed the number of adoptions finalized.

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