

Sen. Wyden Data Center Tax Package Discussion Draft

Short Summary

The proposed legislation addresses the impact of the AI and data center buildout through two main strategies: 1) establishing a federal gross receipts excise tax on data center operators, and 2) removing unnecessary investment incentives for data centers.

Data Center Services Gross Receipts Excise Tax

The discussion draft imposes an excise tax on gross receipts for data center services. A data center is broadly described as the facility or location where data center equipment is housed. Data center services include, among other things, AI training, inference, and data storage, as well as any services from data centers above 25 megawatts in size. There are carve outs for small operators, internet infrastructure, and traditional IT departments. The tax rate will be determined once revenue estimates are available.

To prevent tax avoidance from vertical integration or complex financial arrangements prevalent in the industry, there is an alternative tax on data centers serving the largest hyperscale developers (those with at least \$10 billion of data center assets) and the largest users of data centers (those with at least \$1 billion in annual data center utilization expense). If a data center is providing services to these taxpayers, then it is subject to the tax based on its imputed data center gross receipts. Imputed gross receipts are calculated as the cost of deploying the data center assets and operating the data center, and applying a roughly 40 percent profit margin.

Removal of Unnecessary Investment Incentives

Bonus Depreciation: the discussion draft eliminates 100-percent bonus depreciation for all data center assets placed in service after enactment.

Opportunity Zones: the discussion draft disqualifies data center businesses and data center assets acquired after enactment from being OZ businesses or property.

Private REITs: A REIT whose stock is not traded on an SEC-registered national securities exchange cannot include rents from data centers acquired after the date of enactment as “qualifying income.”

Research Credit: the discussion draft explicitly clarifies current law which prohibits claiming research credits for data center build out costs. This provides certainty in an area of tax law that may be currently subject to inappropriate use.

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Technical Summary

The data center tax package has two major components. One, the creation of a new excise tax on U.S. data centers (section 2 of the bill), and two, the removal of unnecessary incentives for data center build outs (sections 3-6 of the bill).

Section 2: Data Center Services Gross Receipts Excise Tax

Data Center Services Gross Receipts Excise Tax

New Section 5000E imposes an excise tax on any data center operator. The tax is imposed on the gross receipts attributable to data center services provided from a U.S. data center. The tax rate is to be determined.

The definitions in section 5000H provide the basic contours of which taxpayers are subject to the data center excise tax, by defining “data center” and “data center services.”

A data center is broadly described as the facility or location where data center equipment is housed. Data center equipment is electronic equipment used to process, store, and transmit digital information, housed together in a climate-controlled facility designed to maintain optimal operating conditions.

Data center services are defined as:

- Data storage services, cloud services, artificial intelligence training services, inference services, high-volume data processing, other similar services, and other services determined by the Secretary to be comparable to such services,
- Services that use data center equipment on a data center that is 25MW or greater in size, and
- Services that use data center equipment, and which the provisions of those services are a substantial element of the trade or business of the taxpayer.

5000E and 5000H also provide certain exceptions and adjustments to the application of the tax. The exceptions include:

- Small operators. If a data center operator meets the gross receipts test of IRC 448(c), which is \$32 million as of 2026, they are not subject to the tax if they are not servicing hyperscale entities.
- Internet infrastructure. A data center does not include an internet infrastructure data center, such as those providing web hosting or providing broadband internet access.

- IT departments. A data center does not include an IT department data center. There is an exclusion for a taxpayer's data center equipment that is not a substantial part of their business. It applies if either:
 - The total deductions attributable to data center equipment is less than 5 percent of the total deductions of the taxpayer—i.e., owning data center equipment is a relatively small share of the total costs for a taxpayer, or
 - The unadjusted basis of all data center equipment is less than \$25 million.
- There is transition relief for taxpayers that have data center assets put into service before 2025. Until 2030, taxpayers can reduce the amount of their tax, based on what share of assets (using unadjusted basis) were put in service before 2025. E.g., if in 2028, 30 percent of data center assets were placed in service before 2025, the tax due would be reduced by 30 percent.

Alternative Tax on Services from Hyperscale Data Centers

The data center ecosystem is highly complex, with many interlocking relationships between actors in the space. In addition, some companies are vertically integrated, with large corporations providing data center services to themselves, rather than 3rd parties. In both cases, there may not be delineated gross receipts paid for data center services.

To prevent avoidance of the tax in both types of situations, section 5000F creates an alternative tax on services provided by data center operators from “hyperscale data centers.” The alternative tax applies the same rate as the tax under 5000E, calculated on the “imputed data center gross receipts” of the hyperscale data center. The greater of the amount calculated under the alternative tax or the amount under 5000E is the tax due.

Hyperscale data center

Identifying a hyperscale data center is functionally a two-part test: 1) is there a hyperscale entity, and 2) does it have a close economic relationship with the data center from which the services are being provided.

To satisfy the first part of the test, a business qualifies as a hyperscale entity if it fits into one of two groups: 1) major data center operators, or 2) major data center payors. Major data center operators are parties that own or use data center equipment with an unadjusted basis of at least \$10 billion in the prior year. Major data center payors are the parties that have data center services expenses of at least \$1 billion in the prior year.

To satisfy the second part of the test, a data center must have one of three distinct relationships to hyperscale entities:

- Hyperscale-owned data center. One or more hyperscale entities own a majority of the equipment in the data center.
- Hyperscale-controlled data center. One or more hyperscale entities utilize (or have the right to utilize) a majority of the data center's services for most of the year.
- Hyperscale-financed data center. One or more hyperscale entities provided a majority of the financing (in equity or debt) to build or operate the data center, or have the right to force the sale of the operator or the assets.

In the alternative tax, the data center operator is the party subject to the alternative tax on the imputed data center gross receipts from the hyperscale data centers.

Imputed data center gross receipts

The alternative tax applies a statutory "cost-plus" method to determine imputed data center gross receipts. The imputed data center gross receipts consists of three parts:

- The data center depreciable asset use amount,
- The applicable data center costs, and
- A profit addition.

First, the data center depreciable asset use amount reflects the cost associated with the use of depreciable assets, such as servers and computers. For simplicity, in most years, the depreciable asset use amount is the same as the taxable depreciation for each asset. Note that as bonus depreciation for data centers is repealed in this broader package, standard depreciation rules (such as MACRS) would apply to data center assets.

Special rules apply for distinct cases:

- Land is generally not depreciated, so land is incorporated by treating it similar to nonresidential real property, i.e., as if it had a 39-year depreciable life.
- If assets have reached the end of their tax depreciation life but continue to be in use (e.g., a 5-year asset is in its 8th year of use), the amount used is 80 percent of the amount used in the final full year of depreciation.
- If assets are disposed of before the end of their depreciable life, any remaining depreciation is included in the depreciable asset use amount in the year of disposition.
- For most short-term assets (3-years or less), the taxpayer can elect to treat the amount spent as a cost rather than an asset.
- For assets placed in service prior to the date of enactment of this legislation, depreciation is recalculated as if bonus depreciation did not apply when originally placed in service. As a result, any depreciation that would have occurred (absent

bonus depreciation) in years prior to this legislation's enactment is treated as taken into account in those prior years.

Second, the applicable data center costs include all the direct or allocable costs related to providing services from the data center. Significant costs include rent, energy, water, wages, and payment for services, as well as the allocable amount of other costs related to the data center. Allocable costs would include payments to third parties, as well as work performed in-house or by related parties.

Data center equipment that is leased rather than owned is included in the imputed data center gross receipts of the operator at the greater of 1) the lease or rental cost to the data center operator or 2) the data center depreciable asset use amount to the equipment owner.

Finally, a profit addition is applied. The data center depreciable asset use amount and the applicable data center costs are summed, and then a profit addition of 67 percent is added. A profit addition of 67 percent of costs is roughly equivalent to a 40 percent profit margin.¹

A provision to address orbital data centers is in development.

Section 3. Repeal of Bonus Depreciation for Data Center Assets

Section 3 eliminates bonus depreciation under section 168(k) for all data center assets placed in service in taxable years beginning after the date of enactment of this legislation. It applies to data centers that are 25 MW or larger. Data center assets placed in service in prior years would not lose bonus depreciation.

Section 4. Treatment Under Opportunity Zones

Section 4 amends Section 1400Z-2 to exclude businesses providing data center services from qualifying as qualified opportunity zone businesses. It also excludes data centers with a capacity of 25 MW or larger from being considered qualified opportunity zone business property. This section only applies to stock, capital or profits interests, and property acquired after the date of enactment of this legislation.

¹ Profit margins are typically profit as a share of revenues, and revenue is essentially costs plus profits. So, if revenue is \$167, and profit is \$67, the profit margin is 40%. If costs are \$100 and profits are \$67, this is a 67 percent profit addition to costs.

Section 5. Rents Received by Private Real Estate Investment Trusts from Data Centers

Section 5 amends Section 856(d)(2) to exclude certain rental income attributable to data centers from qualifying income (“good income”) necessary to retain tax-favored Real Estate Investment Trust (REIT) status. The new exclusion only applies to private REITs. For this purpose, a REIT is treated as a private REIT if less than 80% of its stock (by vote or value) is publicly traded on a national securities exchange, such as the New York Stock Exchange or NASDAQ. If a private REIT’s data center rental income is subject to this rule, it is not good income for either the 75-percent test in section 856(c)(3) or the 95-percent test in section 856(c)(2).

The rule only applies to rents earned from data centers acquired after the date of enactment of this legislation, and which are 25 MW or larger. As such, rents received after the enactment of this legislation can still be qualifying income to a private REIT if the related data center was acquired before the date of enactment. However, data centers placed in service before the date of enactment can produce rent that would not qualify as good income to the extent a private REIT acquired its interest in that legacy data center after the date of enactment.

Section 6. Clarify Disallowance of Research Credit for Expenses Paid for Data Center Equipment

This section amends Section 41(b)(2)(C) to clarify that a data center cannot be treated as “supplies” for purposes of the research credit.

This is added to increase certainty in the application of the law in response to reports that a large taxpayer may have been improperly claiming the credit. It includes “no inference” language to make clear that adding this provision does not create any implication that it was legal for a taxpayer to claim the research credit on data centers built in years prior to the introduction of the legislation or prior to this legislation becoming law.