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Tax Update

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IRS and Treasury Issue Proposed Regulations on Clean Fuel Production Credit

Section 45Z, which was added to the Code by the Inflation Reduction Act of 2022 and amended by the One Big Beautiful Bill Act, provides a tax credit for eligible fuels that are produced after December 31, 2024 and sold before January 1, 2030.

On February 3, 2026, the Internal Revenue Service (the IRS) and the Department of the Treasury (the Treasury) issued proposed regulations (the Proposed Regulations) regarding clean fuel production tax credits under section 45Z (the 45Z Credit).^[1] Section 45Z, which was added to the Code by the Inflation Reduction Act of 2022 and amended by the One Big Beautiful Bill Act (the OBBBA), provides a tax credit for eligible fuels that are produced after December 31, 2024 and sold before January 1, 2030.^[2] The text of the Proposed Regulations can be found [here](#). Our prior alert on the changes enacted by the OBBBA to clean energy tax provisions can be found [here](#).

The Proposed Regulations^[3] are lengthy and complex and address a myriad of issues. Below, we highlight five significant issues and developments.

1. **Qualified Sale: No Need to Cut out the Middleman**

- *Appropriate scope of “qualified sale.”* To claim 45Z Credits, a taxpayer must make a “qualified sale” of an eligible transportation fuel to an unrelated person for use in a trade or business or for production of a fuel mixture or a retail fuel sale. In January 2025, the IRS released a notice of forthcoming proposed regulations (the January 2025 Notice) that would have provided that a sale would meet the requirement for use in a trade or

business only if the sale were to a purchaser who was going to use the fuel “as a fuel.” In a welcome development, the Proposed Regulations confirm that a qualified sale includes a sale of transportation fuel to a reseller, such as an intermediary wholesaler and distributor, eliminating concern among taxpayers about the narrower (and deeply questionable) interpretation in the January 2025 Notice.

- *Expanded look-through rule.* The Proposed Regulations also provide a broad look-through rule for sales made through related intermediaries, allowing a taxpayer to be treated as engaging in a qualified sale of fuel to an unrelated person if that related intermediary (such as a dealer) ultimately sells the fuel to an unrelated person. This rule expands on the IRS’s January 2025 look-through rule, which had applied only to corporations that were members of the same consolidated group.
2. **Watch Out for Stacking Pitfalls.** 45Z Credits cannot be stacked with certain other credits, including section 45V credits (clean hydrogen production), section 48 credits claimed in lieu of 45V credits, and section 45Q credits (carbon capture, sequestration and utilization). The Proposed Regulations provide various clarifications and examples that illustrate the application of anti-stacking rules that provide more certainty to taxpayers. For example, if a credit under section 45Q is claimed in respect of a facility in year 1 but not in year 2, a 45Z Credit could not be claimed in year 1 but could be claimed in year 2.
 3. **Watch Your Feedstock**
 - *No doubling up of 45Z Credits allowed.* As amended by the OBBBA, 45Z Credits are not allowed for fuel that is produced from another fuel for which a 45Z Credit is allowable. Before the OBBBA amendment, the IRS, in January 2025, had asserted that a fuel was ineligible for a 45Z Credit if it had a primary feedstock that itself also qualified as a 45Z Credit-eligible transportation fuel. The preamble to the Proposed Regulations clarify that a fuel still can qualify for the 45Z Credit even if its production process uses a 45Z Credit-eligible transportation fuel solely as a process fuel or as another non-primary-feedstock input, but not as a primary feedstock.
 - *Enhanced 45Z Credit may be available for animal manure feedstock.* Fuels derived from animal manure feedstock (including dairy, swine, and poultry manure) potentially are eligible for an enhanced 45Z Credit amount. Section 45Z authorizes Treasury to identify “any other sources” of animal manure feedstock (other than dairy, swine, or poultry manure) that are eligible for this enhanced rate, but the Proposed Regulations do not do so.
 4. **Suitable for Use Does Not Require Actual Use.** 45Z Credits are available only if a fuel is “suitable for use” as fuel in a highway vehicle or aircraft, but section 45Z does not define “suitable for use,” and the Proposed Regulations confirm helpful guidance from the January 2025 Notice making clear that fuel is “suitable for use” if it has practical and commercial fitness for use in a highway vehicle or aircraft (or may be blended into a fuel mixture that has practical and commercial fitness for use as fuel in a highway vehicle or aircraft) and that actual use as a fuel in a highway vehicle or aircraft is not required. Thus, for example, a diesel fuel that meets all other section 45Z requirements would be considered suitable for use in a highway vehicle or aircraft even if it is sold to a customer that uses that fuel as marine diesel fuel.

5. **Being a Producer (of Alternative Natural Gas) is Good.** The Proposed Regulations make clear that the person potentially eligible for 45Z Credits in connection with the production of alternative natural gas (including renewable natural gas) is the person that processes untreated sources of alternative natural gas to remove water, carbon dioxide, and other impurities. The Proposed Regulations thus make clear that a producer of renewable natural gas that delivers that gas to a pipeline (and otherwise satisfies the section 45Z requirements) is eligible for 45Z Credits even if another person subsequently removes the alternative natural gas from a pipeline, compresses it further, and then sells that further compressed alternative natural gas.

[1] Unless indicated otherwise, all “section” references are to the Internal Revenue Code of 1986, as amended (the Code).

[2] The legal name for the Inflation Reduction Act of 2022 is “An Act to provide for reconciliation pursuant to title II of S. Con. Res. 14,” and the legal name for the OBBBA is “an Act to provide for reconciliation pursuant to title II of H. Con. Res. 14.”

[3] The preamble to the Proposed Regulations provides that taxpayers may rely on the Proposed Regulations until final regulations are published in the Federal Register, provided that taxpayers follow the Proposed Regulations in their entirety and in a consistent manner. 91 Fed. Reg. 5160, 5181 (Explanation of Provisions, IX).

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Gibson Dunn lawyers are available to assist in addressing any questions you may have regarding this proposed legislation. To learn more about these issues or discuss how they might impact your business, please contact the Gibson Dunn lawyer with whom you usually work, the authors, or any member of the firm’s Tax and Tax Controversy and Litigation practice groups:

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