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KPMG report: Analysis and observations about prevailing wage and apprenticeship requirements

The IRS on November 29, 2022, issued **Notice 2022-61** [PDF 237 KB] providing much-needed guidance on the prevailing wage and apprenticeship requirements introduced in H.R. 5376 (commonly called the "Inflation Reduction Act of 2022" (IRA)).

Treasury plans to issue additional proposed regulations with respect to these requirements in the coming months. These requirements must be satisfied in order to qualify for the increased credit rates and deduction amounts available for the clean energy and climate tax incentives in the IRA.

Generally, but with exceptions described in more detail below, these prevailing wage and apprenticeship requirements apply to qualifying facilities, projects, property, or equipment for which construction begins 60 days or more after Treasury publishes guidance. This notice serves as the published guidance establishing the 60-day period described in those provisions. As such, these requirements will affect facilities for which construction begins, or certain properties for which installation begins, on or after January 29, 2023.

Both the prevailing wage and apprenticeship requirements apply to the following tax incentives:

- Section 48 Renewable energy property investment tax credit
- Section 48E Clean electricity investment credit
- Section 45 Renewable energy production tax credit
- Section 45Y Clean electricity production credit
- Section 45Q Credit for carbon oxide sequestration
- Section 45V Credit for production of clean hydrogen
- Section 45Z Clean fuel production credit
- Section 48C Advanced energy project credit
- Section 30C Alternative fuel refueling property credit
- Section 179D Energy efficient commercial buildings deduction

The prevailing wage requirements also apply to the following tax incentives:

- Section 45L New energy efficient home credit
- Section 45U Zero-emission nuclear power production credit

KPMG observation

As described above, the prevailing wage and apprenticeship requirements apply to the section 48C advanced energy project investment credit such that taxpayers are only eligible for the 30% credit rate if those requirements are satisfied. It should be noted, however, that the 60-day transition rule does not apply in the case of section 48C.

The effective date for the IRA amendments to section 48C provide that the changes "shall take effect on January 1, 2023." This language would appear to make the prevailing wage and apprenticeship requirements applicable starting on January 1, 2023, and therefore inapplicable to work occurring on projects before that date.

Similarly, while the prevailing wage and apprenticeship requirements apply in order to claim the higher rates for the section 45Z clean fuel production tax credits, the 60-day transition rule does not apply. Section 45Z does, however, clearly articulate when the requirements begin to apply. Specifically, section 45Z states that in the case of facilities placed in service prior to January 2025, the prevailing wage and apprenticeship requirements only apply to alterations and repairs and only with respect to tax years starting after 2024 for which the credit is allowed.

Guidance with respect to prevailing wage rate requirements

A prevailing wage is the combination of the basic hourly wage rate, and any fringe benefits rate, paid to workers in a specific classification of laborer or mechanic in the area where construction, alteration, or repair is performed, as determined by the Secretary of Labor in accordance with subchapter IV of chapter 31 of title 40 of the United States Code, also known as the Davis-Bacon Act.

A taxpayer will satisfy the prevailing wage rate requirement if:

- The taxpayer satisfies the prevailing wage rate requirements with respect to any laborer or mechanic employed in the construction, alteration, or repair of a facility, property, project, or equipment by the taxpayer or any contractor or subcontractor of the taxpayer; and
- The *taxpayer* must maintain and preserve sufficient records, including books of account or records for work performed by contractors or subcontractors of the taxpayer, to establish that such laborers and mechanics were paid wages not less than such prevailing rates, and shall be retained so long as the contents thereof may become material in the administration of any internal revenue law.

The term "construction, alteration or repair" has the same meaning as "construction, prosecution, completion, or repair" in 29 CFR § 5.2(j), which is defined as all types of work done on a particular building or work at the site thereof, including work at a facility which is deemed a part of the site of the work (including altering, remodeling, and installation; painting and decorating; the manufacturing or furnishing of materials, articles, supplies or equipment on the site of the work; and transportation between the taxpayer's facility and an off-site facility dedicated to the construction of the taxpayer's facility and deemed part of the site of the work).

The prevailing wage rates are set based on the particular classification of laborers or mechanics for the type of construction and the geographic area in which the facility is located. The Department of Labor determines the applicable rates and issues them at **www.sam.gov**.

If the Secretary of Labor has not published a prevailing wage determination for the geographic area or job type, the guidance provides methodology for taxpayers to request a wage determination, or wage rates, for unlisted classifications. Specifically, the taxpayer must contact the Department of Labor, Wage and Hour Division via email at ***IRAprevailingwage@dol.gov*** and provide the Department of Labor Wage and Hour Division with the type of facility, facility location, proposed labor classifications, proposed prevailing wage rates, job descriptions and duties, and any rationale for the proposed classifications. The Department of Labor, Wage and Hour Division will review and notify the taxpayer of the wage rates by which to comply.

KPMG observation

This guidance provides some much-needed clarity with respect to the procedures and satisfaction of the prevailing wage rate requirement. However, there are still outstanding questions that will require further guidance.

First, additional clarity may be required with respect to the procedure provided in the guidance allowing taxpayers to request a wage determination from the Department of Labor. The guidance identifies the "taxpayer" as the person who makes the request but leaves unclear whether contractors or sub-contractors can make inquiries on behalf of the taxpayer. Additionally, the guidance is silent on how long responses to these requests may take whether these requested wages will become publicly available in the **www.sam.gov** system, or elsewhere once they are reviewed and issued to respective taxpayers.

One of the burning questions to date had been how taxpayers will document compliance with these requirements. The guidance indicates that the taxpayer bears the burden to maintain and preserve sufficient records. The first example provided in the notice indicates that a taxpayer satisfied the Prevailing Wage Rate Requirements by maintaining sufficient records to establish in that case that the taxpayer, the contractor, and the subcontractor paid wages not less than such prevailing wage rates. The example explains that such records include but are not limited to, identifying the applicable wage determination, the laborers and mechanics who performed construction work on the facility, the classifications of work they performed, their hours worked in each classification, and the wage rates paid for the work. Additionally, as stated in the FAQs issued by the Department of Labor, if a worker performs work in more than one labor classification, the taxpayer, contractor, and subcontractor should keep an accurate record of the time spent in each classification and pay the correct rate for the time spent in each classification. These additional details on documentation are helpful but it may still be difficult for taxpayers to obtain this level of information from contractors and subcontractors, and the guidance does not provide exceptions or alternatives for situations where documents may not be available or accessible. It may be necessary for taxpayers to start contractually requiring that this information be recorded, maintained and provided to the taxpayer as a part of negotiations and agreements with contractors and subcontractors.

Lastly, Section 45(b)(7)(A) provides that to meet the prevailing wage requirements with respect to any qualified facility, a taxpayer must ensure that any laborers and mechanics employed by the taxpayer or any contractor or subcontractor in: (1) the construction of such facility, and (2) the alteration or repair of such facility (with respect to any tax year, for any portion of such tax year that is within the 10-year period beginning on the date the qualified facility is originally placed in service). The guidance provides that the term "alteration or repair" has the same meaning as "construction, prosecution, completion, or repair" in 29 CFR § 5.2(j). This definition may not logically apply to many of the projects incentivized by the relevant tax credits. Additional guidance may be necessary to understand what is considered an alteration or repair in these contexts, as opposed to work that should be considered regular operations and maintenance.

Guidance with respect to apprenticeship requirements

The apprenticeship requirement requires taxpayers to provide that no fewer than the applicable percentage of total labor hours are performed by qualified apprentices. The applicable percentage for purposes of this requirement would be 10% for projects for which construction begins in 2022. This rate would be increased to 12.5% in 2023, and 15% thereafter.

The guidance provides that a taxpayer satisfies the apprenticeship requirements if the taxpayer:

- Satisfies the apprenticeship labor hour requirements, subject to any applicable apprenticeship ratio requirements
- Satisfies the apprenticeship participation requirements
- Complies with certain recordkeeping requirements including maintaining books of account or records for contractors or subcontractors of the taxpayer, as applicable, in sufficient form to establish that the requirements have been satisfied

Further, under the Good Faith Effort Exception, the taxpayer will be considered to have made a good faith effort in requesting qualified apprentices if the taxpayer requests qualified apprentices from a registered apprenticeship program in accordance with usual and customary business practices for registered apprenticeship programs in its respective industry.

The guidance goes on to further clarify and define journeyworker, apprentice-to-journeyworker ratio, and State Apprenticeship Agency for instances where the apprentice-to-journeyworker ratios may apply. Taxpayers, contractors, or subcontractors can check whether a state has been authorized by the Department of Labor to approve **apprenticeship programs**.

KPMG observation

Similar to the wage rate requirement documentation, the guidance indicates that the burden of documentation falls on the taxpayer, which must maintain and preserve sufficient records. Thus, it could be difficult for taxpayers to obtain this level of information from contractors and subcontractors. It may be necessary for taxpayers to start contractually requiring that this information be recorded, maintained, and provided to the taxpayer as a part of the negotiations and agreements with contractors and subcontractors.

The guidance attempts to clarify the Good Faith Effort Exception, but additional clarity may be needed to offer taxpayers comfort that they comply with this exception. Specifically, the statute provides that a taxpayer is deemed to have satisfied the apprenticeship requirements if the taxpayer has requested qualified apprentices from a registered apprenticeship program and either such request has been denied, provided that such denial is not the result of a refusal by the taxpayer or any contractors or subcontractors to comply with the established standards and requirements of the registered apprenticeship program, or the registered apprenticeship program fails to respond to such request within five business days after receiving such request. The guidance does not clarify whether the Good Faith Effort Exception is met at the earlier of receipt of denial or the passage of five business days without reply. It is also unclear how the taxpayer should properly document the passage of five business days without reply to comply.

Determining when construction or installation begins

For taxpayers that begin construction within the 60-day safe harbor period, the prevailing wage and apprenticeship requirements are not required to be satisfied to achieve the "bonus rates" available for the various incentives, subject to exceptions explained above for section 48C and 45Z. Therefore, the determination of when the project has begun construction is important for the purposes of applying the prevailing wage and apprenticeship requirements.

To determine when construction begins for purposes of Sections 30C, 45V, 45Y, and 48E, this guidance refers to prior issued guidance under Notice 2013–29 regarding the beginning of construction. Specifically, construction begins with by starting physical work of a significant nature or paying or incurring 5% of the total project costs.

Similar principles to those under section 3 of Notice 2016–31 regarding the Continuity Safe Harbor also apply for purposes of Sections 30C, 45V, 45Y, and 48E. Taxpayers may rely on the Continuity Safe Harbor provided the facility is placed in service no more than four calendar years after the calendar year during which construction began.

For purposes of Sections 45, 45Q, and 48, the IRS Notices will continue to apply under each respective Code section, including application of the Physical Work Test and 5% Safe Harbor, and the rules regarding the Continuity Requirement and Continuity Safe Harbors.

Finally, the guidance provides that for purposes of the energy efficient commercial building deduction under section 179D, the IRS will accept that installation has begun if a taxpayer generally satisfies principles similar to the begin construction rules in Notice 2013-29.

KPMG observation

Additional clarity may be needed in order to apply the begin construction rules to a clean hydrogen production facility for purposes of section 45V. The definition of "facility" under section 45V is an area in need of guidance and absent that definition it may be hard to determine what physical work or which costs may trigger the beginning of construction.

Conclusion

While open issues remain, this guidance, and the speed at which it was issued, is a positive development in understanding the various new tax credit rules enacted under the IRA. Forthcoming proposed regulations on these requirements will hopefully offer additional clarity on these issues.

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