Tax & Business Alert – December 2025

Abstract: Generally, except for home mortgage interest, personal interest expense isn't deductible for federal income tax purposes. Now, the One Big Beautiful Bill Act has added another exception for eligible car loan interest on qualified passenger vehicles. This article covers the eligibility rules.

How does the new tax deduction for car loan interest work?

Generally, except for home mortgage interest, personal interest expense isn't deductible for federal income tax purposes.
With the passage of the One Big Beautiful Bill Act (OBBBA), another exception has been added. That is, you might be able to deduct your car loan interest. But various rules and limits apply.

The specifics

The OBBBA allows eligible individuals, including those who don't itemize deductions, to deduct some or all the interest on a car loan they take out to purchase a qualifying passenger vehicle. The maximum car loan interest you can deduct is $10,000 per year, for 2025 through 2028.

But the deduction is phased out starting at $100,000 of modified adjusted gross income (MAGI) or $200,000 for married couples filing jointly. For an unmarried individual, the deduction is completely phased out when MAGI reaches $150,000, and for married joint filers, the phaseout is complete when MAGI reaches $250,000.

Another limit is that only certain vehicles qualify for the deduction:

- The vehicle must be a car, minivan, van, SUV, pickup truck or motorcycle with a gross vehicle weight rating under 14,000 pounds,
- The vehicles must have been manufactured primarily for use on public streets, roads and highways,
- The vehicle must be new, and
- The "final assembly" of the vehicle must have occurred in the United States.

You must report the vehicle identification number (VIN) on your tax return. A car assembled in the United States has a special VIN to signify that it's American-made.

Loan-related requirements

The loan must be taken out after 2024 and must be a first lien secured by a vehicle used for personal purposes. If an original qualified car loan is refinanced, the new loan will be a qualified loan for purposes of the deduction as long as: 1) the new loan is secured by a first lien on the eligible vehicle, and 2) the initial balance of the new loan doesn't exceed the ending balance of the original loan.

Also be aware that interest on loans from certain related parties doesn’t qualify. And lease financing isn’t eligible.

To claim the deduction, you’ll need to substantiate how much interest you paid during the year. For that, your car loan lender must file an information return with the IRS specifying the amount.

Final thoughts

The new deduction for auto loan interest can make buying a car less expensive. But you need to consider the eligibility requirements. First, is your income below the phaseout threshold? Second, have you checked that the car you’re considering will qualify? Also, don’t make a decision based solely on the ability to qualify for the tax deduction. In some cases, buying a used or foreign vehicle or leasing a vehicle might make more sense, even if you won’t be able to claim a tax deduction. Finally, keep in mind that the deduction will expire after 2028 unless Congress acts to extend it.

Have questions about the deduction? Contact us.