Date of Hearing: May 5, 2025

ASSEMBLY COMMITTEE ON REVENUE AND TAXATION
Mike Gipson, Chair

AB 490 (Tangipa) – As Introduced February 10, 2025

SUSPENSE

Majority vote. Tax levy.

SUBJECT: Personal Income Tax Law: deduction from gross income: car loan interest payments

SUMMARY: Allows, under the Personal Income Tax (PIT) Law, a deduction equal to the amount of interest paid by a taxpayer on a "qualified motor vehicle loan", as specified. Specifically, **this bill**:

1) Allows, for taxable years beginning on or after January 1, 2026, and before January 1, 2031, under the PIT Law, a deduction equal to the amount paid by a taxpayer during the taxable year in interest on a "qualified motor vehicle loan".

2) Defines a "qualified motor vehicle loan" as a loan obtained by the taxpayer for a personal use vehicle.

3) Provides that the deduction created by this bill shall be limited to interest payments on one "qualified motor vehicle loan" per taxpayer.

4) Finds and declares the following for the purposes of satisfying the requirements of Revenue and Taxation Code (R&TC) Section 41:

   a) The specific goals, purposes, and objectives of the deduction are to assist Californians in affording the cost of a vehicle; and,

   b) To measure whether this bill achieves its intended purpose, the performance indicators are the number of taxpayers claiming the deduction and the total amount of deductions allowed.

5) Requires the Franchise Tax Board (FTB), by December 1, 2027, and annually thereafter, to prepare a report on the number of taxpayers claiming the deduction and the total amount of deductions allowed.

6) Takes immediate effect as a tax levy.

7) Sunsets these provisions on December 1, 2031.

EXISTING LAW:

1) Conforms to the Internal Revenue Code (IRC), with certain modifications, as of January 1, 2015. (R&TC Section 17201.)

2) Allows an itemized deduction equal to the amount of interest a taxpayer pays on a mortgage secured by their principal or secondary residence, subject to certain limitations. (IRC Section 163(h) and R&TC Section 17201.)

FISCAL EFFECT: The FTB estimates General Fund revenue losses of $600 million in fiscal year (FY) 2025-26, $1.1 billion in FY 2026-27, and $1.2 billion in FY 2027-28.

COMMENTS:

1) The author has provided the following statement in support of this bill:

   In places where public transportation isn't a reliable option, having a car is crucial for getting to work, school, and other important places. AB 490 helps make owning a car a little easier by offering a tax break on car loan interest. This bill will provide financial help for working families who rely on their vehicles to get around, giving them the mobility they need to stay financially stable and build a better future.

2) Brett Hedrick, Dealer Operator of Hedrick's Chevrolet of Clovis, writing in support, notes, in part:

   Our taxpayers are always in need of relief. We sell many vehicles to people who only survive by transportation and it is quickly becoming more difficult for many to afford. Rural and low-income individuals rely on personal vehicles to get to work, school, and other essential destinations. This bill will make it more affordable for individuals to own reliable vehicles for themselves and their families. By offering tax incentives to car buyers, it may also incentivize Californians to purchase newer, safer, and more environmentally friendly vehicles. The environment wins and so does California as a whole.

3) The California Tax Reform Association, writing in opposition to AB 490, notes, in part:

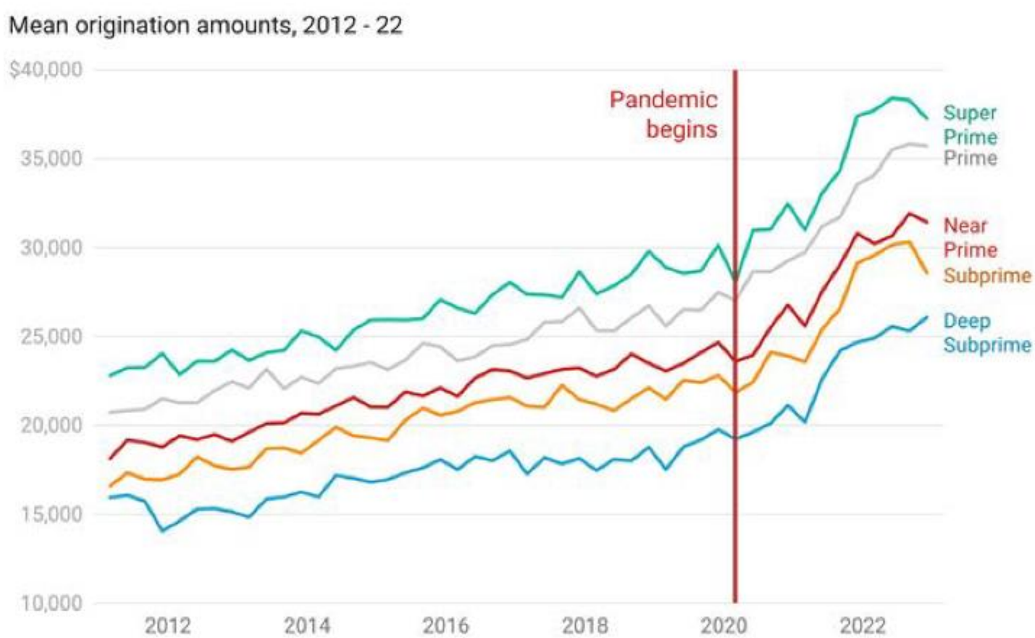
   Consumer interest was deductible many years ago, but that deduction has long been eliminated for good policy reasons, including the inconsistent way some taxpayers were helped while others were not. On that point, this bill would disproportionately help taxpayers in the higher tax brackets while providing no relief to middle-income families who pay little in income tax because of our child credit and standard deductions. Substantial tax benefits should not accrue to upper-income consumers who purchase expensive cars with debt financing and substantial interest costs, nor should the deductibility of consumer interest be reintroduced to the tax system.

4) Committee Staff Comments:

   a) *What would this bill do?* This bill would create an "above-the-line" deduction for the full costs paid in interest on a qualified motor vehicle loan by a taxpayer. A qualified motor vehicle loan is defined as a loan obtained by the taxpayer for a personal use vehicle. Taxpayers are prohibited from claiming the deduction for interest paid on more than one qualified motor vehicle loan. There is no limit to the amount of interest on a qualifying loan that a taxpayer could deduct.

b) *Motor vehicle debt*: According to a report published by the California Policy Lab in April 2023, nearly eight million Californians have auto loans, owing an average of $24,900.[1] The California Policy Lab found that "over the last decade, the number of Californians with auto loans increased by 36% and the average amount owed by Californians on their auto loans surged by a startling 51%." Further, the report found that the average auto debt in Q4 2012 was about $8,500 lower than it is today. The monthly payment on a newly originated auto loan rose 48% over the last decade, from $405 in Q4 2012 to $598 in Q4 2022.[2]

The Federal Reserve Bank of New York's Consumer Credit Panel finds that Americans with the highest credit scores borrow the most. In Q3 2024, borrowers with credit scores of at least 720 took out $97.6 billion in auto loan debt. The remaining credit tiers accounted for $86.7 billion combined.[3] As the figure below demonstrates, the increases in loan amounts have been consistent for consumers across all credit ratings:



Notes: We do not apply an adjustment for joint accounts, so some of these balances are shared among multiple borrowers. We use a generic VantageScore® (version 4.0) provided by the credit bureau. The range is 300-850 (the same as FICO®), with five scoring buckets defined as follows: deep subprime (300-580), subprime (580-619), near-prime (620-659), prime (660-719), and super-prime (720-850).

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[1] Hoover, Ramos, and White, *Startling Increase in California Auto Loans*, California Policy Lab (April 2023). https://www.capolicylab.org/wp-content/uploads/2023/09/Startling-Increase-in-California-Auto-Loans.pdf.
[2] *Ibid.*
[3] Davis, *Average Car Payment and Auto Loan Statistics: 2025*, LendingTree (December 17, 2024). https://www.lendingtree.com/auto/debt-statistics/.

c) *Who is likely to benefit?* As an "above-the-line" deduction, this tax benefit would be available to all taxpayers who are paying interest on qualifying motor vehicle loans, including those who take the standard deduction and do not itemize. In effect, this deduction would operate in a similar fashion to existing "above-the-line" deductions, such as contributions to certain retirement accounts or interest paid on qualifying student loans. This deduction would not be available for owners of cars and trucks that have already been paid off and are not subject to a loan; it would also not benefit those leasing a vehicle.

The value of the deduction increases as the amount paid in interest increases. Loans with high interest rates and longer payment terms typically result in borrowers paying more in interest so the deduction would provide a greater benefit to taxpayers with those types of loans. By partially subsidizing the act of borrowing to purchase a motor vehicle, this bill would likely also benefit car dealerships and companies that finance motor vehicles.

d) *Deductions tend to benefit higher income households*: A deduction is generally more valuable to high-income taxpayers because the "value" of a deduction varies with the marginal tax rate (or tax bracket) of the taxpayer. For example, an individual taxpayer in a 10% tax bracket would receive a tax benefit of $10 on a $100 deduction. In contrast, a taxpayer in a 25% tax bracket would save $25 in taxes for every $100 deducted from income. Thus, assuming the same level of deductions, high-income taxpayers, presumably with a greater ability to pay taxes, would receive a greater tax benefit from the proposed deduction than lower income taxpayers.

e) *Tax Reform Act of 1986*: President Ronald Reagan signed the Tax Reform Act of 1986 into law, stating that the bill was "the most sweeping overhaul of the tax code in our nation's history." Among many other significant modifications to the tax code, one major change enacted by this landmark legislation was the elimination of all deductions for interest paid on car loans, charge-account purchases, credit card balances, vacations, and anything else that fell under what the law termed "consumer loans." The sole exception was interest payments on home loans, also known as the home mortgage interest deduction. At the time, according to the Joint Committee on Taxation's analysis, Congress believed deductions for personal interest encouraged people to consume and were a significant disincentive to saving.[4] Thus, deductibility of consumer interest, except for home mortgages, was phased-out over a five-year period.

f) *What is a "tax expenditure"*? Existing law provides various credits, deductions, exclusions, and exemptions for particular taxpayer groups. In the late 1960s, U.S. Treasury officials began arguing that these features of the tax law should be referred to as "expenditures" since they are generally enacted to accomplish some governmental purpose and there is a determinable cost associated with each (in the form of foregone revenues).

As the Department of Finance notes in its annual Tax Expenditure Report, there are several key differences between tax expenditures and direct expenditures. First, tax

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[4] *General Explanation of the Tax Reform Act of 1986 (H.R.3838, 99th Congress; Public Law 99-514)*, Joint Committee on Taxation (May 4, 1987). https://www.jct.gov/getattachment/d3acafe0-6405-43d1-afcf-20fa0a3052a3/jcs-10-87-3367.pdf.

expenditures are typically reviewed less frequently than direct expenditures. Second, there is generally no control over the amount of revenue losses associated with any given tax expenditure. Finally, it should also be noted that, once enacted, it takes a two-thirds vote to rescind an existing tax expenditure absent a sunset date. This effectively results in a "one-way ratchet" whereby tax expenditures can be conferred by majority vote, but cannot be rescinded, irrespective of their efficacy or cost, without a supermajority vote.

g) *Committee's tax expenditure policy*: Both R&TC Section 41 and Committee policy require any tax expenditure bill to outline specific goals, purposes, and objectives that the tax expenditure will achieve, along with detailed performance indicators for the Legislature to use when measuring whether the tax expenditure meets those stated goals, purposes, and objectives. A tax expenditure bill will not be eligible for a Committee vote unless it has complied with these requirements.

In its current form, this bill states that the deduction is intended to assist Californians in affording the cost of a vehicle. In addition, this bill provides that the expenditure's effectiveness shall be measured by the number of taxpayers claiming the deduction pursuant to this bill and the total amount of deductions allowed. This bill requires the FTB to submit a report to the Legislature by December 1, 2027, and annually thereafter, estimating the number of taxpayers claiming the deduction and the total amount of deductions allowed.

In addition to the R&TC Section 41 requirements, this Committee's policy also requires that all tax expenditure proposals contain an appropriate sunset provision to be eligible for a vote. According to this policy, an "appropriate sunset provision" means five years, except in the case of a tax expenditure measure providing relief to California veterans, in which case "appropriate sunset provision" means ten years. This bill contains a five-year sunset provision and therefore complies with the Committee's policy on sunset dates.

h) *Appropriately targeted*? As described above, deductions disproportionately benefit higher income taxpayers. As currently drafted, this bill does not limit the total amount of interest that could be deducted. This bill also does not limit the deduction based on a taxpayer's income, meaning even very high-income filers that can afford their motor vehicle loan costs could claim the deduction. Additionally, the definition of "qualified motor vehicle loan" is extremely broad and covers any vehicle used for personal use. This could include vehicles used purely for recreational purposes, such as sports cars, motorhomes, off-road utility vehicles, and even dirt bikes.

The Committee may wish to consider whether a deduction is appropriately targeted to achieve the stated goal of relieving financial burdens for those who are struggling to pay for a motor vehicle and whether the current definition of "qualified motor vehicle loan" is overly broad. Alternatively, the Committee may wish to consider whether the deduction amount should be capped, effectively reducing the benefit to borrowers with larger loan balances.

i) *Implementation Considerations*:

i) *What about joint filers*? As currently drafted, this bill limits the deduction to interest payments on one qualified motor vehicle loan per taxpayer. While this restriction is straightforward for single-filers, it may not be as clear for the many taxpayers who file joint returns. Does a married couple filing a joint return qualify for the deduction if they have two motor vehicle loans? The author may wish to clarify the intent of this restriction with language that addresses joint filers.

ii) *Lack of federal conformity*: This bill proposes a deduction that has no counterpart in the Federal tax code. In general, state conformity with federal law promotes greater simplicity and eases administration of complex tax laws. This bill would bring California further out of conformity with federal law as the deduction created by this bill could not be claimed on a Federal return. In the absence of similar federal treatment, taxpayers may need to keep separate accounting for state and federal tax purposes.

iii) *Reporting timeline*: As currently drafted, this bill requires the FTB to provide a report on the deduction no later than December 1, 2027. If the author's intent is to be able to review a report that contains complete information for the 2026 taxable year, it is recommended that the report due date be extended later in the year to July 1, 2028 (or due annually starting in 2028 and each year thereafter). For instance, the due date for the 2026 personal income tax return is April 15, 2027, and with extension individuals may file as late as October 15, 2027. The FTB needs approximately six months to complete return processing and to finalize and submit the report.

j) *Keyed non-fiscal*: It appears that this bill was erroneously keyed as non-fiscal by Legislative Counsel. Based on the revenue impacts described above, this bill could have a significant fiscal impact and would need to be referred to the Appropriations Committee should this bill pass this Committee.

REGISTERED SUPPORT / OPPOSITION:

Support

Hedrick's Chevrolet of Clovis

Opposition

California Tax Reform Association
CFT- a Union of Educators & Classified Professionals, AFT, AFL-CIO

Analysis Prepared by: Wesley Whitaker / REV. & TAX. / (916) 319-2098