



June 3, 2019

Regulations Division
Office of General Counsel
United States Department of Housing and Urban Development
451 7th Street SW, Room 10276
Washington, DC 20410-0500

RE: RIN 2501-AD87, Notice of Proposed Rulemaking on Enhancing and Streamlining the Implementation of Section 3 Requirements for Creating Economic Opportunities for Low- and Very Low-Income Persons and Eligible Businesses

To Whom It May Concern:

The Local Initiatives Support Corporation (LISC) appreciates the opportunity to provide comments on proposed amendments to the U.S. Department of Housing and Urban Development's (HUD) Section 3 regulations.

Established in 1979, LISC is a national nonprofit housing and community development organization that is dedicated to helping community residents transform distressed neighborhoods into healthy and sustainable communities of choice and opportunity. LISC mobilizes corporate, government and philanthropic support to provide local community development organizations with loans, grants and equity investments; as well as technical and management assistance. Our organization has a nationwide footprint, with local offices in 33 cities. LISC invests approximately \$1.4 billion each year in these communities and our work covers a wide range of activities, including affordable housing, economic development, building family wealth and incomes, education, and creating healthy communities.

General Comments

Before we address specific questions posed in the rule, we have some general comments about the proposal. LISC believes that Section 3 is one of HUD's most important responsibilities since it creates the standards by which employment, training, and contracting opportunities are generated from HUD financial assistance. LISC has a deep understanding of the need and models for building low-income families financial well-being. For instance, LISC provides community organizations throughout the United States financial support and technical assistance to operate Financial Opportunity Centers (FOCs). Through LISC's FOCs, clients receive three bundled services - financial coaching, employment and career counseling and income supports - frequently enhanced with low-cost financial products that help build credit, savings and assets. Clients can also access LISC's small business and microenterprise lending products, which can support construction businesses in need of working capital or other assistance triggered by Section 3 opportunities. FOCs' mutually reinforcing program components have proven to help people stay motivated, as evidenced by improved job retention; and to improve their economic prospects, as evidenced by improvements in credit scores and in credit building behavior.

HUD's Section 3 regulations have the ability to provide employment and economic opportunities for our nation's lowest income communities and people. LISC sees great potential in how a stronger Section 3 rule can link our FOC efforts with increased hiring and contracting opportunities. For instance, FOCs

provide contextualized skills training to link low-income people to employment, often for construction trades, and could be a vital training and referral source for employment and contracting opportunities generated from covered projects receiving HUD financial assistance. LISC has facilitated these connections in Houston, where we are working to link our FOC work with Section 3 economic opportunities generated from Community Development Block Grant-Disaster Recovery (CDBG-DR) financial assistance. The goal is to ensure that Section 3 Business Concerns and low-income residents enrolled in Houston based FOCs providing construction training receive hiring and contracting opportunities as affordable housing is rehabilitated and built using CDBG-DR funding.

The current Section 3 rule is over 20 years old and LISC has seen both the success and challenge of using the regulation to provide HUD assisted and low-income residents and businesses economic opportunities generated from HUD funding. LISC believes HUD's proposed rule has many merits and is an overall improvement from the current regulation. The comments below provide our feedback on the major provisions of this proposed rule, followed by responses on specific questions stated in the Notice.

Promoting Long Term Employment

HUD's current Section 3 rule requires at least 30 percent of new hires be Section 3 residents for covered projects. As HUD notes in the proposed rule, the emphasis on new hiring does not promote sustained employment. In practice, Recipients have often brought on new hires for short periods of time, which doesn't provide the employment necessary to increase earned income or the contextualized skills training and credentialing that connect employees to a career pathway. HUD proposes in the rule to track labor hours as a proportion of the total work performed by all workers on a project instead of new hires. Recipients would be held to benchmarks published in the Federal Register every three years and HUD would refine these thresholds as it receives data through compliance reporting. HUD states this is more in line with standard business practices since most businesses, including construction, regularly track labor hours, which should reduce administrative burden. HUD also proposes to encourage sustained employment by allowing employers to consider a Section 3 worker who was low-income at the time of hire as a Section 3 worker even if they exceed low-income thresholds at a future date.

LISC supports HUD's proposal to track labor hours instead of new hires since we believe this will promote longer term employment, which we know through our FOC and financial stability work to be one of the strongest ways to move families out of poverty. In addition, we support HUD's proposal to allow low-income Section 3 workers to continue to be counted as low-income if they were at the time of hire. We think this is a sensible proposal since Section 3 policy should be incentivizing increases in income over time and not penalizing those employees who substantially raise their incomes.

Proposed Applicability and Reporting Thresholds

The Section 3 proposed rule applies to Public Housing Program assistance and Section 3 projects, which are defined as HUD program assistance used for housing rehabilitation, housing construction, and other public construction projects that generally exceed a \$200,000 project threshold or any funding from the Lead Hazard Control and Healthy Homes program. The proposed rule exempts small public housing authorities (PHA), which are defined as those with fewer than 250 units of public housing, from benchmark reporting, and would instead only require reports on Section 3 qualitative efforts.

The statute authorizing Section 3 makes no mention of HUD financial assistance thresholds and instead states "that the employment and other economic opportunities generated by Federal financial assistance for housing and community development programs shall, to the greatest extent feasible, be directed toward low- and very low-income persons, particularly those who are recipients of government assistance for housing." A key part of the Section 3 statute is the use of "greatest extent feasible" and "best efforts", which shows Congressional intent for HUD to provide Recipients leeway when implementing Section 3 due to constraints outside of their control, which may limit their ability to achieve the hiring and

contracting goals. LISC supports the \$200,000 project threshold and recommends that HUD develop guidance materials on how to show best efforts when organizations don't meet their Section 3 goals.

Section 3 Workers and Targeted Section 3 Workers

HUD's proposed rule includes new terminology, including Section 3 Workers and Targeted Section 3 Workers. Section 3 Workers replaces the current interim rule's Section 3 Resident definition and is defined to mean a low-income person, a worker who lives in a low-income housing tax credit (LIHTC) qualified census tract (QCT), or a worker employed by a Section 3 Business. HUD proposes the use of the Targeted Section 3 Worker definition since the statute requires Recipients of certain financial assistance to direct employment and economic opportunities to specific groups of low- and very low-income individuals. Targeted Section 3 Workers for public housing financial assistance would include public housing or Section 8 (tenant-based or project-based) residents; residents of other PHA projects expending assistance; YouthBuild participants; or Section 3 Business employees. Targeted Section 3 Workers for Section 3 Projects include low- or very low-income workers in the service area or neighborhood of the Project; YouthBuild participants; or Section 3 Business employees.

LISC generally supports both definitions since the regulatory responsibilities are clear and in line with the statute. That said, we have concerns about including LIHTC QCTs in the Section 3 Worker definition. LIHTC QCTs are census tracts with a poverty rate of 25 percent or more, or with at least 50 percent of households having income less than 60 percent of AMI. We don't believe having a place-based criteria is needed for the Section 3 Worker definition since it's generally unnecessary and poses risks to HUD. We believe it's unnecessary since the current Section 3 Resident definition is targeted to public housing residents or low- or very-low income persons in metropolitan and nonmetropolitan areas. The statute and current rule, target resources to low-income people. We see no reason to include place-based criteria since the proposed definition already captures low-income people or businesses majority owned or staffed by low-income people. In addition, LIHTC QCTs, while majority low-income, can include non-low-income populations, which creates risk to HUD and potential abuse by Recipients.

The Section 3 Workers and Targeted Section 3 Workers definitions also allow workers employed by Section 3 businesses to count as eligible employees. This creates some risk of non-low-income persons receiving benefits, since there can be higher income populations working at these business, although we believe this is generally mitigated by the definition's inclusion of low-income ownership control and/or staffing and the statute's emphasis on contracting opportunities. We do note however that "a worker employed by a Section 3 business" is included in both the Section 3 Worker and Targeted Section 3 Worker definition. We recommend that it only be included in the Targeted Section 3 Worker definition since this was created to better align the regulation with the law.

Section 3 Business Concern

The proposed rule includes a new definition for defining a Section 3 Business Concern. The new definition states that a Section 3 Business Concern is at least 51 percent owned by low-income people; or low-income people work more than 75 percent of the labor hours at the business; or at least 25 percent of the business is owned by public housing or Section 8 residents. The first part of the definition is the same as the current rule while the second part increases the labor hour percentage from 30 percent to 75 percent. The last part is new and HUD states it was included to emphasize small business formation by public housing and Section 8 residents.

LISC supports the first part of the new Section 3 Business Concern definition since it follows the statute's intent. We do have concerns about increasing the percentage of low-income employee labor hours from 30 percent to 75 percent. While we believe this is well intended and in line with statute's emphasis on "employing a substantial number of persons", LISC is concerned that it will be difficult for many businesses to achieve such a high threshold and may preclude businesses with a high proportion of low-

income workers from being eligible. LISC recommends that HUD change the labor hours threshold to 51 percent although allow a three year window after the rule's enactment to meet the new standard. This will further align the rule with the statutory language, while allowing time for businesses to adjust to the new rule and minimize compliance risk.

Benchmarks

HUD proposes Section 3 Benchmarks in a separate Federal Register Notice and states that these benchmarks will be updated every three years and refined over time as HUD collects data. The proposed rule would require PHAs and Section 3 Project Recipients to generally report the total number of labor hours, Section 3 Labor Hours, and Targeted Section 3 Labor Hours. HUD proposes the same benchmarks for public housing financial assistance and Section 3 Project Recipients. The proposed benchmarks are 25 percent of all project labor hours be performed by Section 3 Workers, and 5 percent of all project labor hours come from Targeted Section 3 Workers. Recipients who achieve these safe harbor benchmarks are presumed to be in compliance. HUD would require qualitative reporting from PHAs and Recipients that don't achieve compliance and HUD will develop a reporting form, which captures other efforts made, including outreach to job applicants, provision of the on-the-job training, tuition for training, and outreach to identify bids from Section 3 businesses.

LISC generally supports the 25 percent and 5 percent benchmarks and believe these are a reasonable starting point for the new rule. LISC recommends though that HUD strengthen its compliance practices around Section 3 to incentivize performance, while recognizing legitimate constraints with complying with the rule. The statute appropriately allows Recipients to report best efforts since achieving the yearly benchmarks may be difficult for reasons outside of a Recipient's control, including tight labor markets, lack of local training and referral sources, or a paucity of Section 3 eligible businesses. LISC recommends that HUD state in the proposed rule that it will deduct points in relevant HUD program Notices to applicants of HUD competitive funding, which have not achieved Section 3 benchmarks. The proposed rule should note that such Notices must allow applicants the ability to provide justifications on why they weren't able to achieve the Section 3 benchmarks and HUD should review such information in a standardized way that doesn't penalize organizations, which documented good faith efforts to comply. LISC provides examples of what efforts HUD should consider in our response to HUD's question 1 below. Evaluating Section 3 performance in competitive funding Notices would further incentivize Section 3 compliance. In addition, HUD should utilize Community Compass technical assistance funds to create best practice resources and employ contractors to support jurisdictions and PHAs without a Section 3 Coordinator position, or that may need help in complying with the rule.

Section 3 Compliance

HUD proposes to incorporate Section 3 compliance enforcement into HUD program office staff duties. HUD states this will make Section 3 a more integral part of the program office's work and justifies it since these staff are regularly in contact with their award Recipients. The Department proposes to eliminate the current interim rule's provision on public complaint and compliance review procedures, which are currently administered by the Office of Fair Housing and Equal Opportunity (FHEO).

LISC is concerned about this proposal and recommends that HUD maintain their complaint and compliance enforcement out of FHEO. Our main concern with this proposal is that the HUD program staff offices are thinly staffed, and that incorporating new responsibilities outside of their daily program administration duties will lead to inconsistent enforcement across the Department. Relatedly, HUD program staff do not have expertise in Section 3 regulations and it seems counterproductive to embed compliance in their offices when they have limited knowledge of the administrative, regulatory, and systems needs for Section 3 enforcement. In addition, it's not clear how the public will be able to make Section 3 complaints if HUD removes the current public complaint process. For instance, how would an individual or business know which office to call if they have a grievance? And would the program staff

person be able to help them address Section 3 problems? Lastly, HUD states the Office of Field Policy and Management (FPM) would have a role in compliance although FPM has not traditionally had any HUD programmatic enforcement role. It seems much simpler and transparent for the Department to allow program offices to incentivize Section 3 performance and compliance practices individually in their respective funding Notices although have a Department wide entity focus on all aspects of compliance, including reporting, analysis, and information technology systems.

Training Needs

The Section 3 statute's provisions on public housing assistance and other HUD programs emphasizes that HUD shall ensure that employment and (*italicize added*) *training* opportunities from HUD covered financial assistance are made available to low-income and HUD assisted residents. HUD's proposed rule and associated benchmarks emphasize employment and contracting through the monitoring of labor hours, which we believe is appropriate, although mainly leaves out any focus on skills training. Training is only referenced as a potential response for Recipients who have to submit a qualitative compliance report for failing Section 3 benchmarks.

LISC agrees that Recipients who don't meet Section 3 benchmarks should be allowed to describe their training and outreach efforts, since we know from our FOC and financial stability work that high quality training is essential to getting low-income people prepared for long-term employment. This requirement will help incentivize training integration into Section 3 efforts, even if they don't meet HUD's benchmarks. LISC also recommends that HUD include in the proposed rule an explicit requirement that public housing authorities and jurisdictions receiving HUD block grant dollars make reasonable efforts to connect Section 3 Workers and Targeted Section 3 Workers to local workforce development and career and technical education training organizations. Many PHAs and jurisdictions have Section 3 coordinators, which perform this function, and coordinate with relevant local government employment services agencies, FOCs, nonprofit organizations, and other relevant organizations.

LISC also recommends that HUD actively provide outreach on the Department's training, employment, and asset building programs to HUD assisted residents. HUD is in a unique position to be able to promote its own voluntary programs, including Family Self Sufficiency, Jobs Plus, and the Resident Opportunity and Self-Sufficiency programs, to ensure that HUD assisted residents can access limited resources available for training and service coordination.

Lastly, LISC notes that up to 15 percent of CDBG dollars can be used for Public Services, which includes employment services, such as job training, as an eligible use. Many jurisdictions utilize CDBG for this purpose and it's one of the only HUD programs able to support job training for low-income people. LISC recommends that HUD create case studies and resource guides on how CDBG has been utilized to support effective job training programs. Jurisdiction have leeway on how to use these block grant dollars, which we believe is appropriate, although could benefit from additional resources on how these dollars can be used to support Section 3 and local job training and hiring initiatives. LISC believes this is especially important for the CDBG-DR program since jurisdictions often receive substantial allocations of HUD assistance. This provides an opportunity to ensure equitable hiring and contracting opportunities when localities engage in rebuilding efforts.

Comments on the Notice of Proposed Rulemaking

The following lists LISC's specific comments by request number:

1) HUD seeks comments on the use of the statutory terms "best efforts" and "greatest extent feasible" in this proposed rule.

The Section 3 statute uses the terms “best efforts” and “greatest extent feasible” for Section 3 efforts while the current interim rule only uses the term “greatest extent feasible.” HUD’s proposed rule uses the terms “best efforts” in conjunction with public housing assistance and “greatest extent feasible” with Section 3 Projects, which is more in line with the statutory language.

LISC supports this framework and recommends that HUD provide Recipients guidance on how to show best efforts complying with the rule. LISC recommends that HUD create data collection forms, which collect: 1) creation of local labor and contractor databases matching eligible workers and businesses; 2) education and employment training initiatives, including coordination with local government employment services offices, FOCs, community organizations, and other relevant groups. Section 3 Recipients should document that they reached out to these entities to publicize training opportunities and to market employment and contracting opportunities; 3) creation of education and training funds for eligible persons; 4) promotion of HUD asset building programs, if the local PHA has an active grant with one of HUD’s asset building programs; and 5) other directed and relevant activities. LISC recommends these be included in any new HUD Section 3 Plan template posted on the Department’s website.

3) HUD seeks comments on whether an alternate threshold would be more appropriate or equally effective to the proposed \$200,000 per project threshold. HUD also seeks comment on the inclusion of all projects under the HUD Lead Hazard Control and Healthy Homes programs and exclusion of Section 8 programs. Lastly, HUD seeks comments on whether the threshold for Section 3 projects should be established by project, total funding received by the Recipient, or whether the threshold should be based on total funds expended by a Recipient.

LISC supports HUD’s \$200,000 project threshold since this is aligned with local hiring and disadvantaged small business requirements and ensures some employment opportunities by the covered program. Under this standard, most Section 3 Projects are covered by the regulation while minimizing burden to small jurisdictions and other Recipients. In addition, LISC doesn’t recommend that Section 8 programs be included in the proposed rule since they aren’t explicitly included in the Section 3 statute and since the covered Section 3 Project programs are affordable housing and community development project subsidy sources, while Section 8 programs provide operating subsidy. This is a key distinction and we don’t believe that owners receiving Section 8 program assistance should be subject to Section 3 regulatory responsibilities.

4) HUD seeks comment on HUD’s proposal to include hours worked by Section 3 business employees in the Targeted Section 3 Worker definition as a way to report all Section 3 activities in a single metric rather than reporting on Section 3 Business Concern participation separately through the existing aggregate dollars spent calculation.

As mentioned, LISC has concerns that the Section 3 Business Concern definition will be difficult to achieve, specifically with increasing the percentage of low-income employee labor hours from 30 percent to 75 percent. LISC recommends that HUD change the labor hours threshold to 51 percent although allow a three year window after the rule’s enactment to meet the new standard. This will further align the rule with the statutory language, while allowing time for businesses to adjust to the new rule and minimize compliance risk.

LISC believes the proposed rule’s focus on hours worked, which includes Section 3 business employees in the Section 3 Worker and Targeted Section 3 Worker definitions is appropriate since the statute specifically focuses on prioritizing businesses providing economic opportunities for low-income residents. Aggregating the hours worked by Section 3 business employees creates some risk to HUD, since there can be non-low-income people reporting hours although the majority of the business is by

definition either low-income owned or staffed. LISC believes this mitigates risk to HUD and ensures that contracting opportunities are being directed to business providing opportunities to low-income people.

6) HUD seeks comments on whether Section 3 requirements, as it applies to Section 3 projects, should apply to all subcontractors, and whether at a certain level HUD should consider reducing the reporting or compliance burden for subcontractors.

LISC recommends that Section 3 requirements apply to both contractors and subcontractors since the use of a subcontractor shouldn't negate Section 3 responsibilities. Removing Section 3 requirements for subcontractors would decrease the reach of Section 3 regulations and lessen the amount of covered hiring and contracting responsibilities.

7) HUD requests comment on whether its initial and future benchmarks should include benchmarks for both the number of labor hours worked by Section 3 workers divided by the total number of labor hours for all workers and the number of labor hours worked by Targeted Section 3 workers divided by the total number of labor hours for all workers. Alternatively, HUD seeks comment on limiting the benchmark to include Targeted Section 3 workers only.

LISC supports HUD's proposed initial benchmarks and focus on labor hours since we believe it will encourage longer-term employment. We believe that HUD should evaluate the efficacy of this approach as the Department receives compliance data and make changes, as necessary, in future benchmarks if the data indicates it's not supporting sustained employment.

8) For Section 3 projects, the statute requires that "where feasible, priority should be given to low- and very low-income persons residing within the service area of the project or the neighborhood in which the project is located." The statute does not define "neighborhood" or "service area" for purposes of how recipients determine where they should focus their prioritization. The lack of definitions complicates compliance for contractors, subcontractors, and grantees receiving multiple types of HUD financial assistance. HUD proposes to provide a definition for recipients to use when prioritizing and reporting workers for Section 3 projects. The definition differs from existing regulatory definitions and local or state definitions, and HUD specifically requests comment on whether the definition works for recipients or if a different definition for "neighborhood" or "service area" is needed for purposes of Section 3. HUD also asks whether the 1 mile and 5,000 population radius is an appropriate geographic size of a 'neighborhood' or 'service area.'

HUD's proposes for the purposes of Section 3 only, to define "service area or the neighborhood of the project" to mean an area within 1 mile of the Section 3 project or, if fewer than 5,000 people live within one mile of a Section 3 project, within a circle centered on the Section 3 project that is sufficient to encompass a population of 5,000 people according to the most recent U.S. Census. LISC supports HUD's proposed definition since we believe it provides enough flexibility to capture a local area's employment base. We also appreciate that it limits the risk of not capturing individuals who may live across the street from covered projects, although who may reside in different jurisdictions or census tracts. LISC has experienced this constraint with place-based compliance practices in other federal programs and believes, based on HUD's data in the proposed rule, that this is a reasonable definition.

LISC would be happy to provide additional information on our comments. Please contact Mark Kudlowitz (mkudlowitz@lisc.org) with any questions.

Sincerely,

A handwritten signature in black ink, appearing to read "Matt Josephs", with a long horizontal flourish extending to the right.

Matt Josephs
Senior Vice President for Policy
Local Initiatives Support Corporation