

## § 1.141-6

## 26 CFR Ch. I (4-1-02 Edition)

meet the tax assessment loan exception because the improvements to property owned by a nongovernmental person are not an essential governmental function under section 141(c)(2). The issue also meets the private business tests of section 141(b).

[T.D. 8712, 62 FR 2296, Jan. 16, 1997]

### § 1.141-6 Allocation and accounting rules.

(a) *Allocation of proceeds to expenditures.* For purposes of §§ 1.141-1 through 1.141-15, the provisions of § 1.148-6(d) apply for purposes of allocating proceeds to expenditures. Thus, allocations generally may be made using any reasonable, consistently applied accounting method, and allocations under section 141 and section 148 must be consistent with each other.

(b) *Allocation of proceeds to property.* [Reserved]

(c) *Special rules for mixed use facilities.* [Reserved]

(d) *Allocation of proceeds to common areas.* [Reserved]

(e) *Allocation of proceeds to bonds.* [Reserved]

(f) *Treatment of partnerships.* [Reserved]

(g) *Examples.* [Reserved]

[T.D. 8712, 62 FR 2297, Jan. 16, 1997]

### § 1.141-7T Special rules for output facilities (temporary).

(a) *Overview.* This section provides special rules to determine whether arrangements for the purchase of output from an output facility cause an issue of bonds to meet the private business tests. For this purpose, unless otherwise stated, water facilities are treated as output facilities. Sections 1.141-3 and 1.141-4 generally apply to determine whether other types of arrangements for use of an output facility cause an issue to meet the private business tests.

(b) *Definitions.* For purposes of this section and § 1.141-8T, the following definitions and rules apply:

(1) *Available output.* The available output of a facility financed by an issue is determined by multiplying the number of units produced or to be produced by the facility in one year by the number of years in the measurement period of that facility for that issue.

(i) *Generating facilities.* The number of units produced or to be produced by a generating facility in one year is determined by reference to its nameplate capacity or the equivalent (or where there is no nameplate capacity or the equivalent, its maximum capacity), which is not reduced for reserves, maintenance or other unutilized capacity.

(ii) *Transmission and other output facilities—(A) In general.* For transmission, cogeneration, and other output facilities, available output must be measured in a reasonable manner to reflect capacity.

(B) *Electric transmission facilities.* Measurement of the available output of all or a portion of electric transmission facilities may be determined in a manner consistent with the reporting rules and requirements for transmission networks promulgated by the Federal Energy Regulatory Commission (FERC). For example, for a transmission network, the use of aggregate load and load share ratios in a manner consistent with the requirements of the FERC may be reasonable. In addition, depending on the facts and circumstances, measurement of the available output of transmission facilities using thermal capacity or transfer capacity may be reasonable.

(iii) *Special rule for facilities with significant unutilized capacity.* If an issuer reasonably expects on the issue date that persons that are treated as private business users will purchase more than 20 percent of the actual output of the facility financed with the issue, the Commissioner may determine the number of units produced or to be produced by the facility in one year on a reasonable basis other than by reference to nameplate capacity, such as the average expected annual output of the facility. For example, the Commissioner may determine the available output of a financed peaking electric generating unit by reference to the reasonably expected annual output of that unit if the issuer reasonably expects, on the issue date of bonds that finance the unit, that an investor-owned utility will purchase more than 20 percent of the actual output of the facility during the measurement period under a take or pay contract, even if the amount of

output purchased is less than 10 percent of the available output determined by reference to nameplate capacity. The reasonably expected annual output of the generating facility must be consistent with the capacity reported for prudent reliability purposes.

(iv) *Special rule for facilities with a limited source of supply.* If a limited source of supply constrains the output of an output facility, the number of units produced or to be produced by the facility must be determined by reasonably taking into account those constraints. For this purpose, a limited source of supply shall include a physical limitation (for example, flow of water), but not an economic limitation (for example, cost of coal or gas). For example, the available output of a hydroelectric unit must be determined by reference to the reasonably expected annual flow of water through the unit.

(2) *Measurement period.* The measurement period of an output facility financed by an issue is determined under § 1.141-3(g).

(3) *Sale at wholesale.* For purposes of this section, a sale at wholesale means a sale of output to any person for resale.

(4) *Take contract and take or pay contract.* A *take contract* is an output contract under which a purchaser agrees to pay for the output under the contract if the output facility is capable of providing the output. A *take or pay contract* is an output contract under which a purchaser agrees to pay for the output under the contract, whether or not the output facility is capable of providing the output.

(5) *Transmission facilities—(i) In general.* *Transmission facilities* are facilities for the transmission or distribution of output.

(ii) *Special rule for ancillary services.* For purposes of paragraph (f)(5), transmission facilities include facilities necessary to provide ancillary services required to be offered as part of open access transmission tariffs under rules promulgated by the FERC under sections 205 and 206 of the Federal Power Act (16 U.S.C. 824d and 824e). Thus, if a facility also serves another function (for example, a facility that provides for operating reserves for transmission and also provides generation) an allo-

cable portion of the facility is treated as a transmission facility for purposes of paragraph (f)(5) of this section.

(6) *Nonqualified amount.* The nonqualified amount with respect to an issue is determined under section 141(b)(8).

(c) *Output contracts—(1) General rule.* The purchase by a nongovernmental person of available output of an output facility (output contract) financed with the proceeds of an issue is taken into account under the private business tests if the purchase has the effect of transferring substantial benefits of owning the facility and substantial burdens of paying the debt service on bonds used (directly or indirectly) to finance the facility (the benefits and burdens test). See paragraph (c)(5) of this section for the treatment of an output contract that is properly characterized as a lease for Federal income tax purposes. See paragraphs (d) and (e) of this section for rules regarding measuring the use of, and payments of debt service for, an output facility for determining whether the private business tests are met. See also § 1.141-8T for rules for when an issue that finances an output facility (other than a water facility) meets the private business tests because the nonqualified amount of the issue exceeds \$15 million.

(2) *Benefits and burdens test—(i) Benefits of ownership.* An output contract transfers substantial benefits of owning a facility if the contract gives the purchaser (directly or indirectly) rights to capacity of the facility on a basis that is preferential to the rights of the general public.

(ii) *Burdens of paying debt service.* An output contract transfers substantial burdens of paying debt service on an issue to the extent that the issuer reasonably expects that it is substantially certain that payments will be made under the terms of the contract (disregarding default, insolvency, or other similar circumstances). For example, an output contract is treated as transferring burdens of paying debt service on an issue if payments must be made upon contract termination.

(iii) *Payments pursuant to pledged contract.* Payments made or to be made under the terms of an output contract

that is pledged as security for an issue are taken into account under the private business tests even if the issuer reasonably expects that it is not substantially certain that payments will be made under the contract (disregarding default, insolvency, or other similar circumstances). For this purpose, an output contract is pledged as security only if the bond documents provide that the pledged contract cannot be substantially amended without the consent of bondholders or a trustee for the bondholders. This paragraph (c)(2)(iii) applies to pledges made on or after February 23, 1998, with respect to bonds that are subject to this section.

(3) *Take contract or take or pay contract.* The benefits and burdens test is met if a nongovernmental person agrees pursuant to a take contract or a take or pay contract to purchase available output of a facility.

(4) *Requirements contracts—(i) In general.* A requirements contract under which a nongovernmental person agrees to purchase all or part of its output requirements is taken into account under the private business tests only to the extent that, based on all the facts and circumstances, the contract meets the benefits and burdens test. See § 1.141-15T(f)(2) for special effective dates for the application of this paragraph (c)(4) to issues financing facilities subject to requirements contracts.

(ii) *Significant factors.* Significant factors that tend to establish that the benefits and burdens test is met under the rule set forth in paragraph (c)(4)(i) of this section include, but are not limited to—

(A) The purchaser's customer base has significant indicators of stability, such as large size, diverse composition, and a substantial residential component;

(B) The contract covers historical requirements of the purchaser, rather than only projected requirements that are in addition to historical requirements; and

(C) The purchaser agrees not to construct or acquire other power resources to meet the requirements covered by the contract.

(iii) *Special rule for retail requirements contracts.* In general, a requirements

contract that is not a sale at wholesale (a *retail requirements contract*) does not meet the benefits and burdens test because the obligation to make payments on the contract is contingent on the output requirements of a single user. Such a requirements contract in general meets the benefits and burdens test, however, to the extent that it contains contractual terms that obligate the purchaser to make payments that are not contingent on the output requirements of the purchaser or that obligate the purchaser to have output requirements. For example, a requirements contract with an industrial purchaser meets the benefits and burdens test if the purchaser enters into additional contractual obligations with the issuer or another governmental unit not to cease operations. A retail requirements contract does not meet the benefits and burdens test by reason of a provision that requires the purchaser to pay reasonable and customary damages (including liquidated damages) in the event of a default, or a provision that permits the purchaser to pay a specified amount to terminate the contract while the purchaser has requirements, in each case if the amount of the payment is reasonably related to the purchaser's obligation to buy requirements that is discharged by the payment.

(5) *Output contract properly characterized as a lease.* Notwithstanding any other provision of this section, an output contract that is properly characterized as a lease for Federal income tax purposes shall be tested under the rules contained in §§ 1.141-3 and 1.141-4 to determine whether it is taken into account under the private business tests.

(d) *Measurement of private business use.* If an output contract results in private business use under this section, the amount of private business use generally is the amount of output purchased under the contract.

(e) *Measurement of private security or payment.* The measurement of payments made or to be made by nongovernmental persons under output contracts as a percent of the debt service of an issue is determined under the rules provided in § 1.141-4.

(f) *Exceptions for certain contracts*—(1) *Small purchases of output.* An output contract is not taken into account under the private business tests if the average annual payments under the contract that are substantially certain to be made under paragraph (c)(2)(ii) of this section do not exceed 0.5 percent of the average annual debt service on all outstanding tax-exempt bonds issued to finance the facility, determined as of the effective date of the contract.

(2) *Swapping and pooling arrangements.* An agreement that provides for swapping or pooling of output by one or more governmental persons and one or more nongovernmental persons does not result in private business use of the output facility owned by the governmental person to the extent that—

(i) The swapped output is reasonably expected to be approximately equal in value (determined over periods of one year or less); and

(ii) The purpose of the agreement is to enable each of the parties to satisfy different peak load demands, to accommodate temporary outages, to diversify supply, or to enhance reliability in accordance with prudent reliability standards.

(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, is not longer than 1 year;

(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.

(4) *Special 3-year exception for sales of output attributable to excess generating capacity resulting from participation in open access.* The purchase of output of an electric generating facility by a nongovernmental person is not treated as private business use if all of the following requirements are met:

(i) The term of the contract is not longer than 3 years, including all renewal options.

(ii) The issuer does not make expenditures to increase the generating capacity of its system during the term of the contract that are, or will be, financed with proceeds of tax-exempt bonds (other than expenditures for property that does not increase the generating capacity of the system by more than 3 percent).

(iii) The governmental owner offers non-discriminatory, open access transmission tariffs for use of its transmission system pursuant to rules promulgated by the FERC under sections 205 and 206 of the Federal Power Act (16 U.S.C. 824d and 824e) (or comparable provisions of state law).

(iv) All of the output sold under the contract is attributable to excess capacity resulting from the offer of the non-discriminatory, open access transmission tariffs referred to in paragraph (f)(5)(iii) of this section.

(v) All payments received by the governmental owner under the contract (other than the portion of such payments described in § 1.141-4(c)(2)(C)) are applied as promptly as is reasonably practical to redeem tax-exempt bonds that financed the output facility in a manner consistent with § 1.141-12.

(5) *Special exceptions for transmission facilities*—(i) *Mandated wheeling.* Entering into a contract for the use of transmission facilities financed by an issue is not treated as a deliberate action under § 1.141-2(d) if—

(A) The contract is entered into in response to (or in anticipation of) an order by the United States under sections 211 and 212 of the Federal Power Act (16 U.S.C. 824j and 824k) (or a state regulatory authority under comparable provisions of state law); and

(B) The terms of the contract are bona fide and arm's length, and the consideration paid is consistent with the provisions of section 212(a) of the Federal Power Act.

(ii) *Actions taken to implement non-discriminatory, open access.* An action is not treated as a deliberate action under § 1.141-2(d) if it is taken to implement the offering of non-discriminatory, open access tariffs for the use of transmission facilities financed by an

issue in a manner consistent with rules promulgated by the FERC under sections 205 and 206 of the Federal Power Act (16 U.S.C. 824d and 824e) (or comparable provisions of state law). This paragraph (f)(5)(ii) does not apply, however, to the sale, exchange, or other disposition of transmission facilities to a nongovernmental person.

(iii) *Application of reasonable expectations test to certain current refunding bonds.* An action taken or to be taken with respect to transmission facilities refinanced by an issue is not taken into account under the reasonable expectations test of § 1.141-2(d) if—

(A) The action is described in paragraph (f)(5)(i) or (ii) of this section;

(B) The bonds of the issue are current refunding bonds that, directly or indirectly, refund bonds originally issued before February 23, 1998; and

(C) The weighted average maturity of the refunding bonds is not greater than the remaining weighted average maturity of those prior bonds.

(6) *Certain conduit parties disregarded.* A nongovernmental person acting solely as a conduit for the exchange of output among governmentally owned and operated utilities is disregarded in determining whether the private business tests are met with respect to financed facilities owned by a governmental person. Use of property by a power marketer in the trade or business of purchasing and reselling power, however, is taken into account under the private business tests.

(g) *Allocations of output facilities and systems—(1) Facts and circumstances analysis.* Whether output sold under an output contract is allocated to a particular facility (for example, a generating unit), to the entire system of the seller of that output (net of any uses of that system output allocated to a particular facility), or to a portion of a facility is based on all the facts and circumstances. Significant factors to be considered in determining the allocation of an output contract to financed property are the following:

(i) The extent to which it is physically possible to deliver output to or from a particular facility or system.

(ii) The terms of a contract relating to the delivery of output (such as delivery limitations and options or obliga-

tions to deliver power from additional sources).

(iii) Whether a contract is entered into as part of a common plan of financing for a facility.

(iv) The method of pricing output under the contract, such as the use of market rates rather than rates designed to pay debt service of tax-exempt bonds used to finance a particular facility.

(2) *Illustrations.* The following illustrate the factors set forth in paragraph (g)(1) of this section:

(i) *Physical possibility.* Output from a generating unit that is fed directly into a low voltage distribution system of the owner of that unit and that cannot physically leave that distribution system generally must be allocated to those receiving electricity through that distribution system. Output may be allocated without regard to physical limitations, however, if exchange or similar agreements provide output to a purchaser where, but for the exchange agreements, it would not be possible for the seller to provide output to that purchaser.

(ii) *Contract terms relating to performance.* A contract to provide a specified amount of electricity from a system, but only when at least that amount of electricity is being generated by a particular unit, is allocated to that unit. For example, a contract to buy 20 MW of system power with a right to take up to 40 percent of the actual output of a specific 50 MW facility whenever total system output is insufficient to meet all of the seller's obligations generally is allocated to the specific facility rather than to the system.

(iii) *Common plan of financing.* A contract entered into as part of a common plan of financing for a facility generally is allocated to the facility if debt service for the issue of bonds is reasonably expected to be paid, directly or indirectly, from payments substantially certain to be made under the contract (disregarding default, insolvency, or other similar circumstances).

(iv) *Pricing method.* Pricing based on the capital and generating costs of a particular turbine tends to indicate that output under the contract is properly allocated to that turbine.

(3) *Transmission contracts.* Whether use under an output contract for transmission is allocated to a particular facility or to a transmission network is based on all the facts and circumstances, in a manner similar to paragraphs (g)(1) and (2) of this section. In general, the method used to determine payments under a contract is a more significant contract term for this purpose than nominal contract path. In general, if reasonable and consistently applied, the determination of use of transmission facilities under an output contract may be based on a method used by third parties, such as reliability councils.

(4) *Allocation of payments.* Payments for output provided by an output facility financed with two or more sources of funding are generally allocated under the rules in § 1.141-4(c).

(h) *Examples.* The following examples illustrate the application of this section:

*Example 1. Joint ownership.* Z, an investor-owned electric utility, and City H agree to construct an electric generating facility of a size sufficient to take advantage of the economies of scale. H will issue \$50 million of its 24-year bonds, and Z will use \$100 million of its funds for construction of a facility they will jointly own as tenants in common. Each of the participants will share in the ownership, output, and operating expenses of the facility in proportion to its contribution to the cost of the facility, that is, one-third by H and two-thirds by Z. H's bonds will be secured by H's ownership interest in the facility and by revenues to be derived from its share of the annual output of the facility. H will need only 50 percent of its share of the annual output of the facility during the first 20 years of operations. It agrees to sell 10 percent of its share of the annual output to Z for a period of 20 years pursuant to a contract under which Z agrees to take that power if available. The facility will begin operation, and Z will begin to receive power, 4 years after the H bonds are issued. The measurement period for the property financed by the issue is 20 years. H also will sell the remaining 40 percent of its share of the annual output to numerous other private utilities under contracts of one year or less that satisfy the exception under paragraph (f)(3) of this section. No other contracts will be executed obligating any person to purchase any specified amount of the power for any specified period of time. No person (other than Z) will make payments substantially certain to be made (disregarding default, insolvency, or other similar circumstances) under para-

graph (c)(2) of this section that will result in a transfer of substantial burdens of paying debt service on bonds used directly or indirectly to provide H's share of the facilities. The bonds are not private activity bonds, because H's one-third interest in the facility is not treated as used by the other owners of the facility. Although 10 percent of H's share of the annual output of the facility will be used in the trade or business of Z, a non-governmental person, under this section, that portion constitutes not more than 10 percent of the available output of H's ownership interest in the facility.

*Example 2. Requirements contract treated as take contract.* (i) City J issues 20-year bonds to acquire an electric generating facility having a reasonably expected economic life substantially greater than 20 years and a nameplate capacity of 100 MW. The available output of the facility under paragraph (b)(1) of this section is approximately 17,520,000 MWh (100 MW × 24 hours × 365 days × 20 years). On the issue date, J enters into a contract with T, an investor-owned utility, to provide T with all of its power requirements for a period of 10 years, commencing on the issue date. J reasonably expects that T will actually purchase an average of 30 MW over the 10-year period. Based on all of the facts and circumstances, including the size, diversity, and composition of T's customer base, J reasonably expects that it is substantially certain (disregarding default, insolvency, or other similar circumstances) that T will actually purchase only an average of 26 MW over the 10-year period. The contract is a requirements contract that must be taken into account under the private business tests pursuant to paragraph (c)(4) of this section because it provides T with substantial benefits of ownership (rights to capacity) and obligates T with substantial burdens of making payments that the issuer reasonably expects are substantially certain.

(ii) Under paragraph (d) of this section, the amount of reasonably expected private business use under this contract is approximately 15 percent (30 MW × 24 hours × 365 days × 10 years, or 2,628,000 MWh) of the available output. Accordingly, the issue meets the private business use test. J reasonably expects that the amount to be paid for an average of 26 MW of power (less the operation and maintenance costs directly attributable to generating that 26 MW of power), will be more than 10 percent of debt service on the issue on a present-value basis. The payment for 26 MW of power is an amount that J reasonably expects is substantially certain to be made under paragraph (c)(2) of this section. Accordingly, the issue meets the private security or payment test because J reasonably expects that it is substantially certain that payment of more than 10 percent of the debt service will be indirectly derived from payments by T. The

bonds are private activity bonds under paragraph (c) of this section. Further, if 15 percent of the sale proceeds of the issue is greater than \$15 million and the issue meets the private security or payment test with respect to the \$15 million output limitation, the bonds are also private activity bonds under section 141(b)(4). See § 1.141-8T.

*Example 3. Allocation of existing contracts to new facilities.* Power Authority K, a political subdivision created by the legislature in State X to own and operate certain power generating facilities, sells all of the power from its existing facilities to four private utility systems under contracts executed in 1999, under which the four systems are required to take or pay for specified portions of the total power output until the year 2029. Existing facilities supply all of the present needs of the four utility systems, but their future power requirements are expected to increase substantially beyond the capacity of K's current generating system. K issues 20-year bonds in 2004 to construct a large generating facility. As part of the financing plan for the bonds, a fifth private utility system contracts with K to take or pay for 15 percent of the available output of the new facility. The balance of the output of the new facility will be available for sale as required, but initially it is not anticipated that there will be any need for that power. The revenues from the contract with the fifth private utility system will be sufficient to pay less than 10 percent of the debt service on the bonds (determined on a present value basis). The balance, which will exceed 10 percent of the debt service on the bonds, will be paid from revenues derived from the contracts with the four systems initially from sale of power produced by the old facilities. The output contracts with all the private utilities are allocated to K's entire generating system. See paragraphs (g)(1) and (2) of this section. Thus, the bonds meet the private business use test because more than 10 percent of the proceeds will be used in the trade or business of a nongovernmental person. In addition, the bonds meet the private security or payment test because payment of more than 10 percent of the debt service, pursuant to underlying arrangements, will be derived from payments in respect of property used for a private business use.

*Example 4. Allocation to displaced resource.* Municipal utility MU, a political subdivision, purchases all of the electricity required to meet the needs of its customers (1,000 MW) from B, an investor-owned utility that operates its own electric generating facilities, under a 50-year take or pay contract. MU does not anticipate that it will require additional electric resources, and any new resources would produce electricity at a higher cost to MU than its cost under its contract with B. Nevertheless, B encourages MU to construct a new generating plant sufficient

to meet MU's requirements. MU issues obligations to construct facilities that will produce 1,000 MW of electricity. MU, B, and I, another investor-owned utility, enter into an agreement under which MU assigns to I its rights under MU's take or pay contract with B. Under this arrangement, I will pay MU, and MU will continue to pay B, for the 1,000 MW. I's payments to MU will at least equal the amounts required to pay debt service on MU's bonds. In addition, under paragraph (g)(1)(iii) of this section, the contract among MU, B, and I is entered into as part of a common plan of financing of the MU facilities. Under all the facts and circumstances, MU's assignment to I of its rights under the original take or pay contract is allocable to MU's new facilities under paragraph (g) of this section. Because I is a nongovernmental person, MU's bonds are private activity bonds.

*Example 5. Transmission facilities transferred to regional transmission organization.* (i) In 2001, the public utilities commission of State C adopts a plan for restructuring its electric power industry. The plan fosters competition by providing both wholesale and retail customers with non-discriminatory access to transmission facilities within the State. The plan provides that investor-owned utilities will transfer operating control over all of their transmission assets to a regional transmission organization (RTO), which is a nongovernmental person that will operate those combined assets as a single, state-wide system. Municipally-owned utilities are eligible for, but are not required to participate in, the open access system implemented by the RTO. The functions of the RTO include control of transmission access and pricing, scheduling transmission, control area operations, and settlements and billing. The RTO's compensation under its operating agreement with transmission owners is based on a share of net profits from operating the facilities. The restructuring plan is approved by the FERC pursuant to sections 205 and 206 of the Federal Power Act.

(ii) In 1994, City D had issued bonds to finance improvements to its transmission system. In 2001, D transfers operating control of its transmission system to the RTO pursuant to the restructuring plan. At the same time, D chooses to apply the private activity bond regulations of §§ 1.141-1 through 1.141-15 to the 1994 bonds. The operation of the financed facilities by the RTO results in private business use under § 1.141-3. Under the special exception in paragraph (f)(5) of this section, however, the transfer of control is not treated as a deliberate action. Accordingly, the transfer of control does not cause the 1994 bonds to meet the private activity bond tests.

*Example 6. Current refunding.* The facts are the same as in Example 5 of this paragraph (h), and in addition D issues bonds in 2003 to

currently refund the 1994 bonds. The weighted average maturity of the 2003 bonds is not greater than the remaining weighted average maturity of the 1994 bonds. D chooses to apply the private activity bond regulations of §§ 1.141-1 through 1.141-15 to the refunding bonds. In general, reasonable expectations must be separately tested on the date that refunding bonds are issued under § 1.141-2(d). Under the special exception in paragraph (f)(5) of this section, however, the transfer of the financed facilities to the RTO need not be taken into account in applying the reasonable expectations test to the refunding bonds.

[T.D. 8941, 66 FR 4665, Jan. 18, 2001]

**§ 1.141-8T \$15 million limitation for output facilities (temporary).**

(a) *In general*—(1) *General rule.* Section 141(b)(4) provides a special private activity bond limitation (the \$15 million output limitation) for issues 5 percent or more of the proceeds of which are to be used to finance output facilities (other than a facility for the furnishing of water). Under this rule, an issue consists of private activity bonds under the private business tests of section 141(b)(1) and (2) if the nonqualified amount with respect to output facilities financed by the proceeds of the issue exceeds \$15 million. The \$15 million output limitation applies in addition to the private business tests of section 141(b)(1) and (2). Under section 141(b)(4) and paragraph (a)(2) of this section, the \$15 million output limitation is reduced in certain cases. Specifically, an issue meets the test in section 141(b)(4) if both of the following tests are met:

(i) More than \$15 million of the proceeds of the issue to be used with respect to an output facility are to be used for a private business use. Investment proceeds are disregarded for this purpose if they are not allocated disproportionately to the private business use portion of the issue.

(ii) The payment of the principal of, or the interest on, more than \$15 million of the sales proceeds of the portion of the issue used with respect to an output facility is (under the terms of the issue or any underlying arrangement) directly or indirectly—

(A) Secured by any interest in an output facility used or to be used for a private business use (or payments in respect of such an output facility); or

(B) To be derived from payments (whether or not to the issuer) in respect of an output facility used or to be used for a private business use.

(2) *Reduction in \$15 million output limitation for outstanding issues*—(i) *General rule.* In determining whether an issue 5 percent or more of the proceeds of which are to be used with respect to an output facility consists of private activity bonds under the \$15 million output limitation, the \$15 million limitation on private business use and private security or payments is applied by taking into account the aggregate nonqualified amounts of any outstanding bonds of other issues 5 percent or more of the proceeds of which are or will be used with respect to that output facility or any other output facility that is part of the same project.

(ii) *Bonds taken into account.* For purposes of this paragraph (a)(2), in applying the \$15 million output limitation to an issue (the later issue), a tax-exempt bond of another issue (the earlier issue) is taken into account if—

(A) That bond is outstanding on the issue date of the later issue;

(B) That bond will not be redeemed within 90 days of the issue date of the later issue in connection with the refunding of that bond by the later issue; and

(C) 5 percent or more of the sale proceeds of the earlier issue financed an output facility that is part of the same project as the output facility that is financed by 5 percent or more of the sale proceeds of the later issue.

(3) *Benefits and burdens test applicable*—(i) *In general.* In applying the \$15 million output limitation, the benefits and burdens test of § 1.141-7T applies, except that “\$15 million” is substituted for “10 percent”, or “5 percent” as appropriate.

(ii) *Earlier issues for the project.* If bonds of an earlier issue are outstanding and must be taken into account under paragraph (a)(2) of this section, the nonqualified amount for that earlier issue is multiplied by a fraction, the numerator of which is the adjusted issue price of the earlier issue as of the issue date of the later issue, and the denominator of which is the issue price of the earlier issue. Pre-issuance accrued interest as defined in