November 20, 2007 Energy Practice

## IRS Narrows Definition of "Liquid Hydrocarbons Derived from Biomass"

Notice 2007-97, released by the IRS on November 13, 2007, originally as Notice 2007-92, made a narrow retroactive change (back to October 1, 2006) to the definition of "liquid hydrocarbons derived from biomass" for purposes of the alternative fuel credit and alternative fuel mixture credit, to clarify the definition to exclude oil, natural gas, coal, or any product derived from these three products.

The Notice makes changes to the section 6426(d) and (e) credits but not the section 45 production credits. Under the Internal Revenue Code (Code) section 6426(d), taxpayers who produce or use qualifying alternative fuels are eligible for a 50 cent per gallon credit, beginning October 1, 2006. Under section 6426(e), taxpayers who produce alternative fuel mixtures are eligible for an equivalent credit according to the amount of alternative fuel that the taxpayer sells for use as fuel or actually uses as fuel in creating such mixtures. The Code includes liquid hydrocarbons derived from biomass as one type of qualifying alternative fuel. Others include liquefied petroleum gas, P-series fuels, compressed or liquefied natural gas, liquefied hydrogen, and any liquid derived from coal through the Fischer-Tropsch process.

The Notice defines liquid hydrocarbons derived from biomass as "chemical compounds that are liquid when eligibility for the credit or payment is determined and are derived from any organic material, including oceanic and terrestrial crops and crop residues, and organic waste products that have a market value." Eligibility for the alternative fuel credit or payment is determined at the time when a tax would otherwise be imposed by various Code sections. Eligibility for the alternative fuel mixture credit or payment is determined when the fuel mixture is produced. The Notice reflects existing Code provisions by expressly excluding ethanol, methanol, and biodiesel from the definition of liquid hydrocarbons derived from biomass, but goes further to also exclude oil, natural gas, coal, or any product of the latter three from the definition, though certain forms of natural gas and coal fall within the general definition of an alternative fuel.

In addition, the IRS noted that the Senate Finance Committee had recently approved technical corrections clarifying that any liquid fuel derived from biomass qualified as an alternative fuel but that any fuel qualifying for an alcohol, biodiesel, or renewable diesel credit would not qualify for the alternative fuel credit. If enacted, the technical corrections would be retroactive to October 1, 2006, meaning that any taxpayer who had been allowed an alternative fuel credit or payment for any alcohol fuel would be required to repay such amount with interest.

For more information on the IRS's Notice or Mayer Brown's Energy Practice, please contact Arthur Walker (awalker@mayerbrown.com), Tom Geraghty (tgeraghty@mayerbrown.com), Marc Folladori (mfolladori@mayerbrown.com), Kevin Shaw (kshaw@mayerbrown.com), or any other Mayer Brown attorney with whom you work.

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