

Car Loan Interest Deduction Final Regulations

Cross References

- TD 10054

Effective for indebtedness incurred after December 31, 2024, a taxpayer may deduct up to \$10,000 of qualified passenger vehicle loan interest, regardless of whether the taxpayer claims the standard deduction or itemizes. The IRS recently issued final regulations that provide guidance on implementing this new deduction. The final regulations in general adopt the proposed regulations published in January of 2026, with a few minor clarifications. The following is a summary of some of the provisions contained in the final regulations.

QPVLI. IRC section 163(h)(4) defines qualified passenger vehicle loan interest (QPVLI) as interest that is paid or accrued during the tax year on indebtedness incurred after December 31, 2024, for the purchase of, and that is secured by a first lien on, an applicable passenger vehicle (APV) for personal use. The regulations state that interest is QPVLI only if the interest is paid or accrued on a specified passenger vehicle loan (SPVL) that is secured by a first lien on the purchased APV at the time the taxpayer pays or accrues interest on that SPVL. A lender's release of a lien typically occurs following the borrower's final payment on the related indebtedness. Thus, at the time of the final payment, an SPVL would typically still be secured by a lien on the purchased APV.

The final regulations clarify that QPVLI also includes prepaid interest in the form of points and deferred or capitalized interest. QPVLI may also include origination-related or financing-related charges, prepayment penalties, late-payment charges, default-related charges, and similar fees.

Estates and trusts. The regulations provide that only individuals, decedents' estates, and non-grantor trusts (including with respect to a grantor trust or disregarded entity deemed owned by the individual, decedent's estate, or non-grantor trust) may deduct QPVLI. This is because only those taxpayers could be considered to have purchased an APV for personal use.

QPVLI exceptions. QPVLI does not include amounts paid or accrued on:

- 1) A loan to finance fleet sales,
- 2) A loan incurred for the purchase of a commercial vehicle that is not used for personal purposes,
- 3) Any lease financing,
- 4) A loan to finance the purchase of a vehicle with a salvage title, or
- 5) A loan to finance the purchase of a vehicle intended to be used for scrap or parts.

Lien on APV substitutes. The regulations permit the substitution of collateral on the SPVL in limited circumstances. If an SPVL is secured by a first lien on an APV that is

replaced with a substitute APV due to an unforeseen intervening event, and the lien is transferred to that substitute APV under the loan documentation terms, the indebtedness will continue to be treated as an SPVL. Unforeseen intervening events would include a defective APV required to be replaced under State or other applicable lemon laws, or an APV that is required to be replaced by insurance.

First lien. The regulations state that “secured by a first lien” means a valid and enforceable security interest in an APV with priority ahead of all other security interests, other than tax liens or other similar security interests that may be given higher priority at a later date following the date of purchase and only in limited circumstances. This exception clarifies that so-called springing liens that result due to the operation of State or other applicable law and that may be given a higher priority at a later date following the date of purchase, such as a tax lien arising due to the non-payment of State property taxes, do not prevent the APV from being secured by a first lien.

The final regulations clarify that an SPVL is secured by a first lien if the lender holds the first voluntary security interest recorded against the vehicle. Any involuntary liens are disregarded even if given temporary higher priority at a later date.

An SPVL may be considered secured by a first lien even if the lien has not yet been perfected or recorded. A first lien also applies when the lien is removed in connection with the taxpayer no longer owning the vehicle but the taxpayer continues to be liable for repayment of the loan.

SPVL. The regulations state that an SPVL includes indebtedness incurred for the purchase of an APV, plus any other items or amounts customarily financed in an APV purchase, such as vehicle service plans, extended warranties, sales taxes, and vehicle-related fees. An SPVL does not include indebtedness representing negative equity under an existing loan on a trade-in vehicle that is rolled over into the loan on the purchase of the new vehicle. An SPVL does not include indebtedness to purchase collision and liability insurance. An SPVL does not include indebtedness on property such as a boat or trailer that is included with the purchase of the APV.

A taxpayer must allocate the debt on a pro rata basis when the loan includes the purchase of non-APV items.

Refinanced SPVL. A new loan resulting from refinancing an SPVL is an SPVL if the new loan is secured by a first lien on the APV with respect to which the refinanced SPVL was incurred, but only to the extent the amount of the new loan does not exceed the amount of the refinanced SPVL. The final regulations clarify that the amount of the new loan that is an SPVL is limited to the outstanding balance of the refinanced SPVL as of the date of the refinancing. If there is a change in obligor as part of the refinancing, the new loan is not an SPVL with regard to any obligor other than the original obligor, unless the refinancing is in connection with a change in obligor by reason of the obligor’s death.

Likewise, if an obligor incurs an SPVL and subsequently is replaced by a different obligor on the same loan, the indebtedness is no longer an SPVL, except in the case of the death of the original obligor.

APV. An APV means any vehicle:

- 1) The original use of which commences with the taxpayer,
- 2) That is manufactured primarily for use on public streets, roads, and highways (not including a vehicle operated exclusively on a rail or rails),
- 3) That has at least 2 wheels,
- 4) That is a car, minivan, van, sport utility vehicle, pickup truck, or motorcycle,
- 5) That is treated as a motor vehicle for purposes of title II of the Clean Air Act, and
- 6) That has a gross vehicle weight rating of less than 14,000 pounds.

An APV does not include any vehicle the final assembly of which did not occur within the United States.

Original use. Original use commences with the first person that takes delivery of a vehicle after the vehicle is sold, registered, or titled. In the case of a dealer, original use does not commence with the dealer unless the dealer registers or titles the vehicle to itself (for example, in the case of certain demonstrator vehicles or loaner vehicles). The regulations recognize that dealers may operate vehicles prior to the sale to retail purchasers in a manner that does not require the vehicle to be registered or titled under state or other applicable law, and that operation of the vehicle in this manner would not result in original use commencing with the dealer. For example, if a dealer uses a vehicle for test drives or as a demonstrator vehicle, and state or other applicable law does not require the dealer to register or title the vehicle, original use of that vehicle would not commence with the dealer.

On the other hand, if dealer operation requires the vehicle to be registered or titled, original use would commence with the dealer. For example, if a dealer uses a vehicle as a courtesy car loaned to customers in connection with servicing or repairing vehicles and state law requires the dealer to register or title the vehicle, original use of that vehicle would commence with the dealer.

The final regulations clarify that original use does not commence with a lessee if the lessee purchases the vehicle during or at the end of the lease term.

Final assembly. The final assembly point is listed on the vehicle information label attached to each vehicle on a dealer's premises. The regulations state that to establish that final assembly occurred within the United States, the taxpayer may rely on:

- 1) The vehicle's plant of manufacture as reported in the VIN, or
- 2) The final assembly point reported on the label affixed to the vehicle.

Personal use of the APV. Personal use means use by an individual other than in any trade or business (except for use in the trade or business of performing services as an employee) or for the production of income. Costs of commuting between an individual's home and regular place of work are personal expenses.

IRC section 163(h)(4) does not require that a vehicle be purchased exclusively for personal use. The regulations provide that a taxpayer is considered to purchase that APV for personal use if, at the time the indebtedness is incurred, that taxpayer expects that the APV will be used for personal use by the taxpayer that incurred the indebtedness, or by certain members of the taxpayer's family and household, for more than 50% of the time.

In the case of a decedent's estate or non-grantor trust, personal use is determined based on the expected personal use of the vehicle by the legatees or heirs, or beneficiaries who have present or future interest in such decedent's estate or non-grantor trust, a spouse of such legatees, heirs, or beneficiaries, or an individual who is related to such legatees, heirs, or beneficiaries, or a combination of these individuals.

The personal use requirement is a requirement that must be satisfied in connection with the incurrence of indebtedness, as opposed to an ongoing requirement. As a result, a taxpayer is not required to re-evaluate personal and non-personal use in tax years after the indebtedness is incurred. Differences between expected use and later actual use do not affect the taxpayer's eligibility to deduct QPVLI, nor the amount of the taxpayer's QPVLI. The personal use requirement must be determined to be met at the time the indebtedness is incurred.

Non-personal use and independently deductible interest. Under certain circumstances, a taxpayer may deduct interest that is QPVLI as a different type of interest. For example, taxpayers paying interest attributable to a vehicle used in a trade or business may be able to deduct that interest as a business interest expense.

Independently deductible interest means interest paid or accrued that is QPVLI and that also is deductible as a different type of interest (such as business interest). The regulations clarify that taxpayers may take any available interest deductions permitted under IRC section 163 or a different code section, but a taxpayer may not deduct more total interest than otherwise is allowable. A taxpayer must report any amount of independently deductible interest that is deducted in a tax year as non-QPVLI on Form 1040 Schedule 1-A or other relevant form.

Author's Comment

For example, a taxpayer who expects to use a vehicle 60% for personal purposes and 40% in a Schedule C business meets the more-than-50% personal use requirement. The taxpayer could deduct 40% of the interest as business interest and the remaining 60% as QPVLI. The 40% claimed as business interest on Schedule C would also have to be listed as non-QPVLI on Form 1040 Schedule 1-A.

Reporting rules. The final regulations also provide guidance under IRC section 6050AA for the operational, administrative, and definitional rules for persons in a trade or business who receive interest on an SPVL to comply with the statutory information reporting requirements with respect to receipt of interest.