F I S C A L   I M P A C T   R E P O R T

ORIGINAL DATE 2/19/15

SPONSOR Baldonado **LAST UPDATED** **HB** 476

SHORT TITLE Increase Special Needs Adoption Tax Credit **SB**

ANALYST Graeser

REVENUE (dollars in thousands)

Estimated Revenue					Recurring or Nonrecurring	Fund Affected
FY15	**FY16**	**FY17**	**FY18**	**FY19**		
	($785.0)	($785.0)	($785.0)	(785.0)	Recurring	General Fund

(Parenthesis ( ) indicate revenue decreases

SOURCES OF INFORMATION
LFC Files

Responses Received From
Taxation and Revenue Department

SUMMARY

Synopsis of Bill

House Bill 476 increases the special needs adoption tax credit from $1,000 per adoption to $1,500 per adoption. The bill also requires TRD to compile and deliver to the Revenue Stabilization and Tax Policy interim committee a report on utilization of this credit and the benefits accruing to the credit.

There is no effective date of the bill, assume 90 days after adjournment or June 19, 2015. The provisions of the act are applicable to the 2015 tax year, so that the first fiscal impact will be with returns filed on or before April 15, 2016.

FISCAL IMPLICATIONS

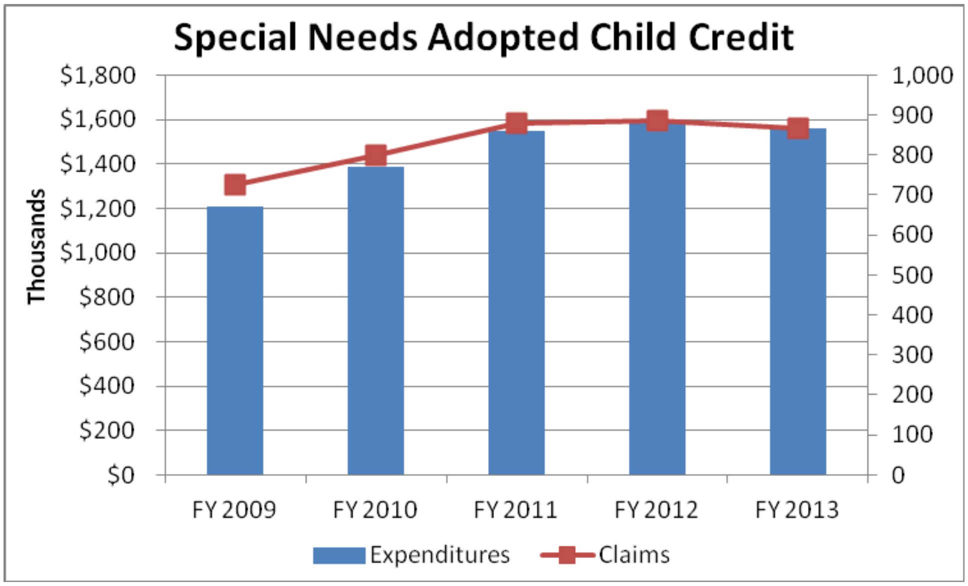

Figure 1 -- Source: TRD's 2014 Tax Expenditure Report

The FY 11, 12 and 13 claims for this credit have averaged about 875 in number and $1,560,000 in annual cost to the General Fund. This represents an average credit per adopting family of about $1,700 per claim. This is consistent with around 200 families adopting a single child and the remainder adopting two or more. Once a child qualifies the taxpayer for the credit, the credit amount may be claimed each year that the child is a dependent. After peaking in 2012, very few new adoptions have qualified for this tax credit.

Increasing the credit amount is unlikely to increase, to any noticeable extent, the number of adoptions, because the federal government offers a far more generous non-refundable special needs adoption credit of $13,190 per child adopted in 2014.

However, the combination of the $1,000 State non-refundable tax credit and the approximately $13,000 Federal non-refundable tax credit per child may have had a significant impact on aggregate adoptions. In the analysis of 2007's HB 973, it was assumed that 350 families would adopt 600 special needs children for an average of $1,700 in tax credit per family. By 2011, 879 families had adopted 1,550 special needs children – about double the original estimate.

The $500 additional per child pursuant to the increase proposed in this bill, represents a 3.5 percent increase in direct tax credits and a significantly lower percentage in terms of total tax benefits, including the child tax credit, the child care credit, the personal exemption and these special needs child adoption credits. Even assuming that the higher increase obtains, an additional 55 children would be adopted at a marginal general fund cost of $14,000 per child.

See comments below on measuring benefits attributable to this proposal.

This bill may be counter to the LFC tax policy principles of adequacy, efficiency, accountability and equity. Due to the increasing cost of tax expenditures revenues may be insufficient to cover growing recurring appropriations. However, the costs to the general fund may be offset to some extent by the benefits accruing to society from ensuring that children leave foster care and get started on a productive life path. While the costs of this tax expenditure are relatively easy to measure, since the credits and separately reported, the benefits are very difficult to measure, since they can affect a lifetime of public expenditures.

SIGNIFICANT ISSUES

There is general agreement that getting all children, but especially special needs children (as defined by Federal law), out of foster care as soon as possible in life and into adoptive families will result in a lifetime of benefits to society. Most studies of these lifetime costs quote a panel study by Rand Corporation, entitled "Proven Benefits of Early Childhood Interventions.[1]" While the study addresses prekindergarten education, the results of the study may quantify some of the benefits of early adoption, as well.

The bill asks the Taxation and Revenue Department to compile the data and prepare a report on the costs and benefits of this special needs adoption. The costs are relatively easy to determine, since the credit is claimed as a separate line on the PIT-1 form filed with TRD. Measuring the benefits, however, will be very difficult one compelling reason:

- TRD has expertise in tax administration and tax policy, including compiling data on the costs of this tax credit. CYFD is highly conversant with issues of children and families and, in particular, the lifetime benefits accruing to adopting younger children out of foster care. If the bill assigned both agencies to the preparation of the required report, then the report would have credence. If assigned to TRD alone, then the benefit side of the report would be deficient. If assigned to CYFD, then the economic expertise of the TRD analysts would be lost.

PERFORMANCE IMPLICATIONS

Although the LFC tax policy of accountability is met since TRD is required in the bill to report annually to an interim legislative committee regarding the data compiled from the reports from taxpayers taking the deduction and other information to determine whether the deduction is meeting its purpose. However, the determination of benefits accruing to adoption are far beyond TRD's expertise.

ADMINISTRATIVE IMPLICATIONS

The required report will require a great deal of effort at TRD to quantify the benefits accruing to adoption of special needs children. The report may be somewhat deficient, since TRD has little if not expertise in quantifying the lifetime benefits accruing to adoption. See, for example, the rough calculation of maximum increase in number of adoptions assuming a unit tax subsidy elasticity.

OTHER SUBSTANTIVE ISSUES

Although LFC frequently recommends enacting most tax expenditures with a sunset date, TRD notes in its 2014 Tax Expenditure Report that the legislature can always bring a particular tax

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[1] **http://www.rand.org/pubs/research_briefs/RB9145.html**

expenditure up for review by having an interim committee schedule that review or by an individual member propose to amend the tax expenditure and have the effect of the provision debated in committee.

LG/bb