

Interest on Auto Loans

Quick-Take: The new Tax Act provides a new auto interest loan deduction, but how many borrowers will really benefit once all the law's conditions are satisfied?

Background: A new provision under the One Big *Beautiful* Bill (no comment on that title!) provides for no tax on car loan interest. [Section 70203.] Translated, new IRC 163(h)(4) provides for a tax deduction for interest on *certain* auto loans that is available to individuals who are below specified modified adjusted gross income (MAGI) levels, whether they itemized their deductions or not. Some key conditions to claim this income tax deduction include the following:

Deduction Duration: This auto interest deduction is available **2025 through 2028**.

New Vehicles: While the House version of this new provision applied it to new or used vehicles, the Senate's version of the final bill requires that it applies only to **new** vehicles.

Income Levels: The income levels are low relative to the average price of a new vehicle, which now hovers close to \$50,000 a vehicle. The eligible individual must have a **marginal tax rate of 10%, 12%, or 22%**. Accordingly, those individuals may find that the tax savings obtained with this new deduction may be less than the money savings that they might otherwise enjoy if they purchased a used car, when they have to spend money on a *new* vehicle just to become eligible to claim this new tax deduction, comparing the cost differential between new and used vehicles.

Deduction Phaseout: Like many other provisions under the new Tax Law, there is a **phaseout** of the deduction; it reduces otherwise the deductible amount by \$200 for each \$1,000 or portion thereof by which the purchaser's MAGI exceed \$100,000 (\$200,000 if married filing jointly.) MAGI is defined to be AGI + Sections 911, 931, and 933 exclusions.

Reporting: The new vehicle purchased must have its **VIN reported on the purchaser's income tax return**.

No Itemization: This auto interest tax deduction is from adjusted gross income, even if the purchaser does not itemize his/her other deductions. This deduction apparently is also allowed for the alternative minimum tax (AMT.)

Qualified Passenger Vehicle Loan Interest: This is regarding any debt incurred **after** 2024 for the purchase of, and secured by, a first lien on 'applicable passenger vehicle' for **personal use**. It may include refinancing of such debt that does not exceed the balance at the refinancing date. It **excludes related-party financing**.

Deduction Limit: The interest deduction cannot exceed **\$10,000 in any one year**.

U.S. Assembly: The vehicle must be manufactured primarily for use on public roads. It must have at least two wheels. (I'm glad Congress included this- I'd hate to see an expensive one-wheel unicycle covered.) It must be a car, minivan, SUV, pickup truck, or motorcycle. It must be treated as a motor vehicle under Title II of the Clean Air Act. It must have gross vehicle weight of less than 14,000 pounds. Finally, it must have **final assembly in the U.S.** [IRC 163(h)(4)(E)(i).]

Lenders: A lender is required to issue information if interest is \$600 or more, and it must also report origin date of loan and the year, make, model and VIN of the vehicle, and any other information that the IRS might require.

Lost Revenue: With this new income tax deduction, it is projected that it will cost the government \$30 billion in revenue over the next 4 years.

Conclusion: Most folks who will qualify to claim this new auto loan interest deduction will probably not have \$10,000 of interest expense a year. Also, the phaseout level starts at low amounts for individuals who are likely to be able to afford a new car. And as mentioned, given the price differential between new and used cars, the tax-savings of deducting loan interest will probably not be enough to justify purchasing a new car just to claim the

interest deduction. Not to mention the additional paperwork burden the law places on lenders, that tend to pass through those additional costs to borrowers.

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