Section 3 Compliance and Reporting
Perspectives for Subrecipients, Developers, General Contractors and Builders

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Please Note!

- This presentation focuses on Section 3 requirements for housing and community development projects (including CDBG-DR and MIT) which are different than the requirements for Public Housing Authorities.

- Within this presentation, the terms “Developer,” “General Contractor” and “Builder” may be used interchangeably. The requirements under Section 3 apply to any recipient of HUD funds over the applicable dollar threshold, regardless of terminology.

- The recent Section 3 “Final Rule” modified Section 3 requirements. The first section covers these changes in detail, and throughout this presentation the new requirements will be indicated by *purple italic text*.

- Arrows mean recommended options or solutions to meet compliance but not articulated in the regulations or prescribed by HUD.
Section 3 Final Rule
What is Section 3?

- Provision of Housing and Urban Development Act of 1968
- Helps bring economic opportunities generated by some HUD assistance to low-income and very low-income persons residing in the area where HUD funds are being expended
- Results in a dual benefit for low- and moderate-income areas:
  - New or rehabilitated housing and public facilities and/or infrastructure
  - Jobs and other economic opportunities working on HUD-assisted projects
Why did Section 3 Change?

- Streamline tracking and reporting to make compliance easier
- Align regulations with standard business practices
- Increase positive Section 3 outcomes
## Highlights of the Final Rule (1/2)

<table>
<thead>
<tr>
<th>Previous Requirement</th>
<th>New Requirement</th>
</tr>
</thead>
<tbody>
<tr>
<td>30% of new hires must be Section 3 residents</td>
<td>25% of total <em>project hours</em> worked by Section 3 workers; 5% by targeted Section 3 workers</td>
</tr>
<tr>
<td>Used the term “Section 3 resident”</td>
<td>Uses the term “Section 3 worker”</td>
</tr>
<tr>
<td>No preference or definition for targeted Section 3 worker</td>
<td>Added preference &amp; definition for targeted Section 3 worker</td>
</tr>
<tr>
<td>Business could be Section 3 if subcontracting 25% of work to other Section 3 firms</td>
<td>Business can be Section 3 if 51% owned by PHA resident or 75% of hours worked are by Section 3 workers</td>
</tr>
<tr>
<td>10% of construction costs contracted to Section 3 firms</td>
<td>No numeric benchmark but must contract with Section 3 businesses to greatest extent feasible</td>
</tr>
<tr>
<td>3% of non-construction costs contracted to Section 3 firms</td>
<td>Professional services that require specialized degrees or licensing not subject to Section 3</td>
</tr>
</tbody>
</table>
## Highlights of the Final Rule (2/2)

<table>
<thead>
<tr>
<th>Previous Requirement</th>
<th>New Requirement</th>
</tr>
</thead>
<tbody>
<tr>
<td>Program-wide compliance required if &gt;$200K in HUD funds</td>
<td>Section 3 compliance required on a per-project basis only</td>
</tr>
<tr>
<td>Covered project = greater than $100K in HUD assistance</td>
<td>Covered project = greater than $200K in CPD assistance or greater than $100K in Lead and Healthy Homes funding</td>
</tr>
<tr>
<td>Covered project threshold was fixed</td>
<td>Covered project threshold may be updated every 3 years by FR notice</td>
</tr>
<tr>
<td>Reported in SPEARS</td>
<td>Reported in IDIS or DRGR depending on funding source</td>
</tr>
<tr>
<td>Implementing regulation 24 CFR 135</td>
<td>Implementing regulation 24 CFR 75</td>
</tr>
<tr>
<td>Fixed numeric benchmarks and project thresholds</td>
<td>Numeric benchmarks updated every 3 years by FR notice; Project thresholds updated every 5 years by FR notice</td>
</tr>
<tr>
<td>Overseen by the Office of Fair Housing and Equal Opportunity</td>
<td>Overseen by Program Offices</td>
</tr>
</tbody>
</table>
Tracking Residents to Workers

• The definition for a Section 3 worker is different than the definition for a Section 3 resident

• **The new rule now requires that the labor hours of all qualified Section 3 “workers” must be tracked and reported**

• Local government or their assigns will be monitoring onsite to document that the stated Section 3 worker is working as reported

• This puts responsibility on developers and general contractors to coordinate site sign-in sheets and logs of labor hours performed by pre-designated Section 3 “workers”

• Criteria for qualifying a Section 3 business were also modified and will impact a change for how developers and/or general contractors report information.
Additional Considerations

• Under the old Section 3 rule, grantees were required to direct 3% of non-construction project costs (such as professional services) to Section 3 business concerns.

• *With the new rule there is no longer a numeric benchmark for non-construction participation, but HUD permits grantees to include professional services in the percentage of Section 3 hours worked to help achieve safe harbor. (This can help you meet the numeric goals.)*

• This allows developers to use professional service providers for soft costs like A&E to help meet Section 3 numeric goals
Overview of How to Apply Section 3
When Does Section 3 Apply?

- Section 3 is required when the following occur:
  1. The project involves new construction, rehab or demolition of housing, infrastructure or public facilities AND
  2. The project costs exceed $200K for CPD (or $100K for Lead and Healthy Homes funded projects) and results in employment, training, or contracting opportunities during the course of the project
- Section 3 applies to the entire project, regardless of whether the activity is fully or partially funded with HUD assistance
- States and subrecipients are responsible for ensuring that contractors, subcontractors and developers comply with Section 3 on applicable projects
- Dollar thresholds may be updated every 3 years by FRN (https://www.federalregister.gov)
Other Section 3 Considerations

• For projects estimated to be near or above the dollar threshold, contractors may be procured with the upfront understanding that Section 3 numeric goals apply.

• Award preference to Section 3 businesses may be given in the evaluation of returned bids—HUD considers this a qualitative effort that can help achieve safe harbor if numeric benchmarks are not achieved.

• Section 3 will only apply on a per-project basis rather than per contracted program activity. “The project is the site or sites together with any building(s) and improvements located on the site(s) that are under common ownership, management, and financing.” (24 CFR 75.3(a)(2))

*For individual projects under $200K Section 3 is still encouraged but not required.
Checkpoint

- What types of projects does Section 3 apply to?
- What is the dollar threshold for a project to trigger Section 3?
- What was the major change to the type of data and reporting requirements for Section 3?
- Do non-construction trades need to meet Section 3?
What is a Section 3 Business Concern?

A Section 3 Business Concern is any business that meets at least one of the following criteria, documented within six months of either the date the contract is executed or throughout the duration of the project:

- At least 51 percent owned and controlled by low- or very low-income persons; or
- Over 75 percent of the labor hours performed at the business over the prior three-month period are performed by Section 3 workers; or
- A business at least 51 percent owned and controlled by current public housing residents or residents who currently live in Section 8-assisted housing
There is no longer a numeric goal for contracting with Section 3 businesses. However, it is still important to certify Section 3 businesses and track contracts awarded to Section 3 business concerns for the following reasons:

• Regulations require grantees to make best efforts to contract with businesses that direct economic opportunities to Section 3 workers

• It may be necessary to certify Section 3 businesses in order to certify workers—subject to State or local certification procedures

• **100% of hours worked by Section 3 business concerns can be counted as Section 3 hours**

• It helps grantees and subrecipients meet best efforts toward safe harbor when numeric goals cannot be achieved
Section 3 Certification for Businesses

• Recipients may establish their own system to certify Section 3 business concerns, including when and how self-certification may be used

• If a business concern claims Section 3 status, certification should be done at the start of the project

• A business retains Section 3 status for the life of the project as long as it continues to meet the definition
  
  ➢ Grantee must set policy as to how long a business may retain its Section 3 certification on a project before re-certification is necessary

  ➢ Three years is a common certification timeframe accepted in other programs. If you seek a longer time period, we recommend that you inform your HUD field office rep of your decision and why it is reasonable
Unit Based Pricing

- If a firm maintains time and effort records for unit-based price estimate deliverables, those records should be submitted to the UGLG to demonstrate compliance with Section 3.

- If a firm does not track time and effort of staff to qualify for Section 3, a reasonable good-faith estimate should be developed upfront with the UGLG to establish a Section 3 hourly rate that could be used for the unit-priced deliverable. (This is rare but may need to be done in cases where a non-construction Section 3 business is qualified and you choose to use those hours as efforts toward Section 3 goals)

- Industry standard cost estimating information provides an average number of hours for specific tasks that could be utilized in situations where a work task is completed but time sheets are not used or available.
Grantees must qualify two categories of Section 3 workers to meet the overall numeric goals for Section 3 projects:

• **Section 3 worker** *(25% total hours worked on project) AND*

• **Targeted Section 3 worker** *(5%* of total hours worked on project)*

*The 5% is included within the overall 25% total numeric goal per project.
What is a Section 3 Worker?

Any employee who meets one of the following categories within the past five* years or at time of project:

- The worker's income for the previous or annualized calendar year is below 80% of the area median income for the area in which the worker resides. Use the worker’s annual gross income based on AMI for a single-person household; or

- The worker is employed by a Section 3 business concern; or

- The worker is a YouthBuild participant.

*Qualifying a worker as a targeted Section 3 worker will count as a Section 3 worker.

*Documentation must be dated within five years of the project start date or date of hire (whichever is later)
What is a Targeted Section 3 Worker?

A targeted Section 3 worker is a subset of Section 3 workers.

Contractors must track hours worked by both Section 3 workers AND targeted Section 3 workers in order to meet numeric goals.

A Targeted Section 3 worker means a Section 3 worker who:

• Is employed by a Section 3 business concern; or

• Currently fits, or when hired fit, at least one of the following categories as documented within the past five years:
  - Living within the service area or the neighborhood of the project
  - A YouthBuild participant.
What is YouthBuild?

https://www.dol.gov/agencies/eta/youth/youthbuild

- National organization with community-based pre-apprenticeship program that provides job training and educational opportunities for at-risk youth ages 16-24 who have previously dropped out of high school

- Participants learn vocational skills in construction and other industries such as health care, IT and hospitality

- Youth also serve the community through construction or rehabilitation of affordable housing for low-income or homeless families in their own neighborhoods

- Administered by the U.S. Department of Labor

- Your local YouthBuild chapter may be a good source for qualifying Section 3 labor when there are opportunities for new hire or re-hire positions
State and local subrecipients must establish a method to certify Section 3 workers, including when and how self-certification can be used. Developers must coordinate and use the subrecipient’s form and method for providing this information.

For targeted Section 3 workers, subrecipient-adopted policies will require developers to document one of the following:

- Employer’s confirmation that a worker’s residence is within the Section 3 service area; or
- Employer’s certification that the worker is employed by a Section 3 business concern; or
- Worker’s self-certification of YouthBuild participation.

Current Section 3 workers who were certified under 24 CFR 135 must be re-certified under 24 CFR 75 (certification under the old rule must be re-done after November 30, 2020)

A worker’s hours may be counted for up to five years toward the Section 3 numeric goal. The five-year period begins at the time of hire, or when the worker is first certified as meeting the definition of a Section 3 worker.
Section 3 Service Area

• “Service area” or the “neighborhood of the project” means an area within one 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

• Residing in the Section 3 service area is one of the criteria for a Section 3 targeted worker

• Section 3 service area is NOT the same as low-mod area, which pertains to meeting a CDBG national objective
Mapping a Section 3 Service Area

- HUD is in the process of developing a Section 3 service area mapping tool

  - In the meantime, recommend working with local GIS or Planning Department to determine correct radius if greater than one mile

  - Use Google Earth to determine the straight-line distance from a worker’s residence to the project site

  - Place printouts of map and Google Earth in project file
### “Section 3” vs. “Targeted Section 3”

<table>
<thead>
<tr>
<th>Section 3 Worker</th>
<th>Targeted Section 3 Worker</th>
</tr>
</thead>
<tbody>
<tr>
<td>Any worker who currently fits, or when hired within the past five years fit, at least one of the following categories, as documented: 1. Employed by a Section 3 business concern 2. YouthBuild participant or 3. Income is below 80% AMI</td>
<td>Any Section 3 worker who: 1. Is employed by a Section 3 business concern; or 2. Currently fits, or when hired fit, at least one of the following categories as documented within the past five years: a. Living within the service area or the neighborhood of the project b. A YouthBuild participant.</td>
</tr>
<tr>
<td>25% of hours worked on a Section 3 project</td>
<td>5% of hours worked on a Section 3 project (included in 25%)</td>
</tr>
<tr>
<td>Self-certification permitted But grantees should perform due diligence before awarding contracts to firms that have self-certified by ensuring that they meet the definition of a Section 3 business concern as defined by the Department's regulations at 24 CFR 135.5.</td>
<td>Grantee or UGLG must verify status by one of three methods: 1. Employer confirmation that worker resides within the Section 3 service area 2. Employer certification that worker is employed by a Section 3 business concern 3. Worker self-certification of YouthBuild participation</td>
</tr>
</tbody>
</table>
Checkpoint

• What is the benefit of certifying a Section 3 business?
• What are the two types of Section 3 workers?
• When would you need to determine the Section 3 service area?
Numeric Goals for Section 3 Projects

- 25% or more of the total hours worked on a project performed by Section 3 workers
- 5% or more of the total hours on a project performed by Targeted Section 3 workers
- The 5% numeric goal is included within the 25% goal (i.e. the total is 25%, not 30%)
Numeric Goals for Section 3 Projects – Cont.

• Includes hours worked on a project by nonprofit developer subrecipients, contractors and subcontractors

• If numeric goals not achieved, must document “qualitative efforts”

• There is no longer a numeric goal that 10% of construction costs and 3% of non-construction costs must benefit Section 3 business concerns
  
  o States, subrecipients and developers must still make best efforts to contract with Section 3 businesses

• Benchmarks updated every 3 years by FRN (https://www.federalregister.gov)
Section 3 Safe Harbor Provision

- If you meet the Section 3 percentages of work hours, HUD will consider you in compliance.

- You may also achieve safe harbor through qualitative efforts toward compliance such as outreach and training.

- If you do not meet the percentage of work hour goals, HUD will evaluate your qualitative efforts to determine if safe harbor is achieved.
Examples of Qualitative Efforts

(https://www.hud.gov/sites/documents/11SECFAQS.PDF)

- Engage in outreach efforts to generate job applicants who are Targeted Section 3 workers
- Provide training or apprenticeship opportunities
- Provide technical assistance to help Section 3 workers compete for jobs (e.g., resume assistance, coaching)
- Assist or connect Section 3 workers with drafting resumes, preparing for interviews, and finding job opportunities
- Hold regular job fairs
- Provide or refer Section 3 workers to services supporting work readiness and retention (e.g., work readiness activities, interview clothing, test fees, transportation, childcare)
- Provide assistance to apply for or attend community college, a four-year educational institution, or vocational/technical training
Examples of Qualitative Efforts Cont.

(https://www.hud.gov/sites/documents/11SECFAQS.PDF)

- Help Section 3 workers to obtain financial literacy training and/or coaching
- Engage in outreach efforts to identify and secure bids from Section 3 business concerns
- Provide technical assistance to help Section 3 business concerns understand and bid on contracts
- Divide contracts into smaller jobs to facilitate participation by Section 3 business concerns
- Provide bonding assistance, guarantees, or other efforts to support viable bids from Section 3 business concerns
- Promote use of business registries designed to create opportunities for disadvantaged and small businesses
- Outreach, engagement, or referrals with the state one-stop system as defined in Section 121(e)(2) of the Workforce Innovation and Opportunity Act
Section 3 Compliance & Reporting
Section 3 Responsibilities

**State**
- Provides Section 3 Plan template and guidance to UGLGs
- Monitors UGLGs for compliance with Section 3 requirements
- Reports Section 3 compliance to HUD

**UGLG**
- Refines State plan and implements Section 3
- Ensures contractors and developers make best efforts to comply with Section 3
- Reports Section 3 compliance to the State

**Developer**
- Makes best efforts to comply with Section 3 requirements
- Documents compliance efforts and submits timely reports to UGLG
Section 3 *Project* Implementation Plan

- Sample Forms (1-8) can be completed by bidder/developer to document how they will comply with Section 3 on the project

- **These are not official HUD or California Department of Housing and Community Development forms.** However, these are examples for how to capture information required in order to assess Section 3 compliance

- Grantees/subrecipients may use the template provided or develop their own forms or systems for documenting compliance and coordinating collection of required information

- Forms may be modified to capture additional info such as verification of non-debarment and E-Verify participation
FORM 0: Section 3 Overview

• General Section 3 information one page form
• Briefly describes intent of Section 3, threshold for a covered project, programmatic responsibilities and numeric goals.
• Includes instructions to bidders for completing the subsequent Forms (1-8)
FORM 1: Section 3 Assessment and Certifications

• Assesses whether a project will likely trigger Section 3 and how the bidder will achieve safe harbor

• Contains certifications that obligate bidder to make best efforts to comply with Section 3

• Subrecipients should require **ALL** bidders to submit this form with their bid, even if the project is not anticipated to trigger Section 3 (can count toward qualitative efforts)

• For Section 3 covered contracts, the completed form can be incorporated into the contract by attachment
FORM 2: Subcontractor Information

- Captures relevant information about all subcontractors working on a project.
- May be compared against Section 3 project interviews to assure truthful reporting of hours.
- Because subcontractors may be added or removed at any time, this form should be submitted at least three times during the project: with initial bid, upon contract execution, and with the final Section 3 compliance report – verification is not “one and done” and avoids disputes or misunderstanding.
- May also be modified to assist with Davis Bacon or Prevailing Wage monitoring.
FORM 3: List of Permanent Employees

- Captures information about all workers (not just those working on the Section 3 project) employed by contractor and all subcontractors
- May be compared against Section 3 project interviews and time records to assure truthful reporting of hours
- Because workers may be hired or terminated at any time, this form should be submitted at least twice during the project: with initial bid, and with the final Section 3 compliance report
FORM 4: Documentation of Qualitative Efforts

• Narrative form to document qualitative efforts

• Should be submitted with initial bid and also with each compliance report where numeric goals were not met
FORM 5: Section 3 Sample Contract Clause

- 24 CFR § 135.38 contained a Section 3 clause that was required to be incorporated into contracts under the previous requirements.
- The Section 3 clause spelled out the contractor’s obligations to uphold the provisions of Section 3.
- 24 CFR § 75 does not include an updated clause.

For now, we recommend updating the existing clause with the new implementing regulation and including in all contracts and subcontracts that are subject to Section 3.
FORM 6: Section 3 Compliance Report

- Documents total hours, Section 3 hours and Targeted Section 3 hours worked on project
- Must be accompanied by supporting documentation such as certified payrolls or time and attendance records
- Submitted quarterly and at the end of the project for entry into DRGR.
  - However, we recommend monthly submissions or with each invoice by contractor.
  - State/UGLG may make submission of Section 3 reports a condition of payment to incentivize early and consistent reporting
FORMS 7 & 8: Section 3 Sample Outreach Forms

• Optional/sample forms that awarded contractors may use to try assess which of their subcontractors and workers may qualify for Section 3

• After forms are submitted, the subrecipient Section 3 coordinator follows up with any firms or workers who indicated they may qualify for Section 3 to help them complete an application

• Using forms like these can count toward qualitative efforts even if respondents indicate they do not qualify for Section 3
Tracking Section 3 Hours

Hours tracked may be based on any of the following:

- Prevailing wage data
- Time-and-attendance system data
- Good faith assessments of hourly workers not tracked through a data system or
- Good faith assessments of salaried employees

Good faith assessments **may only be used** if a contractor is not required to report prevailing wage or does not have a time and attendance system in place.

Contractors are **not permitted** to self-certify hours in lieu of providing data (even if the data is just good faith assessments).

➢ Recommend grantees review good faith assessments from contractors to ensure the number of hours reported is reasonable for the project size, scope and **timeline**.
Additional Considerations

• Section 3 does not apply to material supply contracts or contracts that do not require any labor

• Section 3 **does** apply to demolition or remediation services

• The Section 3 status of a worker, targeted worker or business owner cannot be negatively affected by prior arrest or conviction

• Grantees are required to make best efforts to contract with businesses that employ Section 3 workers from the metropolitan area (or nonmetropolitan county) in which the project is located
Subrecipient Reporting Compliance to State/HUD

- Report Section 3 compliance through program-specific reporting systems (IDIS, DRGR)
- CDBG-DR and MIT grantees must enter projected Section 3 hours into DRGR Action Plan and report actuals via Quarterly Performance Reports
- HUD and grantees will be able to track progress meeting Section 3 numeric goals through a new MicroStrategy report
- SPEARS (the existing Section 3 reporting system) will be de-commissioned in 2021
- See HUD video “Section 3 New Rule Guidance for CDBG-DR and CDBG-MIT Grantees” published 7/1/21: https://youtu.be/7_khTGDLaew -- the last 12 minutes discuss DRGR
- For more guidance, refer to DRGR Fact Sheet: DRGR Guidance on Reporting Section 3 Labor Hours (https://www.hudexchange.info/resource/6413/drgr-fact-sheet-drgr-guidance-on-reporting-section-3-labor-hours/)
Timing of Transition to the Final Rule

Section 3 requirements apply to new grants, commitments, contracts, or projects funded on or after the November 30, 2020, effective date. For Section 3 Projects, this means that requirements apply to a legally binding written agreement or contract on or after November 30, 2020. For example, requirements apply to:

- An executed subrecipient agreement, including any subsequent contracts or agreements, that has project- or activity-level details with respective budgets, schedules and/or secured financing
- An executed homeowner rehabilitation loan or grant agreement, and any subsequent procured contracts (only when over $200K)
- An agreement or contract, that includes secured financing, with a developer or for-profit entity to complete a multifamily project
Summary of Transition Requirements

<table>
<thead>
<tr>
<th>Commitment Date</th>
<th>Before 11/30/2020</th>
<th>On or After 11/30/2020 but before 7/1/2021</th>
<th>On or After 7/1/2021</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Applicable Regulations</strong></td>
<td>24 CFR part 135</td>
<td>24 CFR part 75</td>
<td>24 CFR part 75</td>
</tr>
<tr>
<td><strong>Reporting Requirement</strong></td>
<td>Grantee must retain documentation demonstrating compliance with interim rule in project file.</td>
<td>Grantees must retain documentation demonstrating compliance with Final Rule in project file. Grantee will report in IDIS or DRGR for open activities starting July 1, 2021. If the IDIS or DRGR activity was set up prior to the system update, grantees will need to modify the IDIS or DRGR activity to generate the appropriate Section 3 compliance screen(s).</td>
<td>Grantee will report compliance data in IDIS or DRGR within the applicable reporting cycles beginning on or after July 1, 2021.</td>
</tr>
</tbody>
</table>
Checkpoint

• Give one example of how Section 3 worker hours may be documented and submitted.

• Does Section 3 apply to demolition activities?

• What is the minimum frequency a developer must provide Section 3 data?

• New grants, commitments and contracts were subject to the Section 3 Final Rule as of what date?
Regulatory References

- Section 3 requirements are found in several different HUD statutes and regulations, and therefore grantees and subrecipients must refer to different sections of the regulations to find all the requirements.


- **Federal Register Notices:** FR-6085-P-01, FR-6085-F-03
HUD Section 3 Portal: https://www.hud.gov/section3
HUD Section 3 Training Curriculum: https://www.hudexchange.info/trainings/section-3/
HUD Section 3 FAQs: https://www.hud.gov/sites/documents/11SECFAQS.PDF
YouthBuild: https://www.dol.gov/agencies/eta/youth/youthbuild
HUD Income Limits: https://www.huduser.gov/portal/datasets/il.html
Federal Register: https://www.federalregister.gov
DRGR Fact Sheet: https://www.hudexchange.info/resource/6413/drgr-fact-sheet-drgr-guidance-on-reporting-section-3-labor-hours/
Thank You!

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