



December 12, 2025

The Honorable Kenneth J. Kies  
Department of the Treasury  
1500 Pennsylvania Ave., NW, Room 3120  
Washington, DC 20220

Dear Assistant Secretary Kies:

I am writing on behalf of the American Public Power Association (“APPA”) regarding changes to the private activity bond regulations applicable to output facilities promulgated under Treasury Regulation Section 1.141-7 (the “Output Regulations”) and other regulatory matters of importance to public power utilities. There have been no updates or modifications to the Output Regulations since they were published in 2002. Given both the passage of time and significant changes in the electric industry since the release of the Output Regulations, we are sharing our recommendations for modification and changes. Among other changes, large load customers such as data centers and advanced manufacturing, have given rise to unprecedented new demand growth and customized long-term electric service agreements. We believe that our recommendations are consistent with Treasury Department guidance regarding the relaxation of certain long standing private use restrictions on tax-exempt bonds provided in Revenue Procedure 2017-13 and Revenue Procedure 2018-26.

APPA is the voice of not-for-profit, community-owned utilities that power 2,000 towns and cities nationwide. We represent public power before the federal government to protect the interests of the more than 55 million customers that public power utilities serve, and the 100,000 people they employ. Public power utilities are generally units of state or local government, including political subdivisions of a state, instrumentalities, agencies, and joint powers agencies.

### **Background**

The surge in U.S. electricity demand, particularly within the commercial sector, underscores the ongoing transformation toward a more electrified economy. The scale of AI data centers alone and their commensurate power needs are growing exponentially. According to S&P Market Intelligence, annual electricity demand from US data centers is expected to reach 530 terawatt-hours (TWh) by 2028, or

slightly more electricity than what the entire state of Texas produced in 2022.<sup>1</sup> McKinsey & Co. forecasts that U.S. data centers will use 606 TWh of electricity by 2030, up from 147 TWh in 2023.<sup>2</sup> The growth in AI is turning data centers into giant energy users outpacing electric vehicles, hydrogen, and other emerging sectors in power demand growth. By 2035, Bloomberg forecasts that data centers are projected to account for 8.6 percent of all U.S. electricity demand, more than double their 3.5 percent share today.<sup>3</sup>

The United States is seeking to position itself as a global leader in AI. In January 2025, President Trump issued Executive Order 14179 stating that “It is the policy of the United States to sustain and enhance America’s global AI dominance in order to promote human flourishing, economic competitiveness, and national security.”<sup>4</sup> This Executive Order has been followed by other policy actions of the Administration. In July 2025, the White House published *Winning the Race: America’s AI Action Plan*, highlighting three key focus areas for AI: accelerating AI innovation, building AI infrastructure, and leading in international AI diplomacy and security.<sup>5</sup>

Energy-intensive advanced technologies, such as AI, automation, advanced manufacturing, and data centers, are essential for the U.S. economy to maintain economic competitiveness. To fully realize the potential benefits of these technologies, substantial investments in energy infrastructure are necessary. This includes expanding transmission and distribution networks, modernizing the grid, and increasing energy generation capacity. These investments will not only support growing electricity demand but also ensure that the U.S. economy can continue to grow competitively and sustainably and win the AI race. Meeting new energy requirements will necessitate substantial capital investment in such facilities by APPA members.

The private activity bond regulations regarding output facilities have a historic foundation that is unique and dissimilar to the concepts and tax policy generally applicable to other governmental bonds. The private activity bond regulations applicable to governmental bonds for other than “output facilities” are generally based on the doctrine of “special legal entitlement” and whether such entitlement has been

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<sup>1</sup> S&P Executive Summary (2024). US datacenter and energy report. <https://pages.marketintelligence.spglobal.com/Datacenter-renewables-US-Datacenter-and-Energy-Report-MS.html>.

<sup>2</sup> McKinsey & Company (November 6, 2024). How data centers and the energy sector can sate AI’s hunger for power. [www.mckinsey.com/industries/private-capital/our-insights/how-data-centers-and-the-energy-sector-can-sate-ais-hunger-for-power](https://www.mckinsey.com/industries/private-capital/our-insights/how-data-centers-and-the-energy-sector-can-sate-ais-hunger-for-power).

<sup>3</sup> Bloomberg NEF (April 15, 2025). <https://about.bnef.com/insights/commodities/power-for-ai-easier-said-than-built>

<sup>4</sup> The White House (January 23, 2025). Removing barriers to American leadership in artificial intelligence. <https://www.whitehouse.gov/presidential-actions/2025/01/removing-barriers-to-american-leadership-in-artificial-intelligence>

<sup>5</sup> The White House (July 2025). Winning the race: America’s AI action plan. [www.whitehouse.gov/wp-content/uploads/2025/07/Americas-AI-Plan.pdf](https://www.whitehouse.gov/wp-content/uploads/2025/07/Americas-AI-Plan.pdf). See also, Executive Order 14318, accelerating federal permitting of data centers. [www.whitehouse.gov/presidential-actions/2025/07/accelerating-federal-permitting-of-data-center-infrastructure](https://www.whitehouse.gov/presidential-actions/2025/07/accelerating-federal-permitting-of-data-center-infrastructure).

provided to a non-governmental entity. Under the special legal entitlement doctrine, private business use can arise under a range of agreements with non-governmental entities, including arrangements with a duration of no more than 200 days.

On the other hand, the private activity bond regulations applicable to governmental bonds for output facilities have been based on the doctrine of “benefits and burdens” and whether such benefits and burdens have been transferred to a non-governmental entity. It has been clear since the early 1970s Treasury Department guidance that, in the case of sales of output from output facilities, the private business use and private payment or security tests were met only in the case of a contract that transfers the benefits of owning the facility and the burdens of paying debt service on the related bonds to the output purchaser. This long-established regulatory doctrine of benefits and burdens with respect to output facilities provides for a “high bar” or threshold with respect to a determination of private business use.

It is worth noting that trying to avoid private business use restrictions by issuing taxable debt to finance output facilities is not generally a solution. First, issuing taxable debt increases the costs of these investments. Second, it still may not protect existing debt. Specifically, the private business use rules apply system-wide to all the facilities of the public power utility that have been financed with tax-exempt bonds. Thus, a single contract giving rise to private use can cause outstanding tax-exempt bonds to become taxable private activity bonds, triggering costly bond redemptions across all outstanding bond issues and raising costs for existing customers.

In promulgating the Output Regulations, the Treasury and IRS actively sought information regarding regulatory changes imposed by the Federal Energy Regulatory Commission, state and local government formations of independent transmission operators, changes in the electricity markets, and related matters to accommodate such changes. Beginning in 1998, both sets of temporary regulations through the release of the final Output Regulations were generally accommodative to such changes as acknowledged in the preamble of the Output Regulations as set forth below –

*Congress passed the Energy Policy Act of 1992, Public Law 102-486 (106 Stat. 2776), to encourage restructuring of the electric power industry. Since that time, the FERC and many states have adopted policies to provide open access to transmission and distribution facilities. Treasury and the IRS are aware that these initiatives have caused many changes in the electric power industry, and that restructuring efforts are ongoing ... Commentators stated that the lack of final regulations addressing these issues has hindered public power systems in undertaking long-term planning. Commentators also stated that uncertainty regarding the characterization under the private business use test of certain open access transactions has hampered participation by public power systems in open*

*access plans. The final regulations are being issued at this time in order to address these concerns, notwithstanding the restructuring initiatives continue to evolve* (emphasis added).

As noted in the preamble language above, the Treasury Department was aware that electric sector changes were ongoing and evolving at the time of publication of the Output Regulations and such efforts have continued to evolve in the energy markets.

In the wake of new energy demands, the continued viability of public power systems is essential to meet the energy needs of its urban and rural customers. Set forth below are APPA's recommendations for changes to the Output Regulations and related matters. Given that the public power systems operate on an integrated-systems approach, we believe that all the proposed changes described below are warranted.

### **Treatment of Retail Requirements Contracts**

At the present time, large retail electric customers are seeking to negotiate customized contracts for electric service with municipal and other utilities. Various factors have led to this trend by large retail customers, including growing energy use by various industry sectors as noted above, the ability of industries to lock in power rates, and assurance of adequate supply during peak-use periods. Serving and retaining these retail customers is critical to public power utilities. Moreover, these retail customers are important to their communities as sources of local employment and property taxes. In sum, the inability of public power utilities to serve these customers with electric service arrangements can be unsettling and disruptive to a community. Conversely, a lack of relief needlessly hinders utilities serving nearly 15 percent of the nation's retail customers from helping address these needs.

However, serving these large retail electric customers under the existing Output Regulations can also create certain financial risks for public power utilities. If the customer is not contractually committed for a sufficient term, the utility and its other customers may be exposed to stranded costs should the customer not use some or all the new power facilities built to meet its forecasted need. This risk is further heightened by the increasing ability of large retail customers to shop among competing electricity providers. The Output Regulations presently limit the ability of public power utilities to enter customized contracts. This limitation puts public power utilities at risk of losing large retail electric customers, which in turn puts the risk of stranded assets on remaining customers.

Generally, to provide the level of service required by a large retail customer, a public power utility may have to spend substantial funds to upgrade its system and/or finance specific improvements that are necessary to serve that particular customer. As an economic matter, if that large retail customer is not obligated to remain a customer for a sufficient period to recoup these investments, the public power utility

(and by implication, all of its other customers) have financial exposure and they will bear the cost of such improvements (i.e., stranded costs) if the large customer goes out of business or relocates.

Prior to the enactment of the Tax Reform Act of 1986, requirements contracts – both wholesale and retail – did not result in private business use. The Output Regulations changed the prior law interpretation for all requirements contracts. As noted in various APPA comments provided to the Treasury on the temporary output regulations, APPA continues to disagree with the Treasury Department’s treatment of requirements contracts as contracts that can result in private business use.

Despite pre-1986 Act rulings to the contrary, under Treasury Regulations section 1.141-7(c)(3), a retail requirements contract will result in private business use to the extent that it contains contractual terms that obligate the purchaser to make payments that are not contingent on the purchaser’s requirements or that obligate the purchaser to have requirements. These sorts of provisions are often referred to in the industry as “minimum demand” provisions. If a retail requirements contract contains such provisions, then it will result in private business use of any tax-exempt bonds that financed the output being provided under the contract unless the contract meets an exception from private business use.

In contrast, the regulations contain somewhat more generous rules for wholesale requirements contracts. For example, with respect to wholesale requirements contracts, the Output Regulations permit contracts with terms of five years or 30 percent of the term of the bonds, whichever is shorter. Unlike the rules governing retail requirements contracts, the wholesale purchaser can be required to make payments to the public power utility that are not contingent on it having electricity requirements.

One private use exception is the exception for short-term output contracts under Treasury Regulations section 1.141-7(f)(3). This exception provides that an output contract does not result in private business use if:

- (i) The term of the contract, including all renewal options, is not longer than three years;
- (ii) The contract either is a negotiated, arm's-length arrangement that provides for compensation at fair market value, or is based on generally applicable and uniformly applied rates; and
- (iii) The output facility is not financed for the principal purpose of providing that facility for use by that nongovernmental person.

#### **Recommendation - Certain Sales for Large Retail Customers Under Section 1.141-7(f)(3)**

Viewed through the lens of the benefits and burdens doctrine and given the existing inequity in treatment between wholesale and retail requirements contracts with respect to minimum demand provisions, APPA

believes that certain retail requirements customers should be permitted to make payments to public power utilities that are not contingent on output requirements. Without such relief, public power utilities face significant risk serving large customers, which can materially increase a system's load within a single planning cycle. Building generation and distribution for large retail customers often take years with decades-long payback, but under the existing regulations, such contracts are limited to just three years. This forces public power utilities to either assume system-wide financial risk or decline to serve large, new customers, which may be essential to the local economy and jobs.

We understand the Administration's focus on larger capacity projects as key to meeting its goals given projected output demands. However, we would also note that the fastest growing segment of the market is reportedly edge data centers of 500 kilowatts (KW) to 2 megawatts (MW) of capacity.<sup>6</sup> These smaller data centers are critical for reducing latency, bringing computing capability geographically closer to those users situated further away from the heart of the cloud. Many utilities can incorporate such customers into their existing rate structure, but for most public power utilities, a customer of even such size would impose substantial stranded risk to remaining customers. For example, for two thirds (65 percent) of public power utilities, a single 2 MW customers would be 10 percent or more of their peak load. And for 91 percent of public power utilities, one 20 MW customer (or collection of customers) would be more than 10 percent of their peak demand. It is also worth noting that majority of these smaller utilities are rural utilities as defined by the Department of Agriculture.

It is acknowledged that the larger data centers will drive the race to build the bold, large-scale plans necessary to create the policy result envisioned by the Administration. However, we believe it is not only appropriate, but critical to allow communities of all sizes, rural and urban, to participate and serve smaller "large" customers, including edge data centers. As such, we would request that any definition of "large" for purposes of the proposed amendments to section 1.141-7(f)(3) be flexible enough to do so. Specifically, we would propose that a large customer be defined as one demand from which exceeds the lesser of 20 MW or 10 percent of the utility's peak demand.

In light of the above, set forth in Exhibit A, we propose changes to the private business use exception in Treasury Regulations section 1.141-7(f)(3). Our proposal would directly address the difficulties facing public power utilities as they deal with unprecedented load growth from large retail customers.

The amendment defines a "large customer" as a customer and any related parties that are expected within five years of the issue date of the relevant issue of tax-exempt bonds to have a power demand that

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<sup>6</sup> Jones Lang LaSalle IP, Inc., "Why Smaller Data Centers Are Taking Off: AI, 5G, and Hybrid Work Are Fueling the Rise of 'Edge Computing,'" <https://www.jll.com/en-us/insights/why-smaller-data-centers-are-taking-off> (last visited Dec. 10, 2025).

exceeds the lesser of 20 megawatts or 10 percent of the utility's peak demand. The amendments provide in such case the existing three-year contract requirement be extended to 15 years for large customers.

The amendment also clarifies the existing regulatory language regarding whether a bond-financed facility was financed with a "principal purpose" of providing it for use by a nongovernmental person. The amendments provide that an output contract with a nongovernmental person will not be treated as financed for a principal purpose of providing the facility to a nongovernmental person if the output facility is part of the governmental unit's integrated system and is not designed, built, or contractually allocated to the exclusive requirements of that person (other than incidental features).

### **Acquisition of Existing Output Facilities**

Section 141(d) generally prevents state and local governments from issuing tax-exempt bonds to acquire privately-owned output facilities. The provision contains exceptions designed to permit the acquisition of existing private facilities by public power utilities to serve: (i) a qualified service area, and (ii) a qualified annexed area. The exceptions contained in section 141(d)(3) are unclear, difficult and burdensome to apply especially in the context of complex electric systems with multiple electric generating assets. We believe that navigating the complexity created by section 141(d) is likely to become more common for APPA members as output demands grow.

No guidance has been issued by Treasury under section 141(d) since the statute was enacted in 1987. The lack of guidance in this area has frustrated public power utilities and have not kept up with the pace of energy industry developments. To meet the increased demand for generation from large customers, public power utilities will need to acquire or construct generation capacity from a variety of sources. In many cases, a privately-owned asset may be available for sale that could help a public power utility to meet its energy requirements. Also, many public power utilities currently acquire power from privately owned generating facilities through power purchase agreements. These agreements may give the public power utility the option to acquire the generating facilities. Section 141(d) generally blocks a utility from purchasing such output facilities given the adverse tax risk to outstanding tax-exempt bonds or bonds issued to finance the acquisition of the property.

Importantly, the legislative history of section 141(d) provides that sales of electricity that do not result in private business use are treated as qualified sales for purposes of the exceptions provided in section 141(d)(3). The relevant portion of the legislative history is as follows:

*The conference agreement does not preclude a governmental authority from acquiring reasonable amounts of capacity beyond the authority's current demand needs while qualifying under either of the two exceptions provided in the agreement. However, no capacity beyond that*



*necessary to meet current output demands may be acquired if that capacity will be used in a manner that gives rise to an amount of private use of bond proceeds sufficient to characterize the bonds issued as part of the issue used to acquire the facilities as private activity bond...*

Notably, similar compliance-related issues also arose after the adoption of the regulations related to electricity and gas prepayments. The prepayment provisions, like the exception in section 141(d), focus on the actual use of gas and electricity after the bond issuance. To minimize complexity, Congress enacted a statutory “safe harbor” under section 148 pursuant to which compliance with the rules for prepayments could be based on historical use in the service area of the prepaid purchaser.

### Recommendations

1. Section 141(d) should be clarified by stating that output sales that do not give rise to private business use under the Output Regulations are not taken into account for purposes of section 141(d). Such a proposal would account for the amendments that we have proposed above with respect to the private business use rules applied to large customers.
2. For purposes of the existing service area exception of section 141(d), a clear safe harbor should be modeled based on the utility’s historic sales of electricity over the prior five years to customers in its service areas. This latter safe harbor is modeled on section 148(b)(4)(B) of the Code, which relates to a similar rule requiring the use of energy acquired in a prepayment transaction in the historic service area of the utility.

### Equity Allocations for Public Power Utilities

In 2015, final regulations were promulgated under Treasury Regulation 1.141-6, which provide for the ability of issuers to allocate private business use to equity and to allocate government use to the tax-exempt bonds contributed to the project (the “Allocation Regulations”). Although the Allocation Regulations are very helpful in structuring new bond issues, APPA believes that the regulations need to be more comprehensive in nature and should be applicable to all outstanding bond issues. In particular, the Allocation Regulations do not adequately assist issuers with respect to bond issues unable to elect into the 1997 private activity bond regulations.

The “same plan of financing” definition provided in Treasury Regulation section 141-6(b)(4) provides, in part, that qualified equity includes payments made for capital expenditures for a project: (i) no earlier than a date on which such expenditures would be eligible for reimbursement under Treasury Regulation section 1.150-2(d)(2), and (ii) no later than the date on which the measurement period begins (i.e., the place in service date). Many APPA members have used equity funds over the years to finance improvements that fall outside either the reimbursement window or the placed in-service



date/measurement period window. Absent specific guidance, many issuers are in a position where they may obtain no "credit" for their uses of equity.

Moreover, the Allocation Regulations are generally tailored to the financing of individual buildings and facilities. In contrast, APPA members focus on system use – generation, transmission, and distribution assets, rather than particular facilities within those systems when financing improvements. For example, sales of output are often made on a system-wide basis rather than with respect to a single generation unit. To add to the complexity, a single generation unit may be financed with multiple tax-exempt bond issues and equity, as such, it can be difficult to allocate various funding sources in a manner that provides a fair and effective allocation of the equity for private business use purposes.

#### Recommendations

1. For equity used to fund capital expenditures in a particular facility or system prior to the publication of the Output Regulations, any reasonable method of allocating those expenditures to the facility or system should be permitted.
2. Equity should be permitted to be allocated across a generation, transmission, or distribution facility or system in any reasonable method, including by permitting that equity to “float” within such systems or facilities.

We appreciate your attention and consideration of our recommendations. We believe that the proposed changes are consistent with and will advance the Administration’s AI goals. We welcome the opportunity to discuss these proposals with you at your convenience and please feel free to contact me at [jgodfrey@publicpower.org](mailto:jgodfrey@publicpower.org), (202) 256-7710.

Sincerely,

*/s/ John Godfrey*

John Godfrey  
Senior Government Relations Director

## Exhibit A

### Proposed Amendments to Treasury Regulations 1.141-7 Special Rules for Output Facilities

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(f) \* \* \*

(3) Short-term output contracts. An output contract with a nongovernmental person is not taken into account under the private business tests if –

- (i) The term of the contract, including all renewal options exercisable by the nongovernmental person, is not longer than three years (or 15 years in the case of a contract with a qualified large retail customer (as defined in subparagraph (iv))).
- (ii) The contract either is a negotiated, arm's-length arrangement that provides for compensation at fair market value, or is based on generally applicable and uniformly applied rates; and
- (iii) The output facility is not financed for a principal purpose of providing that facility for use by that nongovernmental person. An output facility will not be treated as financed for a principal purpose of providing it for use by a nongovernmental person if the output facility is part of the governmental unit's integrated system and is not designed, built, or contractually allocated to the exclusive requirements of that person (other than incidental features).
- (iv) Qualified large retail customer. For purposes of this subsection (f), a person is a qualified large retail customer with respect to an output contract if:
  - (A) that person purchases output at retail under the contract; and
  - (B) that person reasonably expects on the effective date of the contract that the demand for output of that person, plus the demand of any related party, will, at any time within the five years on or after the effective date of that contract, exceed the lesser of 20 megawatts or 10 percent of the utility's peak demand in the aggregate at one or more locations, including demand under that contract or any other arrangement between that person (or any related party, as defined in section 1.150-1(b)) and the issuer (or any related party, as defined in section 1.150-1(b)).

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