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December 3, 2022

Janet Yellen, Secretary of the Treasury
U.S. Department of the Treasury
1500 Pennsylvania Avenue NW
Washington, DC 20220

Charles Rettig, Commissioner
Internal Revenue Service
1111 Constitution Ave. NW
Washington, DC 20224

**RE: Notice 2022-58, "Request for Comments on Credits for Clean Hydrogen and Clean Fuel Production" (IRS-2022-0029-0001)**

*Submitted via www.regulations.gov*

Dear Secretary Yellen and Commissioner Rettig:

Thank you for the opportunity to comment on amendments to the Internal Revenue Code (IRC) included in the recently enacted Inflation Reduction Act of 2022 (IRA). This letter is being submitted in response to Notice 2022-58, which covers provisions of the IRA relating to tax incentives for clean hydrogen and clean fuel production.[1] Note that our comments will focus exclusively the new Section 45Z clean fuel production credit (the §45Z credit).

## I. About us

The National Energy & Fuels Institute (NEFI) has represented the liquid heating fuels industry and related services companies since 1942.[2] Our industry delivers a safe, dependable, and efficient heating fuel to six million homes and businesses across the country. Of the five billion gallons of heating oil used on average in the United States each winter, 85-percent is utilized by homes and businesses in the Northeast from Maryland to Maine.[3] Many of our retail members, often referred to as "heating fuel dealers," provide both fuel delivery and heating, cooling, ventilation, and air conditioning (HVAC) services. These "full service" companies commonly sell, install, and service residential and commercial HVAC systems, including liquid fuel (i.e., oil- and biofuel-fired) furnaces, boilers, and water heaters.

## II. Transition to Renewable Liquid Heating Fuels

NEFI members are actively working to replace conventional home heating oil with renewable fuels to reduce greenhouse gas (GHG) emissions, support local economies, and contribute to American energy and environmental security. Many now blend biodiesel into their fuel. Biodiesel is produced from an array of sustainable feedstocks, including recycled cooking oils and fats and surplus vegetable oils, and delivers 74% lower GHG emissions on average than conventional petroleum. [4] Renewable diesel is also suitable for use in space heating applications, and next-generation cellulosic heating fuels are currently in development. Biodiesel, renewable diesel, and other advanced biofuels provide our mostly small family businesses with the opportunity to help achieve local, state, and federal climate goals while enhancing their competitiveness and preserving a future for themselves in the new energy economy.

Several Northeast states now require by law or regulation the use of high blends of biofuel, including biodiesel and renewable diesel, in home heating oil:

| State | 5% Blend (B5) | 10% Blend (B10) | 15% Blend (B15) | 20% Blend (B20) | 50% Blend (B50) | Reference |
|---|---|---|---|---|---|---|
| **Connecticut** | July 1, 2022 | July 1, 2025 | July 1, 2030 | July 1, 2034 | July 1, 2035 | 296 CGS §16a-21b |
| **New York** | July 1, 2022 | July 1, 2025 | - | July 1, 2030 | - | NYCL ENV §19-0327 |
| **Rhode Island** | July 1, 2017 | July 1, 2023 | - | July 1, 2025 | July 1, 2030 | 23 RIGL §23-23.7 |

Other states have laws on the books to incentivize the use of biofuels in home heating oil. Massachusetts is working to strengthen its current incentive program that rewards heating oil distributors for delivering blends of at least 10% biodiesel.[5] In addition to its statewide blending requirement, New York offers heating oil customers a tax credit of up to $0.01 per percent of biodiesel blended into each gallon of heating oil purchased annually through 2025, provided the blend is greater than five-percent.[6] Several Northeast states are also considering some form of "clean heat standard" that may offer credits for the sale or use of renewable liquid heating fuels.[7]

Renewable liquid heating fuels offer Northeast states an immediate "plug and play" solution to reducing greenhouse gas emissions in residential and commercial buildings. These fuels utilize existing and well-regulated storage and distribution infrastructure and, with minor and very low-cost modifications, work seamlessly in existing appliances to deliver immediate reductions in greenhouse gas emissions – all at little to no additional cost to the consumer.[8] In other words, heating oil customers can help fight climate change without costly conversions of their entire home heating systems to other fuels or energy sources.[9]

## III. Comments on the 45Z Credit

Federal tax incentives to promote the production, importation, blending, sale, and use of renewable fuels are vital to the heating oil industry's transition to a low carbon future. The current tax credit for biodiesel and renewable diesel blends under IRC §40A has facilitated extraordinary growth in biofuel adoption and infrastructure investment in this sector. Like all other renewable fuel tax incentives, the IRA terminates the §40A biodiesel and renewable diesel blenders' tax credit on January 1, 2025; and replaces them with the new §45Z clean fuels production tax credit. Our comments on this new credit are below.

### *a. Space and water heating as eligible applications*

Heating oil and diesel fuel are the same product and there is no compelling policy justification for giving them disparate tax treatment. Throughout the notice, the IRS and Treasury explicitly refer to "transportation fuel" as qualifying fuels under the §45Z credit. The statute defines "transportation fuel" as a fuel which is "suitable for use as a fuel in a highway vehicle or aircraft."[10] However, that does not mean it must exclusively be used as a fuel in a highway vehicle or aircraft to receive the credit. The agency specifically requests input on factors for which unrelated persons may purchase qualified fuel in relation to a "trade or business."[11] It is the intent of Congress that the agencies include the mixture or sale of clean fuels for use in residential and commercial space and water heating applications in the definition of "qualified mixtures" and "trade or business activities" under § 45Z(a)(4). Consider the below statement, found in the Senate Finance Committee's summary of the legislation:

> Fuels must be at least transportation grade – suitable for use in a highway vehicle or aircraft – but may be used for any business purpose, including as transportation fuel, industrial fuel, *or for residential or commercial heat* [emphases added].[12]

This fact is reiterated in a colloquy between Senator Maggie Hasson of New Hampshire and Senate Finance Committee Chair Ron Wyden of Oregon during floor consideration of the IRA on August 6, 2022:

> Ms. HASSAN. Mr. President, I ask unanimous consent to engage in a colloquy with Senator WYDEN for clarification regarding a tax provision included in the bill currently before the Senate. Section 13704 of the bill, which concerns production credits for biofuels, defines "transportation fuel" that can qualify for the credit as a fuel that is suitable for use as a fuel in a highway vehicle or aircraft. The fuel must also be below a carbon emissions ceiling and meet a processing requirement.
>
> Senator WYDEN, as chair of the Finance Committee, is it his understanding that, although a fuel must be suitable for use as a fuel in a highway vehicle or aircraft to qualify for this biofuel production credit, *it may still actually be used for any business purpose, including as transportation fuel, industrial fuel, or for residential or commercial heat*?
>
> Mr. WYDEN. I thank the Senator for her inquiry. *That is correct.* The credit is intended to incentivize production of biofuels of a certain quality, usable as fuel for highway vehicles or aircrafts, but not limited only to fuels which are actually used in highway vehicles or aircrafts [emphasis added].[13]

***b. Movement to a domestic production credit will disrupt the heating oil market***

NEFI members and other distributors and consumers of liquid fuels have serious concerns with the planned transition to and implementation of the §45Z credit as an incentive exclusively for the domestic production of qualified fuels. Elimination of the blender credit and transition to a new tax credit exclusively for the domestic production of renewable fuels will have significant consequences for the heating oil market, especially in the Northeast. This extraordinary action will undercut millions of dollars' worth of investments in renewable fuel blending technology and distribution infrastructure and may discourage future investments.

Renewable fuels are not currently produced in sufficient quantities to meet growing demand in the Northeast, due in large part to limited conventional feedstock availability. This has required that a substantial portion of fuel be imported into the region. The current biodiesel and renewable diesel blenders' credit under IRC §40A incentivizes fuel suppliers to purchase and blend affordable gallons of biofuel from elsewhere in the U.S. or to import such fuels from Canada or other overseas trade partners. Some are compelled by law to purchase these fuels because, as previously mentioned, several states now require the use of renewable liquid heating fuels. The prohibition on these biofuel imports from obtaining the §45Z credit will place these fuels at a disadvantage in the U.S. market and result in them shipped to other countries.

Suppliers will be forced to search for qualified biofuels in other parts of the United States, which will incur higher costs due to logistics and competition with fuel distributors in other parts of the country. In states where blending is discretionary, the inability to obtain affordable supply may discourage heating oil distributors from continuing their transition to higher blends of renewable fuels. This will increase greenhouse gas emissions and jeopardize the ability of governments in the region to achieve their ambitious climate goals.

NEFI asks that the IRS and Treasury consider these concerns and evaluate how these harmful effects can be minimized though the implementation of the §45Z credit. **In the meantime, NEFI and its members will continue to discuss this matter with Congress and explore future clarifications and improvements to the law that will ensure the continued growth and adoption of renewable fuels in the heating oil sector.**

### *c. The §45Z credit should incentivize fuels with net-negative greenhouse gas emissions*

Unlike existing tax incentives, the §45Z credit offers a higher amount based on the "emissions factor" of qualified fuels. No later than January 1, 2025, the new law requires the administration to issue guidance regarding the calculation of emission factors for qualifying fuels.[14] The IRA requires the agencies to utilize the Argonne GREET model when calculating lifecycle greenhouse gas emissions for all qualifying fuels that are not aviation fuels.[15] NEFI will monitor implementation of this provision closely.

We request the agencies consider structuring the tax incentive to reward fuels that have proven net-negative lifecycle greenhouse gas emissions, not cap the value of the incentives for fuels that achieve net-zero. This will help spur growth of important next-generation renewable fuels designed for use in the space heating sector, such as ethyl levulinate (EL). This net-negative carbon heating fuel, currently under development in northern New England, utilizes unconventional and locally sourced feedstocks, such as sustainably harvested wood products, municipal solid waste, and forestry and agricultural residues.[16]

## IV. Conclusion

The §45Z clean fuel production credit marks a dramatic shift in U.S. biofuels policy that will significantly impact heating oil distributors and their customers. Given the importance of federal incentives to the heating oil industry's transition to renewable liquid heating fuels, we request the IRS and Treasury provide opportunities for NEFI and its members to provide additional feedback and relay their concerns throughout the implementation process.

Thank you again for the opportunity to provide general comments on the 45Z credit. We stand ready to answer any additional questions or provide additional information as needed.

Sincerely,

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National Energy & Fuels Institute (NEFI)

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[1] §§13204 and 13704 of Public Law 117-169, 136 Stat. 1818 (August 16, 2022).

[2] NEFI changed its name and became a national association on July 1, 2020.

[3] U.S. Census Bureau, *American Community Survey (ACS),* Fuel Oil Use by Occupied Housing Units, Five-Year Avg. (2013-2017). Percent (%) of homes is calculated as a percentage of total state occupied housing units.

[4] Argonne National Laboratory; U.S. Department of Energy, Alternative Fuels Data Center, https://afdc.energy.gov/vehicles/diesels_emissions.html.

[5] 225 CMR 16.00

[6] New York Consolidated Laws, Tax Law § 210-B.25

[7] Such proposals are under active consideration in Massachusetts, New York, and Vermont.

[8] National Oilheat Research Alliance, *Developing a Renewable Biofuel Option for the Home Heating Oil Sector: A Report to Congress, State Governments and the Environmental Protection Agency,* May 2015, p.18.

[9] A September 2021 Massachusetts-based study by Diversified Energy Specialists estimates the median project cost of $18,400 for a whole-home conversion from an existing oil heat system to a new air source heat pump system.

[10] P.L. 117-109, 136 Stat. at 2000

[11] Notice 2022-58, pp.9-10.

[12] Senate Finance Committee Section-by-Section Summary of the Inflation Reduction Act, August 2022, p. 24.

[13] Statements of Senators Maggie Hassan and Ron Wyden, *Congressional Record*, 168 (2022) p. S4166.

[14] IRC §45Z(e)

[15] IRC §45Z(b)(1)(B)(ii)

[16] A Biofine Developments Northeast Inc and EarthShift Labs 2019 GREET analysis shows EL reduces emissions by over 100% in heating applications.