

Will the Interest on Your Vehicle Loan be Deductible?

Article Highlights:

- Vehicle loan interest
- Consumer loans secured by the vehicle
- Using home equity loans to create deductibility
- Exercising restraint when using home equity

Whether or not the interest you pay on a loan to acquire a vehicle is deductible for tax purposes depends how the vehicle is being used (for business or personal purposes), the tax form on which the expenses are being deducted, and the type of loan.

If the loan were a consumer loan secured by the vehicle, then the following rules would apply:

- If the vehicle is being used partially for business and the expenses are being deducted on your self-employed business schedule, then the business portion of the interest will be deductible as business interest, but the personal portion will not.
- If the vehicle is being used partially for business as an employee and the expenses are being deducted as an itemized deduction, then neither the business portion nor the personal portion of the interest will be deductible.
- If the vehicle is entirely for personal use, then none of the interest will be deductible, because the only interest that is still deductible as an itemized deduction is home mortgage interest and investment interest.

As an alternative to a nondeductible consumer loan, you might consider acquiring that vehicle with a home equity line of credit. Generally, current law allows individual taxpayers to borrow up to \$100,000 of home equity and deduct the interest on that loan as home mortgage interest. This would also apply to the purchase of a vehicle or motor home. Using a home equity line will generally make the interest deductible.

Before borrowing against the home, you should consider the following:

- Treat the home equity loan like a consumer loan and pay it off over the same period of time you would have had to pay the consumer loan. Otherwise, you may reach retirement age without having the home paid for.
- When buying a car, you can sometimes get very favorable interest rates or a rebate. To determine which is best, compare the difference in total loan payments over the life of the loans to the rebate amount.
- It is also good practice to make sure the benefit of making the interest deductible is greater by using the home equity line of credit than the benefit of the low interest consumer loan or the rebate.
- If there is any chance of defaulting on the loan, the repercussions from defaulting on a home loan are far more serious than on consumer debt.

If you need assistance in deciding on a course of action, please call our office.