EMPLOYER-SPONSORED PROGRAMS

Adoption Benefits

While not as common as child-care assistance, adoption benefits are provided by some employers. In general, adoption benefit policies reimburse employees for the legal, adoption agency, court, and medical fees surrounding an adoption and, less frequently, for temporary foster care expenses and related transportation and lodging costs. Such policies also can provide time off, either paid or unpaid, to employees who adopt a child. (See the chapter on Parental/Family & Medical Leave at 335:225.)

Some of the reasons employers offer adoption assistance benefits include the following:

- to ensure the provision of comparable benefits to all employees, whether they become parents by birth or adoption;
- to generate employee goodwill; and
- to round out a larger work-and-family benefit program. (See the chapter on Work/Life Benefits at 341:101.)

Basic Requirements

Employees may exclude from gross income amounts received as reimbursement for adoption expenses under employer-sponsored adoption assistance programs. I.R.C. §137 authorizes employer-sponsored programs.

[irc USC 137J I.R.C. § 137 defines an adoption assistance program as a separate written plan of the employer's that provides benefits exclusively for its employees. The plan must provide employees with adoption assistance.

In addition, the employer-sponsored plan must meet requirements similar to the requirements for educational assistance programs described in I.R.C. §§ 127(b)(2), 127(b)(3), 127(b)(5), and 127(b)(6). This means that the adoption assistance program must not do the following:

- favor highly compensated employees;
- provide more than 5 percent of the amounts paid or incurred for adoption assistance to the class of individuals who are 5-percent shareholders or owners;
- require the program to be funded;
- fail to provide to eligible employees reasonable notice of the availability and terms of the program.

Employers should report amounts paid or expenses incurred for qualified adoption expenses on Form W-2. In IRS Announcement 96-134, IRS provides the Form W-2 reporting instructions for adoption benefits. Employer payments under an adoption assistance plan for qualified adoption expenses should be reported as Code T in Box 13.
In Announcement 97-64, IRS clarifies that the Form W-2 must reflect the total amount paid or reimbursed by an employer for qualified adoption expenses under an adoption assistance program, including those benefits paid under a cafeteria plan and benefits paid in excess of the $5,000 (or $6,000) exclusion amount. The only amounts not included on the form are adoption benefits forfeited from a cafeteria plan. After Dec. 31, 2001, the exclusion amount is $10,000, including special needs adoptions. Qualified expenses paid or incurred in taxable years beginning on or before Dec. 31, 2001, are subject to the SBPJA dollar limits.

Employees must include excess or unqualified reimbursements as taxable income on their individual income tax form. Because employers will not withhold taxes on any reimbursements under an adoption assistance program, employees may want to adjust amounts withheld on other wages (Form W-4) or make estimated tax payments to avoid potential penalties for underpayment on any taxable portion of a reimbursement.

The 2001 Tax Act provisions permanently extend the adoption credit for children other than special needs children.

Adoption Tax Credit

Tax code § 23, as added by the Small Business Job Protection Act of 1996, allows individuals to credit against income tax their qualified adoption expenses, up to certain limits.

The adoption tax credit is allowed for the taxable year following the taxable year in which the adoption becomes final. For expenses paid or incurred during or after the taxable year in which the adoption becomes final, the credit is allowed in the taxable year the expenses are incurred or paid. For special needs adoptions, the 2001 Tax Act provides the tax credit and exclusion from income regardless of whether the taxpayer has qualified adoption expenses, effective for taxable years beginning after Dec. 31, 2002.

The tax credit cannot be used if an expense is deductible or credited under any other tax code provision or is reimbursed by another state, federal, or local program. Unused credits may be carried forward for up to five years.

As with other types of tax credits, married taxpayers must file joint returns. In addition, taxpayers must provide the IRS with the child's name, age, and taxpayer identification number on their tax return. IRS may require other information to be provided, including the name of the agent assisting with the adoption, if the information described is unavailable.

Tax code § 23(g) provides that a taxpayer may not increase its basis in property for capital improvements required as a condition of adoption (such as a wheelchair ramp) if the tax credit were allowed for the cost of the improvement. However, if the cost of the improvement tax credit were allowed, the excess may be added to the taxpayer's basis in the property.

Employer Policies

Following are examples of employer policies that cover some portion of employees' expenses related to the adoption of a child, in addition to providing time off:
Example: Campbell Soup Company has an adoption-assistance program and a family-care leave of absence policy that covers time off for adoption.

The adoption policy provides for reimbursement of up to $3,000 per adopted child. The benefits are available to all regular full-time and part-time salaried employees. Reimbursement is provided to eligible employees for public or private adoption agency fees, court fees, and legal fees. The company pays all payroll taxes on the reimbursement. Time off for adoption is granted in accordance with the Personal Time policy or practice covering specific employees.

Employees also have access to the Employee Work/Life Assistance Program that provides information on:

- adoption possibilities;
- adoption agencies;
- financing;
- legalities and lawyers;
- support networks;
- information-sharing with children; and
- searching for birth parents and relatives.

Example: The adoption program at General Mills provides financial assistance for adoption expenses. The assistance is 80 percent of adoption-related expenses, up to a maximum of $5,000. In addition, workers who adopt a child are eligible for time off under the company's parental leave policy.