EMA Regulatory Alert: Treasury and IRS Propose Section 45Z Tax Credit Rules

The U.S. Department of the Treasury and the Internal Revenue Service have issued proposed regulations providing guidance to domestic producers of clean transportation fuel on eligibility for, and calculation of, the section 45Z Clean Fuel Production Credit, as amended by the One, Big, Beautiful Bill (OBBB). The section 45Z credit provides an income tax credit for qualifying clean transportation fuel produced in the United States and sold through December 31, 2029.

The proposed rules clarify key definitions, emissions rate determinations, and certification and registration requirements applicable to fuels produced after December 31, 2024. In addition to clarifying core elements of the credit, the proposed regulations implement various changes enacted under OBBB, including extending the credit period through 2029, limiting eligible feedstocks to those produced in the United States, Mexico, or Canada, adding prohibited foreign entity restrictions, revising sale attribution rules, and eliminating the special rate for sustainable aviation fuel.

Importantly for energy marketers, the proposal broadens qualifying sales by recognizing important pass-through barriers in the former guidance. Treasury's proposed regulations now clarify that the clean fuel production credit is not limited to direct sales to end users, a point of particular importance in fuel markets that operate through layered distribution chains. While a more extensive analysis is being conducted for EMA to participate in public proceedings on behalf of energy marketers, the following are key highlights:

45Z is Still a Production Credit
The new tax regime shifted the incentives from blending to production. As a result, the Biodiesel Tax Credit, which accrued to fuel blenders, expired on December 31, 2024. Pursuant to the OBBB, the regime provides a credit of up to $1.00 per gallon for the production of both over-the-road biofuels and sustainable aviation fuel (SAF). Previously, the credit allowed SAF to receive up to $1.75, which diverted feedstock incentives to that sector at the expense of transportation fuels. Now, there is a level-playing field, which EMA called for.

The new proposal also makes clear that blending cannot accrue any credits. Production means "all steps and processes used to make a transportation fuel," starting with "the processing of primary feedstock(s)" and ending "with a transportation fuel ready to be sold in a qualified sale." Importantly, production requires a chemical transformation. Minimal processing does not accrue any credit. The preamble of the rule clearly states:

"The blending of a transportation fuel into another fuel to create a fuel mixture, regardless of whether the fuel mixture itself satisfies the requirements of section 45Z(d)(5)(A), would not constitute production of a transportation fuel because the blending process would constitute minimal processing. For example, the blending of ethanol and gasoline would not constitute production of a transportation fuel." This is consistent with the structure of the 45Z regime, which intentionally shifts incentives upstream.

Finally, the proposal includes rules that intend to prioritize and boost domestic markets. The proposed regulations exclude foreign feedstocks for purposes of claiming credits, as well as imported fuel that undergoes only minimal processing in the country.

Credit Eligibility
Under the credit regime, a taxpayer is eligible to claim a section 45Z credit for the taxable year in which the taxpayer produces and sells a transportation fuel. Notably, the proposed rules define "transportation fuel" as a fuel that meets four criteria:

1. Is suitable for use as a fuel in a highway vehicle or aircraft;
2. Has a lifecycle emissions rate not greater than 50 kg CO_2e/mmBTU;
3. Is not derived from prohibited coprocessing pathways; and
4. Is not produced from another fuel already eligible for a section 45Z credit.

In turn, the phrase "suitable for use" is defined as having practical and commercial fitness for use as a fuel in a highway vehicle or aircraft, or being blendable into a fuel mixture that has such fitness. Actual use as a transportation fuel is not required, meaning a fuel may qualify even if transportation is not its predominant use and it ultimately is used for non-transportation purposes. This definition is particularly relevant to heating oil marketers.

Importantly, the proposal expressly ties this concept to longstanding federal excise tax principles, under which a fuel's classification turns on its physical and commercial capability, not declared end use. As a result, fuels that are chemically and commercially interchangeable with diesel fuel are not excluded from the definition of "transportation fuel" solely because they are sold or used for heating or other non-highway purposes.

The final regulation will contain examples to further clarify eligibility based on suitable use. EMA will comment on this aspect of the proposal to maximize chances of credit generation with pass-through potential for home heating oil.

Another important aspect of the definition of transportation fuels is the carbon intensity thresholds outlined by the credit regime. Even if a fuel meets the "suitable for use" criterion, the proposal imposes a strict emissions screen: lifecycle emissions must not exceed 50 kg of CO2e per mmBTU. In the context of heating oil, even if eligible for credit based on its suitability, credit generation would be limited to the biodiesel and renewable diesel part of the blend. In practice, given the production-level incentive, it may be difficult for heating oil marketers to accrue downstream benefits. There is considerable uncertainty regarding whether any credit could be passed through to heating oil marketers.

Qualifying Sales
The proposed regulation has sought to correct major pass-through barriers present in the former guidance by broadening the scope of what constitutes a qualifying sale. Namely, the proposal makes changes to allow the sale of transportation fuel to an intermediary or reseller. In the preamble, Treasury acknowledges stakeholder concerns, including EMA, that earlier draft

language could have been read to exclude sales to wholesalers, dealers, or other intermediaries that purchase fuel for resale rather than for their own immediate consumption.

While energy marketers themselves do not generate the production credit, since they are not producing the fuel, these rules confirm that the normal downstream resale chain does not disqualify the producer's credit, helping preserve the potential for any upstream pass-through benefit. The proposed regulation contains this helpful example:

Example 5. Qualified sale by taxpayer that produces and subsequently blends a fuel. X produces 9,000 gallons of renewable diesel that qualifies as a transportation fuel. After production, X blends the 9,000 gallons of renewable diesel with 1,000 gallons of petroleum-based diesel fuel that does not qualify as a transportation fuel. X sells the resulting 10,000-gallon fuel blend to an unrelated person for use in that person's trade or business. X has made a qualified sale of the 9,000 gallons of renewable diesel, as part of the fuel blend, under paragraphs (b)(29)(i)(B) and (b)(29)(ii) of this section.

EMA Regulatory Counsel continues to review the guidance to provide further analysis to the membership and participate in the upcoming public proceedings, including comments and a public hearing.