July 2, 2024

Inflation Reduction Act: Recent Guidance under the SAF Credit and What it Means for Section 45Z

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On April 13, 2024, the Internal Revenue Service (IRS) and U.S. Department of the Treasury (Treasury) released Notice 2024-37, which provides additional guidance and safe harbors with respect to the federal income tax credit (the SAF Credit) for sustainable aviation fuel (SAF) under Sections 40B and 6426(k).[1]

The SAF Credit was introduced by the Inflation Reduction Act of 2022 (the IRA). Notice 2024-37 is the latest guidance in connection with the SAF Credit following Notice 2023-6, which was released on December 19, 2022, and Notice 2024-6, which was released on December 15, 2023.

Notice 2024-37 – well received by the aviation biofuels industry – provides direction to blenders seeking the SAF Credit and, perhaps more importantly, offers a strong indication of what the SAF industry should expect in future guidance under the clean fuel production credit under Section 45Z (the CFP Credit).

Background to the SAF Credit

- The SAF Credit is available for each gallon of SAF included in a kerosene-based mixture that contains SAF as a blending component (a Qualified Mixture) and is sold or used by the taxpayer in 2023 or 2024.
- The SAF Credit is a blender's credit and therefore is available to the taxpayer that includes SAF in a Qualified Mixture rather than the SAF producer. In order to be a Qualified Mixture, a mixture of SAF and kerosene must be:
  - Produced by the taxpayer in the United States;
  - Used by the taxpayer in an aircraft or sold by the taxpayer for use in an aircraft by an end user, provided that the use or sale is in the ordinary course of the taxpayer's business; and
  - Transferred into the fuel tank of an aircraft by the taxpayer or end user in the United States.[2]

[1] Unless otherwise indicated, "Section" references are intended to refer to sections of the Internal Revenue Code of 1986, as amended.

[2] Notably, Section 40B does not require that production of the SAF occur in the United States

- In addition, in order to qualify for the SAF Credit, the SAF:
  - Must meet the requirements of one of two American Society for Testing and Materials (ASTM) qualifications: ASTM D7566, which is the standard specification for SAF that consists of conventional and synthetic blending components or (b) the Fischer Tropsch provisions of ASTM D1655 Annex A1.[3]
  - Cannot be derived from palm fatty acid distillates or petroleum, or from co-processing certain fatty acid compounds with non-biomass feedstocks; and
  - Must be certified as having a lifecycle greenhouse gas emissions reduction percentage (Emissions Reduction Percentage) of at least 50 percent.
- The SAF Credit is calculated as the product of (1) the number of gallons of SAF included in a Qualified Mixture and (2) the sum of $1.25 plus a supplementary amount. The supplementary amount equals $0.01 for each percentage point by which the blended SAF's Emissions Reduction Percentage exceeds the threshold Emissions Reduction Percentage of 50 percent. The maximum supplementary amount therefore is 50 cents, effectively capping the total credit at $1.75 per gallon of SAF.[4]
- The Emissions Reduction Percentage means the percentage reduction in lifecycle greenhouse gas emissions achieved by a SAF, as compared to petroleum-based jet fuel, determined in accordance with (1) the most recent Carbon Offsetting and Reduction Scheme for International Aviation (CORSIA) methodology that has been adopted by the International Civil Aviation Organization with the agreement of the United States or (2) any similar methodology that satisfies the criteria under Section 211(o)(1)(H) of the Clean Air Act as in effect on August 16, 2022 (Similar Methodology), calculated as follows:

$$\frac{\text{(Lifecycle emissions value of petroleum-based jet fuel)}^{5} \text{ minus (Lifecycle emissions value of the SAF)}}{\text{(Lifecycle emissions value of petroleum-based jet fuel)}^{5}}$$

- As an alternative to the SAF Credit, a taxpayer may claim a credit under Section 6426(k) against the excise tax applicable to SAF (Excise Tax Credit). If the Excise Tax Credit is chosen, the taxpayer must claim the credit against its excise tax liability and, thereafter, may claim either a cash payment or a refundable income tax credit.
- In order for a taxpayer to qualify for the SAF Credit or the Excise Tax Credit, the SAF producer or importer must be registered with the IRS under Section 4101 and receive certification from an unrelated party demonstrating compliance with any general requirements, supply chain traceability requirements, and information transmission requirements established under CORSIA or, in the case of SAF using a Similar Methodology to determine the Emissions Reduction Percentage, similar requirements (the Unrelated Party Certification).

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[3] Fischer Tropsch is a gas-to-liquid polymerization process used to convert carbon monoxide and hydrogen into liquid hydrocarbon fuels for to replace petroleum-based fuels.

[4] Unlike other federal income tax credits under the IRA, the SAF Credit is not subject to the prevailing wage and apprenticeship requirements.

[5] Per Notice 2023-6, until further notice, the lifecycle emissions value of petroleum-based jet fuel will be 89 grams of carbon dioxide equivalent per megajoule of energy (gCO2e/MJ).

- The SAF Credit is not eligible for the direct pay election under Section 6417 or the credit transfer election under Section 6418.[6]

Notice 2023-6

- Notice 2023-6 provided general guidance with respect to the SAF Credit, including the calculation of the Emissions Reduction Percentage and CORSIA-based safe harbors for determining the Emissions Reduction Percentage and for providing the corresponding Unrelated Party Certification, and procedures for claiming the SAF Credit.

Notice 2024-6

- Notice 2024-6 provided safe harbors for using the Environmental Protection Agency's Renewable Fuel Standard (RFS) program as a Similar Methodology to calculate the Emissions Reduction Percentage and for using RFS guidance to comply with the Unrelated Party Certification requirements.

- Notice 2024-6 clarified that the existing R&D GREET 4 model (referred to in Notice 2024-6 as the ANL GREET Model) and any other currently-available version of Argonne National Laboratory's Greenhouse gases, regulated Emissions, and Energy use in Technologies Model (referred to as the GREET Model) could not be used to calculate the Emissions Reduction Percentage.

- Finally, Notice 2024-6 announced that the Department of Energy is collaborating with other federal agencies to develop a SAF-specific version of the GREET Model that, when complete, would constitute a Similar Methodology for purposes of calculating the Emissions Reduction Percentage.

Highlights of Notice 2024-37

- The 40BSAF-GREET 2024 Model Constitutes a Similar Methodology.
  - Notice 2024-37 provides that the 40BSAF-GREET 2024 model (40BSAF-GREET 2024 Model), which was previewed in Notice 2024-6 and released in April, is a Similar Methodology for purposes of determining the Emissions Reduction Percentage.
  - The 40BSAF-GREET 2024 Model, like the CORSIA methodology, evaluates the full fuel lifecycle of a SAF, including all stages of fuel and feedstock production through to the end use of the finished fuel. The 40BSAF-GREET 2024 Model calculates the lifecycle greenhouse gas emissions of SAF from two production routes – hydroprocessed esters and fatty acids (HEFA) and alcohol-to-jet using an ethanol feedstock (ATJ-Ethanol) – each of which is approved by the ASTM.

- 40BSAF-GREET 2024 Model Safe Harbor.
  - Notice 2024-37 provides a safe harbor with respect to the 40BSAF-GREET 2024 Model.
  - The IRS will accept an Emissions Reduction Percentage for a SAF blending component in a Qualified Mixture that is calculated in accordance with the 40BSAF-GREET 2024 Model, provided (1) the Qualified Mixture satisfies the requirements of ASTM D7566 and (2) the Unrelated Party Certification requirements are met.

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[6] We discussed the direct pay election and the credit transfer election in recent client alerts.

- California LCFS Verifier Safe Harbor.
  - Notice 2024-37 provides a second safe harbor for the use of the California Resource Board's (CARB) Low Carbon Fuel Standard (LCFS) model for purposes of the Unrelated Party Certification requirements.
  - The IRS will consider a registered SAF producer or importer as having met Unrelated Party Certification requirements for a SAF blending component if the producer obtains the requisite certification from a CARB LCFS verifier and the certification is provided in a format that is substantially similar to an LCFS verification, provided the Qualified Mixture for which the SAF blending component is used (1) satisfies the requirements of ASTM D7566, (2) uses the 40BSAFGREET 2024 Model to determine the Emissions Reduction Percentage, and (3) satisfies certain additional verification and certification requirements.
- Climate Smart Agriculture Safe Harbor.
  - Notice 2024-37 provides a third safe harbor for taxpayers seeking to claim an additional reduction in Emissions Reduction Percentage in connection with climate smart agriculture (CSA) practices, which have not yet been incorporated into currently-available lifecycle greenhouse gas emissions models.
  - The USDA has developed a pilot program (the CSA Pilot Program) establishing CSA practices for cultivating domestic corn and domestic soybeans for use as SAF feedstocks.[7] In lieu of requiring that CSA-derived carbon reductions be incorporated into lifecycle greenhouse gas emission models, the IRS will accept a proxy reduction for purposes of calculating the Emissions Reduction Percentage for a SAF blending component produced from CSA corn or CSA soybean, provided that (1) the lifecycle emissions value of the SAF is calculated using the 40BSAF-GREET 2024 model, (2) the requirements of the CSA Pilot Program are met, and (3) certain additional certification and other requirements are satisfied.
  - The proxy reduction for CSA corn and for CSA soybean is an additional 10 gCO2e/MJ reduction and 5 gCO2e/MJ reduction, respectively, in the lifecycle emissions value of the SAF blending component, which would be factored into the fraction shown above and therefore reduce the Emissions Reduction Percentage of the component.

Key Takeaways

Notice 2024-37 provides critical guidance under the SAF Credit. Most notably, Notice 2024-37 offers a SAF-specific version of the GREET model, which is the preferred methodology of the aviation biofuels industry, as a Similar Methodology and therefore an alternative to CORSIA. In addition, for the first time, the IRS and Treasury have provided a clear tax incentive for climate smart farming technology.

Nonetheless, the SAF Credit has a limited runway. The credit is available only for 2023 and 2024 and limited amounts of SAF have been produced in these years. By contrast, the CFP Credit, available during calendar years 2025, 2026, and 2027, is generally understood to be a more valuable credit opportunity for the aviation biofuels industry. In most cases, the CFP Credit will be a larger per-gallon credit. The base credit for SAF under the CFP Credit – $1.75 per gallon of SAF produced by the taxpayer[8] – equals the

[7] For corn ethanol-to-jet, the CSA Pilot Program provides the proxy reduction if certain CSA practices (no-till, cover crop, and enhanced efficiency fertilizer) are used on the same acreage. For soybean-to-jet, only two of these CSA practices (no-till and cover crop) are required to be used on the same acreage. Notice 2024-37 includes a description of the CSA Pilot Program as Appendix A.

[8] This per-gallon rate is available only if the prevailing wage and apprenticeship requirements are satisfied

maximum amount under the SAF Credit and, on account of a per-gallon multiplier based on the SAF's emissions factor, is likely to climb much higher. In addition, unlike the SAF Credit, the CFP Credit is eligible for the direct pay and credit transfer elections and therefore is expected to be a significantly more liquid credit. Finally, the years 2025, 2026, and 2027 are likely to coincide with greater levels of SAF production based on current industry projections.

From this perspective, the most critical feature of Notice 2024-37 is insight into the way the IRS and Treasury could implement the CFP Credit. Absent an unexpected turn of events, future guidance under the CFP Credit should resemble the form and substance of Notice 2024-27. Future guidance is likely to utilize a version of the GREET model (as confirmed by the press release accompanying the Notice). Similarly, the aviation biofuels industry is optimistic that CFP Credit guidance will provide similar safe harbors for the CSA Pilot Program and CARB LCFS verification.

Per the IRA, taxpayers should expect comprehensive guidance for the CFP Credit by the end of 2024.

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If you have questions concerning the contents of this alert, or would like more information about Weil's Tax practice, please speak to your regular contact at Weil, or to:

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