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Data Center Working Group: Sustainability Subgroup Draft Recommendation on Incentivizing Outcomes in Data Center Development

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Scope

In areas across the country where data centers are targeted for growth, State and local jurisdictions have been developing legislation and local ordinances to ensure that this development conforms to the community's vision and values. In the past, these incentives have been focused on economic growth, and competitive measures to attract the industry to their communities. However, change is happening and Frederick along with Maryland has the opportunity to be in the forefront of data center sustainability trends.

What pushes this focus on sustainability? It is the recognition by an increasing number of communities that, as the Department of Energy has cited, **data centers are the most energy-intensive buildings.** They consume 10-50 times the energy per unit of floor space of a typical commercial office building and account for 2% of total US electricity use. These numbers are expected to increase significantly if measures and technologies aren't deployed in data centers to change the rate of growth in energy and water use.

One practice jurisdictions have taken is to incentivize specific types of actions to meet the community's goals on various fronts such as energy, public health, environment and more. Such incentives could move the industry to exceed state of the art practices and achieve "best in class" performance. The Appendix to this recommendation contains a summary matrix on state incentive programs linked to tax and other funding mechanisms. Below is a discussion on what we can learn from these efforts (and answers to recurring questions raised in the work group) and how they may point to innovative solutions.

Key Highlights of Relevant Existing Legislation/Ordinances

- Over the last 10-15 years, many States have focused on attracting data centers to their regions through a variety of incentives including sales, and personal property taxes as well as using economic development funds and general incentive programs.

- Local governments such as cities and counties have also moved toward their own incentives or shared incentives with the state. They tend to focus on local priorities more than the state incentive programs. These priorities can range from Chandler, Arizona's (see the revised Noise Recommendation for further details) recent passage of legislation highly focused on noise or the City of Virginia Beach creating zones where a bundling of various incentives is tied together to meet local community requirements.
- States have singled out areas they wish to support through these incentives, such as:

- Location in enterprise zones
- Location in rural and low-income counties
- Type of data centers services allowed – Internet and others
- Categories of equipment—computers, cooling and more
- Employment – e.g., at least 20 job hires at above average wages for the State
- Electricity
- Building square footage
- Size of investment.

➢ As the matrix depicts the investment levels qualifying for tax breaks vary significantly – from $1 million to over $250 million – see appendix.

Considerations/Recommendations (Recommendations are bolded and highlighted below)

➢ Many States provide cuts in property tax or sales tax on specific types of equipment including cooling. While the summary matrix only provides highlights, the details of qualifying for these tax breaks in some states can be complex. ***Given that precedent, Frederick should consider providing a sale (or other tax break) on Tier 4 data center equipment configurations to incentivize the most energy efficient, noise-mitigating and water conserving approaches in county data centers.***

➢ Moving toward sustainability objectives as opposed to economic development is a trend backed by Federal approaches under the Inflation Reduction Act—see below. ***The County should consider amplifying (add an additional percentage between 5-10 % if feasible) Federal tax credits where they are most applicable and relevant to Frederick County***:

- *Lawmakers … (have come to) a realization that the economic benefits of data center construction are limited. Since modern data centers are largely automated and don't require a lot of maintenance personnel, they don't typically create many new jobs or spur major revenue generation that benefits local businesses. Governments that once encouraged data center construction as a driver of economic growth may be realizing that, while there are some economic benefits to reap from attracting data centers to one's state or locality, they are not as rich as, say, convincing manufacturers to build factories that employ hundreds of workers.*

  *That said, another noticeable trend in data center tax incentivization policy is an increased push by the federal government to reward data center operators who prioritize sustainability. Several provisions in the Inflation Reduction Act of 2022 advanced this goal by, for example, providing financial rewards for purchasing carbon-reducing equipment inside data centers. [**Also noteworthy, the federal government increased the investment tax credit to 30% for standalone energy storage systems]***

  The obvious difference between this legislation and traditional tax incentives for data centers is that the federal government doesn't appear focused on encouraging the growth of the data center industry for economic reasons. Instead, it's all about

advancing data center sustainability – an area where federal lawmakers are hardly alone, given the current widespread interest in sustainability across the tech industry and beyond.

Source: Tozzi, **The State of Data Center Tax Incentives and Legislation in 2023**

- In developments where there is a site developer or master planned community manager, ***the ordinance language needs to recognize the potential for at least four distinct roles, with some being combined depending on how the services are offered***:
  - Data Center Infrastructure Manager – i.e., such as Quantum Loophole (QL)
  - Data Center Owner/Builder – i.e., Rowan
  - Data Center Operator (could be the builder, but could be another firm)
  - Customer.

- The above distinctions are important in the instance of Eastalco, a Master Planned Data Center Community, developed by QL because some features of the planned community (i.e., wooded areas for carbon sequestration provided by QL) are sustainability benefits shared by the community and not attributable to a specific operator. Who, then, claims the credit for these communal features in any possible sustainability reporting that the county may require? It shouldn't be duplicated for various builders/operators in reporting or to gain incentives because then the reduction effect (i.e., for GHG emission reduction) would be over-counted. ***Any reporting required by an ordinance/s should address and clarify this reporting issue.***

- Jurisdictions (State and local) – Michigan, New Jersey, Florida, and others use environmental escrow accounts for water, waste and as safeguards to protect wetlands from associated construction. In most cases, they are set aside to provide funds for remedial actions and other reclamation claims. ***It is a model worth examining for its applicability here in a future ordinance not only for typical uses today, but the possible extension of the model to relevant concerns here in the county.*** It provides sources of funding for issues that could arise down the road and cannot be foreseen today. It would protect the taxpayers of the County from handling the entire burden of any negative outcomes that required "cleanup" actions. Furthermore, since these accounts have been known to yield millions of dollars, ***they could be considered for a discounting system that would lower the amount of payment into the fund if the data center builder/operator demonstrated a "good faith" effort to mitigate circumstances through the use of advanced technologies deployed in the facility and approved by the government entity entering into the escrow account.*** These accounts are typically managed by 3rd-party banking-related entities.

- The State's movement toward a Building Energy Performance Standard (BEPS) has already spurred counties like Montgomery to consider implementing their own BEPS program (under consideration by the Montgomery County Council in 2024). A feature of the clauses under consideration is a renewable energy allowance as "credit" towards the performance target. The concept of a renewable energy credit tied to BEPS, or another incentive option could be a boost toward pushing alternative backup power options (compared with conventional diesel) or a partial onsite generation option. Another way to deploy BEPS is to ask for 5-10% performance above the goal cited for certain sized data centers and incentivize it with a tax break.

CAVEAT: This recommendation is intended to be representative of possibilities and not exhaustive. What is described here are suggestive actions that could be models for incentivizing other priorities or modified further to fit Frederick's own unique set of needs. It is not intended to exclude other possibilities, but tax breaks in general should focus on the "big" impact needs. Tax breaks can be tied to any number of features; however, it is the aim of this subgroup to focus on sustainability.

Sources

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