

Part III - Administrative, Procedural, and Miscellaneous

26 CFR 601.105: Examination of returns and claims for refund, credit, or abatement; determination of correct tax liability.
(Also Part 1, §§ 23, 137.)

Rev. Proc. 2005-31

SECTION 1. PURPOSE

This revenue procedure provides safe harbors for determining the finality of an adoption of a foreign-born child for federal income tax purposes. It finalizes the revenue procedure proposed in Notice 2003-15, 2003-1 C.B. 540.

Announcement 2005-45, 2005-27 I.R.B., discusses the comments received in response to Notice 2003-15 and the changes made by this revenue procedure to the proposed revenue procedure. This revenue procedure also provides guidance on the treatment of re-adoption expenses.

SECTION 2. BACKGROUND

.01 Section 23 of the Internal Revenue Code allows a credit for qualified adoption expenses (QAE) paid or incurred by an individual in connection with the adoption of an eligible child. Section 137 provides an exclusion from an employee's gross income for QAE paid or incurred by the employer under an adoption assistance program. See Notice 97-9, 1997-1 C.B. 365, for general guidance concerning the credit under § 23 and the exclusion under § 137.

.02 QAE are defined in § 23(d)(1) and Notice 97-9 as reasonable and necessary adoption fees, court costs, attorney's fees, traveling expenses (including amounts expended for meals and lodging) while away from home, and other expenses directly related to, and for the principal purpose of, the legal adoption of an eligible child by the taxpayer.

.03 Under § 23(d)(2), an eligible child is an individual who has not attained age 18 or who is physically or mentally incapable of caring for himself. Section 23(d)(1)(C) provides that a stepchild is not an eligible child.

.04 Section 23(a)(2)(A) provides the general rule that, for QAE paid or incurred before the taxable year in which the adoption is final, the credit is allowed in the taxable year that follows the taxable year in which the QAE are paid or incurred. For QAE paid or incurred during or after the taxable year in which the adoption is final, the credit is allowed for the taxable year in which the QAE are paid or incurred. Sec. 23(a)(2)(B). For a foreign adoption, however, § 23(e) provides that (1) the credit is allowed only if the adoption becomes final, and (2) QAE paid or incurred in any taxable year before the taxable year in which the adoption becomes final are treated as paid or incurred in the taxable year in which the adoption becomes final. Rules similar to those under § 23(e) apply under § 137(e) for purposes of the exclusion for employer-provided adoption assistance.

.05 The Intercountry Adoption Act of 2000, Pub. L. 106-279, 42 U.S.C. §§ 14901-14954 (IAA), will implement the Hague Convention on Protection of Children and Co-operation in Respect of Intercountry Adoption (the Convention).

See Senate Treaty Doc. 105-51 (Sept. 20, 2000). When the Convention enters into force in the United States, the IAA generally will apply to Convention adoptions (adoptions in which both the sending and the receiving countries are parties to the Convention).

.06 Section 301 of the IAA (42 U.S.C. § 14931) provides rules for certification of Convention adoptions. A Convention adoption subject to the IAA will be final for federal income tax purposes (1) in the taxable year for which the Secretary of State certifies as final an adoption subject to § 301(b), or (2) in the year in which the state court enters a final decree of adoption for an adoption subject to § 301(c).

.07 A discussion of the IAA and the Convention can be found in Hague Convention on Intercountry Adoption; Intercountry Adoption Act of 2000; Accreditation of Agencies; Approval of Persons; Preservation of Convention Records, 68 Fed. Reg. 54064 (September 15, 2003) (proposed rules to be codified at 22 C.F.R. pts. 96, 98). General information about foreign adoptions can be accessed through the Department of State web site at <http://www.state.gov> and the Department of Homeland Security web site at <http://www.immigration.gov>.

SECTION 3. SCOPE

This revenue procedure applies to taxpayers who claim the adoption credit or exclusion for QAE paid or incurred in connection with the adoption of a foreign-born child, except adoptions for which the Convention and the IAA determine finality. This revenue procedure does not apply to the adoption of a

child who is a citizen or resident of the United States at the time the adoption process commences.

SECTION 4. DEFINITIONS

The following definitions apply for purposes of this revenue procedure.

.01 Foreign-born child. An eligible child (within the meaning of § 23(d)(2)) who is not a citizen or resident of the United States at the time the adoption process commences.

.02 Orphan. A foreign-born child who is under the age of 16 at the time an immigration petition is filed on the child's behalf, and

(1) who has suffered the death or disappearance of, or abandonment or desertion by, or separation from or loss of, both parents, or

(2) for whom the sole or surviving parent is incapable of providing the proper care and has in writing irrevocably released the foreign-born child for emigration and adoption.

.03 Foreign-sending country. The country of citizenship of a foreign-born child, or if the foreign-born child is not permanently residing in the country of citizenship, the country of the child's habitual residence before adoption. See 8 C.F.R. § 204.3(b) (2005).

.04 Competent authority. A court or governmental agency of the foreign-sending country with jurisdiction and authority to make decisions in matters of child welfare, including adoption (as provided in 8 C.F.R. § 204.3(b) (2005)).

.05 Home state. The state (including the District of Columbia and possessions) in which the adopted child and adoptive parents make their habitual

residence in the United States, or in which the child is adopted.

.06 Full and final adoption. An adoption of an orphan in which the competent authority of the foreign-sending country enters a decree of adoption establishing a parent-child relationship under the laws of the foreign-sending country and both adoptive parents (in adoptions by two parents) or the sole adoptive parent (in adoptions by one parent) see the orphan before or during the adoption proceeding.

.07 Simple adoption. An adoption of an orphan in which the competent authority of the foreign-sending country enters a decree of adoption establishing a parent-child relationship under the laws of the foreign-sending country, in which one or both of the adoptive parents do not see the orphan before or during the adoption proceeding.

.08 Re-adoption. An adoption or other recognition proceeding under home state law occurring after the entry of a foreign-born child into the United States under an "immediate relative" IR2, IR3, or IR4 (simple adoption) visa.

.09 IR2 visa. A visa issued to a foreign-born child who is not an orphan, who was adopted in the foreign-sending country while under the age of 16 years, and who has been in the legal custody of, and has resided with, the adoptive parent or parents for at least 2 years.

.10 IR3 visa. A visa issued to an orphan after a full and final adoption of the orphan has occurred in the foreign-sending country. An IR3 visa is issued if (1) the competent authority of the foreign-sending country severs the parental rights of the biological or any previous adoptive parents and establishes a parent-

child relationship between the orphan and the adoptive parent or parents, and (2) both adoptive parents (in adoptions by two parents) or the sole adoptive parent (in adoptions by one parent) see the orphan before or during the adoption proceeding.

.11 IR4 visa. A visa issued to an orphan if (1) a simple adoption occurs in the foreign-sending country, or (2) the competent authority of the foreign-sending country grants legal guardianship or custody either to the prospective adoptive parent or parents or to an individual or agency acting on behalf of the prospective adoptive parent or parents.

SECTION 5. APPLICATION

.01 Finality of adoption of foreign-born child.

(1) In general. For purposes of the adoption credit and the exclusion for employer-provided assistance for QAE, the Internal Revenue Service will treat an adoption of a foreign-born child for which the Convention and the IAA do not determine finality as final if:

(a) a competent authority of a foreign-sending country has entered a decree of adoption with respect to the foreign-born child or has authorized the child to leave the foreign-sending country under a guardianship or legal custody arrangement; and

(b) the child receives an IR visa from the Department of State.

(2) Taxable year of finality safe harbors.

(a) Children who receive an IR2, IR3, or IR4 (simple

adoption) visa. The Service will not challenge a taxpayer's treatment of the adoption of a child who receives an IR2, IR3, or IR4 (if the child was adopted in a simple adoption) visa as final in:

(i) The taxable year in which the competent authority enters a decree of adoption; or

(ii) The taxable year in which a home state court enters a decree of re-adoption or the home state otherwise recognizes the decree of the foreign-sending country, if that taxable year is one of the next two taxable years after the taxable year in which the competent authority enters the decree.

(b) Children who receive an IR4 visa (guardianship or legal custody). The Service will not challenge a taxpayer's treatment of the adoption of a child who was subject to a guardianship or legal custody arrangement and who receives an IR4 visa as final in the taxable year in which a home state court enters a decree of adoption.

.02 Re-adoption expenses. Otherwise qualified expenses paid or incurred in connection with a re-adoption satisfy the requirement that expenses be "reasonable and necessary" for purposes of determining whether the expenses are QAE.

SECTION 6. EFFECTIVE DATE

This revenue procedure is effective for QAE paid or incurred after June 15, 2005. However, the Service will not challenge the time of finality of adoptions by taxpayers who apply this revenue procedure or Notice 2003-15 to QAE paid

or incurred on or before June 15, 2005, in a taxable year for which the period of limitation under § 6511 has not expired.

SECTION 7. EFFECT ON OTHER DOCUMENTS

Notice 2003-15 is modified and, as modified, is superseded.

DRAFTING INFORMATION

The principal author of this revenue procedure is Marilyn E. Brookens of the Office of the Associate Chief Counsel (Income Tax & Accounting). For further information regarding this revenue procedure, contact Ms. Brookens at (202) 622-4920 (not a toll-free number).