

Clean Energy Tax Credits' Wage, Apprentice Rules: Key Points

By **Omar Samji, Gillian Emmett Moldowan and Judy Little** (February 17, 2023)

On Aug. 16, 2022, President Joe Biden signed the Inflation Reduction Act, which included provisions for clean energy tax and climate tax incentive credits for taxpayers — generally builders, developers and owners of clean energy facilities — requiring that prevailing wages be paid to employees, and that registered apprentices are utilized for the construction of energy efficient commercial and residential buildings, electric vehicle charging infrastructure, and other clean energy projects.



Omar Samji

The tax incentives under the IRA are structured in two tiers: a base rate and a higher rate, also known as a bonus, that is five times the base rate when certain requirements are met.

The higher bonus rate will generally only be available to taxpayers with respect to a qualified solar, wind, hydrogen, or carbon capture facility, property, project, or equipment where the taxpayer begins construction on such facility on or after Jan. 29 of this year, if the taxpayer meets the prevailing wage and apprenticeship requirements under the IRA.



Gillian Emmett
Moldowan

A taxpayer who doesn't comply with these requirements can still benefit from the higher tax credits, if the taxpayer can demonstrate that they began construction on a facility before Jan. 29.

It is important for taxpayers to understand in advance how to comply with the complicated prevailing wage and apprentice requirements, and to ensure they have compliance programs in place in order to take advantage of the bonus rate tax incentives provided by the IRA. The learning curve will be more difficult for taxpayers unfamiliar with government sponsored apprenticeship programs and prevailing wages.



Judy Little

On Nov. 30, 2022, the Internal Revenue Service published a notice titled "Prevailing Wage and Apprenticeship Initial Guidance Under Section 45(b)(6)(B)(ii) and Other Substantially Similar Provisions" to provide guidance on the specific labor standards that taxpayers must meet to qualify for the enhanced clean energy and climate tax incentives under the IRA.

The notice also provides critical guidance on the meaning of "begin construction" for those taxpayers seeking to establish that they are not subject to the wage and apprenticeship requirements for facilities that began construction before the Jan. 29 deadline. There are two methods that may be used to establish the beginning of construction: the physical work test and the 5% safe harbor.

Under the physical work test, construction begins when physical work of a significant nature begins. Under the 5% safe harbor, construction has begun if the facility has paid or incurred 5% or more of the total cost of construction.

Applicability of the Wage and Apprenticeship Requirements

The wage and apprenticeship requirements apply to the tax credits enacted or amended by the IRA as follows:

Credit	IRC Section	Prevailing Wage Requirement	Apprenticeship Requirement
Renewable Energy Production Credit*	45	Yes	Yes
Renewable Energy Investment Credit*	48	Yes	Yes
Clean Electricity Production Credit*	45Y	Yes	Yes
Clean Electricity Investment Credit*	48E	Yes	Yes
Qualifying Advanced Energy Project Credit	48C	Yes	Yes
Carbon Oxide Sequestration Credit	45Q	Yes	Yes
Clean Hydrogen Production Credit	45V	Yes	Yes
Clean Fuel Production Credit	45Z	Yes	Yes
Alternative Fuel Vehicle Refueling Property Credit	30C	Yes	Yes
Energy Efficient Commercial Buildings Deduction	179D	Yes	Yes
Zero-Emission Nuclear Power Production Credit	45U	Yes	No
New Energy Efficient Home Credit	45L	Yes	No
Advanced Manufacturing Production Credit	45X	No	No

* The credits under Sections 45, 48, 45Y and 48E are not subject to the wage and apprenticeship requirements if the applicable facility has a maximum net output of less than one megawatt.

Specifics of the Wage and Apprenticeship Requirements

Prevailing Wage Requirements

The IRA requires taxpayers seeking a credit to provide laborers and mechanics employed in the construction, alteration or repair of a facility with wages at rates not less than the prevailing rates of similar employees for similar type of work, in the locality in which such facility is located, as determined by the secretary of labor.

The U.S. Department of Labor's Wage and Hour Division posts labor classifications and their prevailing wage rates in wage determinations on <http://www.sam.gov>. If there is no published prevailing wage determination for a particular geographic area and type of construction, the taxpayer must proactively request a wage rate or wage determination, by contacting the Department of Labor's Wage and Hour Division via email, at IRAPrevailingWage@dol.gov.

The taxpayer must also maintain sufficient records to establish that its laborers and mechanics were paid wages not less than such prevailing rates.

Such records could include, but are not limited to, documentation 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.[1]

Apprenticeship Requirements

The IRA provides that developers of facilities seeking a credit are required to use apprentices from government-registered apprenticeship programs for construction, alteration and repair work. The taxpayers need to satisfy two sets of requirements regarding apprenticeships.

Under the apprenticeship labor hour requirement, these apprentices must account for 12.5% of the total labor hours of the project in 2023, and 15% in 2024 and thereafter. This requirement is subject to prescribed journeyman-to-apprentice ratios.

In addition, under the apprenticeship participation requirement, each taxpayer, contractor and subcontractor employing four or more individuals for a project must employ at least one qualified apprentice from a government-registered apprenticeship program — meaning a program registered under the National Apprenticeship Act or by the DOL.

Finally, taxpayers must maintain sufficient records to establish that these quotas have been satisfied for the duration of the project.[2]

The taxpayers may be able to rely on the good faith effort exception included in the IRA to comply with the apprenticeship requirements. Under this exception, a taxpayer is deemed to have satisfied the apprenticeship requirements with respect to a facility if the taxpayer has requested qualified apprentices from a registered apprenticeship program and at least one of the following has occurred:

1. Such request has been denied, but not due to the taxpayer's failure to comply with the program standards; or

2. The registered apprenticeship program fails to respond to such request within five business days after the date on which the program received such request.

It is important that the taxpayer maintain records that establish the request was made, and the program's denial or nonresponse to the request.

Meaning of "Begin Construction"

As noted above, taxpayers that began construction prior to Jan. 29 may still benefit from the higher tax credit rates without having to comply with the wage and apprenticeship rules. Taxpayers may use the following methods to establish that construction began before the deadline:

1. Starting physical work of a significant nature — the physical work test; or
2. Paying or incurring 5% or more of the total cost of the facility — the 5% safe harbor.

The beginning of construction standard is not new for taxpayers. For instance, the IRS has based the availability of tax credits for solar, wind and carbon capture projects on the year in which construction of a project began.

The IRS previously issued a number of project-type specific notices for such projects under IRS Sections 45, 45Q and 48 that explain how a facility could begin construction in the context of these projects. In the recent notice, the IRS refers to these previous notices for determining when construction commences under IRS Sections 30C, 45V, 45Y, and 48E, and when installation begins under Section 179D.

Physical Work Test

Under the physical work test, construction begins when physical work of a significant nature begins, as long as construction, or efforts toward construction, are continuous. This test focuses on the nature of the work performed, not the amount of work or the costs incurred to date.

There is no set threshold of work required to satisfy this test. Physical work does not include preliminary activities — e.g., planning or designing, securing financing, exploring, researching, obtaining permits, licensing, conducting surveys, preparing environmental or engineering studies, or clearing a site.

Work performed by or for a taxpayer by other persons under a binding written contract can be considered when determining whether construction has begun. Both on-site and off-site work may be taken into account for purposes of demonstrating that physical work of a significant nature has begun.

Physical work of a significant nature does not include work to produce property that is either in existing inventory or is normally held in inventory by a vendor.

5% Safe Harbor

Under the 5% safe harbor, construction is considered to have begun on a facility if:

1. A taxpayer pays or incurs 5% or more of the total cost of such facility; and
2. The taxpayer continues to advance toward completion of such facility.

All costs properly included in the depreciable basis of the facility are considered in determining whether the 5% safe harbor has been met. For property that is produced for the taxpayer by another person under a binding written contract with the taxpayer, property costs incurred by the other person prior to receipt of the property by the taxpayer are deemed incurred by the taxpayer.

Key Takeaways

For taxpayers that have begun, or expect to begin, construction on facilities on or after Jan. 29, and that wish to benefit from the heightened tax incentives, it is important to be aware of these new wage and apprenticeship regulations, and ensure compliance programs are in place.

Establishing compliance programs may require significant planning and legal review, particularly for taxpayers that do not have experience with the prevailing wage rates and government-registered apprenticeship systems. For those taxpayers seeking to establish that they began construction on a facility before Jan. 29, it is critical to be in a position to provide evidence that these projects were started in advance of the deadline.

We expect the U.S. Department of the Treasury and the IRS to issue additional guidance in the coming months to further clarify the operation of the new wage and apprenticeship requirements.

Omar Samji is a partner and head of the global energy innovation team at Shearman & Sterling LLP.

Gillian Emmett Moldowan is a partner at the firm.

Judy Little is counsel at the firm.

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[1] If a taxpayer does not comply with the prevailing wage requirement, the taxpayer can become eligible to receive a credit if the taxpayer corrects the noncompliance by providing back pay to employees, as applicable, and paying a specified penalty to the Department of Labor.

[2] As with the prevailing wage requirement, if a taxpayer does not comply with the apprenticeship requirement, the taxpayer can become eligible to receive a credit if the taxpayer corrects the noncompliance by paying a specified penalty to the Department of Labor.