

## Americas

# Demand for letters of credit surges as data centres scramble for power



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By Jacob Atkins

Demand for big-ticket, syndicated letters of credit is soaring in the US, those involved in the transactions have said, as utility companies and power grid operators seek credit protection for huge power supply contracts inked with data centre developers.

Banks have been cashing in on demand from electricity suppliers that insist developers issue standby letters of credit (LCs) that can be drawn if data centre projects fall over or don't ultimately use the promised amount of electricity.

Publicly available filings from US state regulators show that contracts between utilities and data centre developers typically require the latter to put up collateral in the form of parent company guarantees for well-rated companies, or LCs or cash if the credit rating is below a certain threshold.

Out of 109 regulatory filings tracked by energy market intelligence platform Halcyon that include collateral, 67 mention a letter of credit, according to data shared with **GTR**. Another 12 mention “standby letter”, shorthand for a standby LC. Halcyon said most of the filings they track became active in the last two years.

Investor-owned US electricity utilities are planning around US\$1.4tn in capital spending over the next five years, mainly to fund the huge power generation and infrastructure needs of data centres to power AI, bitcoin mining and other computing needs, according to PowerLines, a non-profit focused on utility regulation.

The data centre pipeline in the US includes 1,254 planned facilities, according to market intelligence provider Cleanview. US\$178.5bn worth of financing deals across public and private markets were struck last year to fund the centres, *Bloomberg* reported.

Obtaining LCs has become a competitive advantage in the scramble to secure electricity supplies to energy-hungry data centres, bankers said.

There has been a “structural shift toward greater use of LCs to support grid interconnection and power procurement obligations” said Trevor Hope, a director in TD Securities’ trade and working capital unit.

Arnaud Stevens, head of global trade, Americas, at French lender Natixis, said: “Power access has become one of the defining constraints for hyperscale growth. If you want to scale large, sophisticated data centres, you need to secure your access to power.”

However, many large data centre projects are stuck in lengthy “interconnection queues”, waiting to be plugged into state electricity grids. To get connected, infrastructure such as transmission lines and substations may need to be upgraded or installed to accommodate the vast power needs.

Electricity suppliers and regional bodies that oversee electricity grids “want to make sure that there is enough or significant credit support in front of that if [data centre developers] are unable to offtake the large volumes that they have committed to, or they are unable to connect the data centres to the grid, because this is definitely now, in the US, the number one issue”, Stevens said.

“There is a growing concern, especially in the US, for the grid or the utility companies, that you have to spend a lot of money and you also have to allocate pretty sizeable power volumes to the data centre developers,” he added.

While smaller deals are done on a bilateral basis, the hefty value of power purchase agreements or grid connection deals necessary for data centres has pushed banks to club together on syndicated LCs.

In one of the few publicly disclosed deals, US data centre developer Switch said in April it had closed a US\$2.6bn syndicated, uncommitted performance letter of credit facility, which it described

as a “first of its kind in the data centre industry”. Earlier this month, the company upsized the deal to US\$3.5bn.

“The facility is designed to provide performance letters of credit to utilities and other counterparties in support of power procurement, energy generation and transmission requirements tied to Switch’s campus development pipeline, giving counterparties additional assurance as projects advance,” Switch said in a statement.

Natixis and BBVA led and structured the LC facility, which was syndicated out to a group of lenders including BNP Paribas, Citi and Société Générale in a several but not joint structure.

Earlier this month, Natixis also arranged a three-bank global LC facility for Yondr, which plans to use the instruments to help secure power for projects in the US and Europe.

### **Boom tipped to continue**

Standalone LC facilities look set to become more common as collateral needs outgrow the revolving credit facilities in which the instruments have typically been included.

“LC requirements are expected to remain a core feature of data centre power procurement and interconnection structures over the long term,” said Hope of TD Securities.

Paul M Roder, a partner at law firm Moses & Singer, said he has “seen a significant uptick in demand for standbys” over the past year. “The pipeline is still robust. There’s a lot going on in the space, and for the near future, we don’t see that stopping.”

Roder said most of the deals support either a grid connection or power purchase deal, but there has also been higher demand for performance guarantees to support the construction of infrastructure such as substations and transmission lines.

Most of the deals use evergreen LCs, which are automatically renewed on expiry, typically at one-year intervals. Many of the agreements are bespoke, but the drawing conditions are usually attached to the insolvency of the applicant or a default on the underlying contract, Roder said.

Documentary credits have also been used to back supply agreements for the vast numbers of semiconductor chips required for data centres.

“We’re doing a number of facilities where major chip purchasers are going to the major suppliers for multi-year agreements to procure the computer chips needed for all of these servers in these data centres, and they’re using letters of credit to support their purchase obligations under those supply contracts,” Roder said.

### **Community angst**

The data centre building spree is continuing despite sporadic anxiety among investors about the longevity of the AI boom, partly fuelled by worries over vast spending by some of the sector's biggest companies.

The complexes also face growing hostility from some local communities, upset by their noise, energy appetite and the small number of workers required to operate them. In some cases, utilities have faced pushback from taxpayers and state regulators over the collateral requirements.

DTE Energy, which is building three energy storage projects to supply a 1,383 megawatt data centre being developed by Oracle in Michigan, was warned by the state's utilities regulator that the government would not foot any of its costs if Oracle's collateral fell short, public filings show.

In the case of Oracle, as well as a Google data centre also set to be supplied by DTE, most of the collateral conditions in the publicly available versions of the contracts are redacted.

"I think we should at least know what that collateral is if it's being offered... if payments can't be made, I think the public needs to know that," one resident told a public hearing on the Oracle-DTE deal last December, according to a transcript.

Michigan's attorney-general has filed an appeal against the utility commission's initial approval of the contract, which is pending.

Tags: [Artificial Intelligence \(AI\)](#), [Core trade finance](#), [data centres](#), [letters of credit \(LCs\)](#), [Moses & Singer](#), [Natixis](#), [Oracle](#), [standby letters of credit \(SBLCs\)](#), [TD Securities](#)

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