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Tax Update July 2, 2024

IRS and Treasury Issue Final Regulations on Prevailing Wage and Apprenticeship Requirements under the IRA

The Final Regulations generally apply to qualified facilities placed in service in tax years ending after June 25, 2024.

On June 25, 2024, the IRS and Treasury published final Treasury regulations (the "Final Regulations") on the prevailing wage and apprenticeship requirements (the "PWA Requirements") that taxpayers must[1] satisfy to receive the full amount[2] of certain tax credits provided for in the Inflation Reduction Act of 2022 (the "IRA").[3] The Final Regulations build upon the proposed Treasury regulations (the "Proposed Regulations") issued on August 30, 2023 (our earlier alert on the Proposed Regulations is available here)

The Final Regulations generally apply to qualified facilities placed in service in tax years ending after June 25, 2024. For facilities that either (1) began construction on or after January 29, 2023 and before June 25, 2024 or (2) were placed in service in taxable years ending on or before June

25, 2024, taxpayers may choose to apply either the Final Regulations or the Proposed Regulations, as long as the chosen guidance is applied consistently.[4]

Background

At a high level, the "prevailing wage requirement" requires that all laborers and mechanics employed by a taxpayer (or a contractor or subcontractor) claiming an applicable credit[5] be paid wages for construction, alteration, or repair of the applicable facility that are not less than the "prevailing" wage for the type of work performed. The "apprenticeship requirement" generally requires a certain percentage of labor hours be performed by apprentices working under the supervision of experienced laborers. Our prior alert (which is available here) summarizes these requirements in greater detail.

Key Changes to Prevailing Wage Requirements

The Final Regulations provide several crucial clarifications to earlier guidance (including the Proposed Regulations) relating to the prevailing wage requirement.

Timing of Wage Determination

Taxpayers generally must consult guidance published by the Wage and Hour Division of the Department of Labor to determine prevailing wages. Unlike the Proposed Regulations, which would have set the applicable wage rate as the one in effect at the beginning of construction, the Final Regulations stipulate that the applicable wage rate is the one in effect when a contract for the construction, alteration, or repair of a facility is executed. Only if there is no contract is the timing of the wage determination determined on when construction begins. If a taxpayer enters into a generalized contract for alteration or repair work (*i.e.*, a contract that does not call for any specific work) for an indefinite period of time, the applicable wage rates must be refreshed on an annual basis, so taxpayers cannot lock in lower wages (or be locked into higher wages) through vague, long-term contracts.

Curing Failures to Pay Appropriate Wages

In some instances, taxpayers seeking to fix failures to pay appropriate wages can avoid penalties if they self-correct. The Final Regulations modify the Proposed Regulations by specifying that self-correction must be made by the last day of the first month following the end of the calendar quarter in which the failure occurred (as opposed to the Proposed Regulations, which would have required the correction payment to be made within 30 days after the taxpayer became aware of the error or the date on which the increased credit was claimed).

Additionally, the Final Regulations add a further clarification to these correction payments rules: if a former worker cannot be found, a taxpayer will be deemed to make a correction payment if it

complies with state unclaimed property laws and all federal and state withholding information reporting requirements. This provision addresses the concern of some taxpayers, expressed after the issuance of the Proposed Regulations, that correction payments might not be possible if an underpaid worker could not be found.[6]

Key Changes to Apprenticeship Requirements

The Final Regulations also include important clarifications related to the apprenticeship requirements, including those highlighted below.

Applicability After Facility is Placed in Service

Under the Proposed Regulations, it was unclear whether the apprenticeship requirements continued to apply after a particular facility was placed in service. The Final Regulations make clear that the apprenticeship requirements cease to apply to alteration or repair work once a facility is placed in service.

Threshold Number of Construction Employees

The Final Regulations confirm that the apprenticeship requirements apply only to taxpayers, contractors, or subcontractors who employ four or more individuals to perform construction, alteration, or repair work in connection with the construction of a qualified facility. The Final Regulations clarify that the four-employee threshold applies over the course of the construction, regardless of whether the employees are employed at the same location or at the same time, increasing the likelihood that the apprenticeship requirements will apply to small contractors or subcontractors.[7]

Requests to Registered Apprenticeship Programs

The Proposed Regulations provided that if a taxpayer made a request for apprentices to a registered apprenticeship program and received a denial or nonresponse, the taxpayer must submit additional requests every 120 days in order to meet the good faith effort exception (to the extent applicable, this exception excuses a taxpayer from complying with the apprenticeship requirements). In response to comments, the Final Regulations relaxed this requirement to provide that the taxpayer only needs to submit additional requests 365 days (or, if applicable, 366 days) after the denial of a previous request to continue to satisfy the good faith effort exception.

Key Changes to Recordkeeping Requirements

The Final Regulations include some important adjustments to the recordkeeping requirements for the PWA Requirements.

Personal Identifying Information

The Proposed Regulations would have required the collection of sensitive personal identifying information, including social security numbers, with respect to the employees of the taxpayer and the employees of contractors or subcontractors. The Final Regulations alter this requirement to provide that only the last four digits of an employee's social security number must be collected.

Options for Compliance

The Final Regulations provide three ways to comply with the recordkeeping requirements:

1. Taxpayers may collect and physically retain relevant records from contractors and subcontractors, with certain personally identifiable information redacted so long as unredacted information is made available to the IRS upon request.
2. Contractors and subcontractors may provide relevant records to a third-party vendor to physically retain on behalf of the taxpayer, with certain sensitive information redacted so long as unredacted information is made available to the IRS upon request.
3. Taxpayers, contractors, and subcontractors may each physically retain the relevant unredacted records for their own employees, and those unredacted records must be made available to the IRS upon request.

[1] Compliance with the PWA Requirements is not required for facilities (i) that have a maximum net output or storage capacity of less than one megawatt or (ii) the construction of which began before January 29, 2023.

[2] Technically, the baseline tax credit is multiplied by five if the PWA Requirements are met, resulting in a tax credit amount that traditionally has been considered the full amount of the federal income tax credits that may be claimed in respect of clean energy technologies. This full credit amount also can be increased by so-called adders, such as the domestic content adder and the energy community adder. Please see our prior alerts on these adders, which can be found here, here, and here, respectively.

[3] As was the case with the so-called Tax Cuts and Jobs Act, the Senate's reconciliation rules prevented Senators from changing the Act's name, and the formal name of the so-called Inflation Reduction Act is actually "An Act to provide for reconciliation pursuant to title II of S. Con. Res. 14." In addition to tax credit guidance, the Final Regulations also include guidance regarding the

PWA Requirements under section 179D, which provides a deduction for the cost of energy efficient commercial building property placed in service during the taxable year.

[4] Unless indicated otherwise, all "section" references are to the Internal Revenue Code of 1986, as amended.

[5] Tax credits with a prevailing wage or apprenticeship requirement include those credits provided for under sections 30C, 45, 45L, 45Q, 45U, 45V, 45Y, 45Z, 48, 48C, and 48E.

[6] The preamble to the Proposed Regulations stated, "[t]he Treasury Department and the IRS expect that taxpayers will be able to establish correction payments even when a former laborer or mechanic cannot be located."

[7] The Final Regulations clarify that the hours devoted to the performance of construction, alteration, or repair work by any qualified apprentice in excess of the applicable ratio requirement will be counted towards the total labor hours but will not be counted as hours performed by qualified apprentices for purposes of the labor hours requirement applicable to qualified apprentices.

The following Gibson Dunn lawyers prepared this update: Mike Cannon, Matt Donnelly, Josiah Bethards, Duncan Hamilton, Blake Hoerster, and Nathan Sauers.

Gibson Dunn lawyers are available to assist in addressing any questions you may have about these developments. To learn more about these issues, please contact the Gibson Dunn lawyer with whom you usually work, any member of the firm's Tax, Cleantech, or Power and Renewables practice groups, or the following authors:

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