Employers Must Meet Federal Prevailing Wage and Apprenticeship Requirements to Earn New Tax Credits and Deductions

Insights
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Federal officials recently outlined prevailing wage and apprenticeship requirements that projects need to adopt if they want to take advantage of the enhanced tax credits and deductions created by the Inflation Reduction Act (IRA). The Internal Revenue Service published Notice 2022-61 on November 30 which, along with subsequent guidance from the United States Department of Labor, Wage and Hour Division, makes clear that businesses—even those who are not federal contractors—must implement the prevailing wage requirements of the Davis Bacon Act (DBA), as well as the DBA's apprenticeship requirements, to obtain the maximum in tax benefits. What do you as an employer need to know about these requirements in order to put yourself in the best position to benefit?

What is the Inflation Reduction Act?

The IRA was signed into law by President Biden on August 16, 2022. In an effort to boost investment in clean energy, the IRA modifies and enlarges certain tax credits and deductions for projects to build and install renewable energy and energy-efficiency "green" technology. Such projects include those for renewable energy production, carbon oxide sequestration, zero-emission nuclear power, investments in solar energy, and energy-efficient commercial buildings. However, to be eligible for the tax credits, and to meet the IRA's secondary goal of creating good-paying jobs, laborers and mechanics must be paid a guaranteed wage of at least the applicable prevailing wage and fringe benefits for all hours worked performing construction, alteration, or repair, on the site of a qualified facility.

The prevailing wage *and* apprenticeship provisions apply to the Alternative Fuel Refueling Property Credit, Production Tax Credit, Credit for the Carbon Oxide Sequestration, Credit for the Production of Clean Hydrogen, Clean Fuel Production Credit, Investment Tax Credit, Advanced Energy Project Credit, and Energy Efficient Commercial Buildings Deduction. Only the prevailing wage provisions apply to the New Energy Efficient Home Credit and Zero-Emission Nuclear Power Production Credit.

What are the Prevailing Wage Requirements?

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Federal contractors are all too familiar with the prevailing wage requirements under the federal DBA. The DBA requires contractors and subcontractors to pay the prevailing wage rate and fringe benefits to all employees who are working on federally funded or assisted contracts in excess of $2,000 for the construction, alteration, or repair of public buildings or public works.

For purposes of the IRA, any taxpayer seeking to realize the tax credits must ensure that laborers and mechanics working on clean energy construction projects are paid wages and fringe benefits consistent with the DBA.

For each locality and type of construction project, the federal government has set forth a prevailing wage rate, which is the minimum rate of pay for a specific job classification. The rate of pay may also be subject to enhancements for overtime, work performed on Saturdays and/or Sundays, and work performed on holidays.

Additionally, there are certain fringe benefits that are required to be paid to employees. Fringe benefits are additional cash compensation, set at an hourly rate, that employers must provide to cover costs such as health insurance benefits. Employers can provide fringe benefits through a combination of cash wages and contributions to employer-provided bona fide fringe benefit plans.

What are the Apprenticeship Requirements?

The IRA is unique in that it sets forth certain requirements for a taxpayer to be eligible for tax credits, including the employment of apprentices on clean energy construction projects. These requirements encourage individuals to learn trades by enhancing training for certain well-paying construction jobs. While the DBA does not require federal contractors to do the same, it permits the payment of reduced prevailing wage and fringe benefit rates for apprentices.

An apprentice is an individual employed and individually registered in a bona fide apprenticeship program. To be eligible for the increased tax credits or deductions, contractors must employ a minimum number of apprentices on the job and a certain percentage of the total labor hours of the construction, alteration, or repair work with respect to the facility must be performed by qualified apprentices.

Specifically, any taxpayer, contractor, or subcontractor who employs four or more people to perform construction, alteration, or repair work with respect to the construction of a qualified facility must employ one or more qualified apprentices to perform the work. Employers will also have to comply with any journeyman to apprentice ratios set by state or local law. The apprentices must be affiliated with an apprenticeship program that is registered with the Department of Labor's Employment and Training Administration or similar state agency.

With respect to the percentage of total labor hours that must be performed by qualified apprentices, the percentage depends on when the work began. For the construction of a qualified facility that begins before January 1, 2023, 10% of the total labor hours must be performed by qualified

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apprentices. For construction that begins after December 31, 2022 and before January 1, 2024, 12% of the total labor hours must be performed by qualified apprentices. For construction that begins after December 31, 2023, 15% of the total labor hours must be performed by qualified apprentices.

How Do We Determine When the Work Begins?

There are two methods that can be used to determine when the construction work begins: the Physical Work Test and the Five Percent Safe Harbor.

- Under the Physical Work Test, construction of a qualified facility is considered to begin when physical work of a significant nature begins, provided there is a continuous program of construction. This can include preliminary activities, such as planning or designing, securing financing, exploring, researching, obtaining permits, licensing, conducting surveys, environmental and engineering studies, or clearing a site and may include on-site or off-site work.
- Under the Five Percent Safe Harbor, construction is considered to begin if the taxpayer pays or incurs 5% or more of the total cost of the facility and, thereafter, makes continuous efforts to advance towards completion of the facility.

What are the Recordkeeping Requirements?

Similar to the DBA, recordkeeping is essential to ensuring compliance with the IRA. Any person subject to income tax is required to keep permanent books of accounts or records, including inventories, as are sufficient to establish the amount of gross income, deductions, credits, or other matters required to be shown in any return of such tax. Records must be maintained so long as the contents may become material in the administration of any internal revenue law.

What Should Employers Do Now?

Employers, including contractors and subcontractors, involved in the construction, alteration, or repair of a clean energy facility must ensure compliance with the IRA's wage and hour requirements in order to take advantage of the increased tax credits and deductions. This means ensuring workers are paid the applicable prevailing wage rates, apprentices are hired to perform some of the work if there are four or more workers on the project, and that apprentices are performing the minimum percentage of work required.

Employers who expect to be awarded contracts for covered projects should look to see what registered apprenticeship programs exist in their area, or consider evaluating whether they can set up their own registered apprenticeship program.

Conclusion

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Fisher Phillips will continue to monitor this area and provide updates as needed. Please ensure you are subscribed to Fisher Phillips' Insight system to gather the most up-to-date information. If you have questions, please contact your Fisher Phillips attorney, the authors of this Insight, or any attorney in our Wage and Hour Practice Group.

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