

**DEPARTMENT OF HOUSING AND
URBAN DEVELOPMENT**

24 CFR Parts 5 and 570

[Docket No. FR-4881-F-02]

RIN 2501-AD03

**Equal Participation of Faith-Based
Organizations**

AGENCY: Office of the Secretary, HUD.

ACTION: Final rule.

SUMMARY: This final rule implements executive branch policy that, within the framework of constitutional church-state guidelines, faith-based organizations should be able to compete on an equal footing with other organizations for Federal funding. Executive Order 13279, entitled "Equal Protection of the Laws for Faith-Based and Community Organizations," establishes fundamental principles and policymaking criteria to guide Federal agencies in formulating and developing policies that have implications for faith-based and community organizations to ensure the equal protection of the laws for these organizations in federally-assisted social service programs. Consistent with the Executive Order, this final rule describes HUD's policy for the participation of faith-based organizations in HUD programs and activities. In addition, this final rule makes a conforming amendment to regulations for the State Community Development Block Grant (CDBG) program regarding the equal participation of faith-based organizations in the program. The final rule follows publication on March 3, 2004, of a proposed rule and takes into consideration the public comments received on the proposed rule. After careful consideration of the public comments, HUD has decided to adopt the proposed rule without change.

DATES: *Effective Date:* August 9, 2004.

FOR FURTHER INFORMATION CONTACT:

Ryan Streeter, Director, Center for Faith-Based and Community Initiatives, Department of Housing and Urban Development, Room 10184, 451 Seventh Street, SW., Washington, DC 20410-0001; telephone (202) 708-2404 (this is not a toll-free number). Hearing- or speech-impaired individuals may access this number through TTY by calling the toll-free Federal Information Relay Service at (800) 877-8339.

SUPPLEMENTARY INFORMATION:

I. Background

On March 3, 2004 (69 FR 10126), HUD published a proposed rule for public comment describing HUD's

policy for the equal participation of faith-based organizations in HUD's programs and activities. The proposed rule was published to implement Executive Order 13279, entitled, "Equal Protection of the Laws for Faith-Based and Community Organizations," which was signed by President George W. Bush on December 12, 2002, and published in the **Federal Register** on December 16, 2002 (67 FR 77141). The Executive Order establishes fundamental principles and policymaking criteria to guide executive branch agencies in formulating and developing policies that have implications for faith-based and community organizations and to ensure the equal protection of the laws for these organizations in programs receiving Federal financial assistance.

Executive Order 13279 is part of the Administration's broader Faith-Based and Community Initiative. President Bush has directed the executive branch agencies, including HUD, to take steps to ensure that Federal policies and programs are fully open to faith-based and community organizations in a manner that is consistent with the Constitution. The Administration believes that all eligible organizations, including faith-based organizations, should be able to participate in Federal programs and activities and compete, where required, for Federal financial assistance on an equal footing.

II. This Final Rule

This final rule follows publication of the March 3, 2004, proposed rule and takes into consideration the public comments received on the proposed rule. After careful consideration of the public comments, HUD has decided to adopt the proposed rule without change. Section IV of this preamble contains a discussion of the public comments received on the proposed rule and HUD's responses to the significant issues raised by those who commented.

A. New § 5.109 Regarding Equal Participation of Faith-Based Organizations

The final rule adds a new § 5.109 to HUD's regulations in 24 CFR part 5, subpart A. The regulations in subpart A of part 5 contain the definitions and Federal requirements generally applicable to all of HUD's programs. By placing the requirements of Executive Order 13279 in those HUD regulations that contain across-the-board requirements, HUD is ensuring the broadest application of the faith-based requirements of Executive Order 13279.

The equal participation policies and requirements set forth in § 5.109 are generally applicable to faith-based

organizations, which are referred to in the rule text as "religious organizations" that participate in HUD's programs or activities. More specific policies and requirements regarding the participation of faith-based organizations in individual HUD programs may be provided in the individual regulations for those programs. The policies and requirements set forth in § 5.109 are similar, and in many cases identical, to those contained in HUD's September 30, 2003, final rule (68 FR 56396) regarding the equal participation of faith-based organizations for several of its Community Planning and Development programs. Section III of this preamble provides an overview of the specific policies and requirements contained in the new § 5.109.

Two of the HUD programs that are affected by the regulatory changes are the Section 202 Supportive Housing for the Elderly Program and the Section 811 Supportive Housing for Persons with Disabilities Program. The regulations for these programs are located in 24 CFR part 891. Specifically, the equal participation requirements contained in this final rule permit faith-based organizations to take part in these programs as project owners. This is a change from the existing procedures governing these two programs, which prohibit a project owner from having a religious purpose in its articles of incorporation.

This final rule does not apply to HUD's Native American housing programs. HUD has determined that making the policies and procedures contained in this proposed rule applicable to its Native American programs requires prior consultation with Indian tribal governments in accordance with Executive Order 13175 (entitled "Consultation and Coordination with Indian Tribal Governments"). The Executive Order requires Federal departments and agencies, to the greatest extent practicable and permitted by law, to consult with tribal governments prior to taking actions that have substantial direct effects on Federally recognized tribal governments. HUD has consulted with Indian tribal governments regarding the applicability of these regulatory changes to its Native American housing programs and on June 21, 2004 (69 FR 34543) published a separate proposed rule to address the equal participation of faith-based organizations in these programs based on the outcome of the consultations.

B. Conforming Change to State CDBG Program Regulations

In addition to the establishment of new § 5.109, this final rule makes a conforming change to the regulations for the State Community Development Block Grant (CDBG) program regarding the equal participation of faith-based organizations. The final rule would clarify that the amendments made by HUD's September 30, 2003, final rule apply to the State CDBG program.

III. Overview of New 24 CFR 5.109

The specific policies and requirements codified in new § 5.109 by this final rule are as follows. As noted above, these requirements are unchanged from the proposals contained in HUD's March 3, 2004, proposed rule.

A. Equal Participation of Faith-Based Organizations in HUD Programs and Activities

This final rule clarifies that faith-based organizations are eligible, on the same basis as any other organization, to participate in HUD's programs and activities. The phrase "participate in HUD's programs and activities" and its variants are used in this rule to mean the full range of HUD programs and activities, including programs that make funds available through contracts, grants, cooperative agreements, or other instruments for eligible goods, services, and activities, and programs that do not make funds available, but involve other forms of benefit or resources. For example, certain Federal Housing Administration (FHA) programs do not provide funds, but make mortgage insurance or foreclosed properties available to qualifying organizations. Neither the Federal government, nor a State or local government, nor any other entity that administers any HUD program or activity shall discriminate against an organization on the basis of the organization's religious character or affiliation. Nothing in the rule, however, would preclude those administering Department-funded programs from accommodating religious organizations in a manner consistent with the Establishment Clause.

B. Inherently Religious Activities

Organizations that receive direct HUD funds under a HUD program or activity may not engage in inherently religious activities, such as worship, religious instruction, or proselytization, as part of the programs or services directly funded under the HUD program or activity. If an organization conducts such activities, the activities must be offered separately, in time or location, from the programs,

activities, or services supported by direct HUD funds, and participation must be voluntary for the beneficiaries of these programs, activities, or services.

As used in this final rule, the term "direct HUD funds" refers to direct funding within the meaning of the Establishment Clause of the First Amendment. For example, direct HUD funding may mean that the government or an intermediate organization with similar duties as a governmental entity under a particular HUD program selects an organization and purchases the needed services straight from the organization (*e.g.*, via a contract or cooperative agreement). In contrast, indirect funding scenarios may place the choice of service provider in the hands of a beneficiary, and then pay for the cost of that service through a voucher, certificate, or other similar means of payment.

C. Independence of Faith-Based Organizations

New § 5.109 clarifies that a faith-based organization that participates in a HUD program or activity will retain its independence from Federal, State, and local governments, and may continue to carry out its mission, including the definition, practice, and expression of its religious beliefs, provided that it does not engage in any inherently religious activities, such as worship, religious instruction, or proselytization, as part of the programs or services supported by direct HUD funds. Among other things, faith-based organizations may use space in their facilities to provide services under a HUD program, without removing religious art, icons, scriptures, or other religious symbols. In addition, a faith-based organization participating in a HUD program retains its authority over its internal governance, and it may retain religious terms in its organization's name, select its board members and otherwise govern itself on a religious basis, and include religious references in its organization's mission statements and other governing documents.

D. Exemption From Title VII Employment Discrimination Requirements

This final rule clarifies that a faith-based organization's exemption from the Federal prohibition on employment discrimination on the basis of religion, set forth in section 702(a) of the Civil Rights Act of 1964 (42 U.S.C. 2000e-1), is not forfeited when the organization participates in a HUD program. Some HUD programs, however, contain independent statutory provisions that impose certain nondiscrimination

requirements on all grantees. Accordingly, grantees should consult with the appropriate Department program office to determine the scope of any applicable requirements.

E. Nondiscrimination Requirements

This final rule clarifies that an organization that receives direct HUD funds shall not, in providing program assistance, discriminate against a program beneficiary or prospective program beneficiary on the basis of religion or religious belief. Organizations participating in HUD programs and activities must also comply with any other applicable Federal fair housing and nondiscrimination requirements.

F. Acquisition, Construction, and Rehabilitation of Structures

HUD funds may not be used for the acquisition, construction, or rehabilitation of structures to the extent that those structures are used for inherently religious activities. HUD funds may be used for the acquisition, construction, or rehabilitation of structures only to the extent that those structures are used for conducting eligible activities under a HUD program or activity. Where a structure is used for both eligible and inherently religious activities, HUD funds may not exceed the cost of those portions of the acquisition, construction, or rehabilitation that are attributable to eligible activities in accordance with the cost accounting requirements applicable to the HUD program or activity. Sanctuaries, chapels, and other rooms that a HUD-funded religious congregation uses as its principal place of worship, however, are ineligible for HUD-funded improvements. Disposition of real property after use for the authorized purpose, or any change in use of the property for the authorized purpose, is subject to government-wide regulations governing real property disposition (*see, e.g.*, 24 CFR parts 84 and 85).

G. Commingling of Federal and State and Local Funds

This final rule clarifies that if a State or local government voluntarily contributes its own funds to supplement federally funded activities, the state or local government has the option to segregate the Federal funds or commingle them. However, if the funds are commingled, the requirements of new § 5.109 will apply to all of the commingled funds. If a state or local government is required to contribute matching funds to supplement a Federally funded activity, the matching

funds are considered commingled with the Federal assistance and therefore subject to the requirements of new § 5.109. Some HUD program requirements govern any project or activity assisted under those programs. Accordingly, grantees should consult with the appropriate HUD program office to determine the scope of applicable requirements.

IV. Discussion of the Public Comments on the March 3, 2004, Proposed Rule

The public comment period on the March 3, 2004, proposed rule closed on May 3, 2004. HUD received eight comments on the proposed rule. Comments were received from private individuals as well as from organizations concerned with civil rights, church-state, and free speech issues. This section of the preamble presents a summary of the significant issues raised by the public comments on the March 3, 2004, proposed rule and HUD's responses to these issues.

A. General Comments

Comment: Support for proposed rule. Two commenters expressed general support for the proposed rule, applauding both the goals of the rule and the specific proposed regulatory changes.

HUD Response. HUD appreciates the support of the commenters. HUD agrees that the final rule will clarify the Department's policy regarding the participation of faith-based organizations in HUD programs and activities. As noted earlier, after careful consideration of the public comments on the proposed rule, HUD has decided to adopt the proposed rule without changes.

Comment: Opposition to rule on constitutional grounds. Several commenters expressed concern that the proposed regulatory changes would conflict with the Establishment Clause and related Supreme Court decisions. Some of the commenters wrote that the rule impermissibly would authorize Federal funding for churches and other "pervasively sectarian organizations." Other commenters were concerned that the regulatory changes would lead to excessive entanglement between the Federal government and religious institutions.

HUD Response. HUD does not agree with these comments. As more fully discussed in the responses to the individual comments below, HUD believes that the policies and procedures contained in this final rule are fully within the bounds of constitutional church-state guidelines and consistent with recent Supreme

Court decisions concerning the Establishment Clause.

Comment: Ensure the availability of secular alternative service providers. Several commenters wrote that HUD should ensure that beneficiaries have the ability to receive services from a different or non-religious provider. The commenters wrote that without reasonable secular alternatives, beneficiaries might be forced to participate in programs provided by faith-based organizations where they may be required to participate in religious activity in order to receive essential government-funded benefits.

HUD Response. HUD has not revised the rule in response to these comments. Under this final rule, directly funded religious organizations are prohibited from discriminating against program beneficiaries on the basis of "religion or religious belief." In addition, the rule provides that religious organizations may not use direct funding from HUD for inherently religious activities, that such activities must be offered separately, in time or location, from services directly funded by HUD, and that no beneficiary served by a HUD-funded provider directly funded by HUD will be required to participate in inherently religious activities as a condition of receiving services. These requirements sufficiently protect the rights of program beneficiaries. Moreover, HUD's general objective is to eliminate barriers to faith-based organizations, to welcome their participation in HUD programs, and most important, to ensure they are treated like other program participants. The commenters' recommendations run counter to the objectives that HUD is trying to achieve through this rule. To prevent a faith-based organization from providing HUD-funded programs or services unless there is a secular organization also providing the same programs or services would defeat the "neutrality" objective sought by this rulemaking.

Comment: Rule fails to establish adequate safeguards for indirect Federal funding of faith-based organizations.

Three commenters wrote that the rule lacks regulatory safeguards to ensure that indirect HUD funding to faith-based organizations is not used inappropriately. One of the commenters wrote that the rule, in effect, establishes a mechanism for the provision of vouchers without meeting the requirements established by the Supreme Court for such programs (e.g., that the program be completely neutral with respect to religion, that use of the vouchers at a religious institution be a wholly genuine and independent

private choice, and that the voucher programs not provide incentives to choose a religious institution over a non-religious one, etc.). Other commenters were primarily concerned that the prohibition on discriminating against a program beneficiary on the basis of religious belief applies solely to direct HUD funds. These commenters wrote that the nondiscrimination requirements should be valid whether the funding is direct or indirect.

HUD Response. HUD has not revised the rule in response to these comments. Any HUD-funded programs that involve indirect funding must, of course, comply with Federal law (including current legal precedent), and nothing in the proposed regulation provides otherwise. As explained in the preamble of the proposed rule as well as the preamble of the final rule, the term "direct HUD funds" refers to direct funding within the meaning of the Establishment Clause of the First Amendment. In other words, HUD's use of the phrase "direct funding" in this rule incorporates current First Amendment jurisprudence into its definition. For example, direct HUD funding may mean that the government or an intermediate organization with similar duties as a governmental entity under a particular HUD program selects an organization and purchases the needed services straight from the organization (e.g., via a contract or cooperative agreement). In contrast, indirect funding scenarios may place the choice of service provider in the hands of a beneficiary, and then pay for the cost of that service through a voucher, certificate, or other similar means of payment.

HUD believes that, under current precedent, faith-based organizations that receive HUD funds as the result of the genuine and independent choice of a beneficiary (for example, where the entity administering HUD funds established a voucher, coupon, certificate, or similar funding mechanism) are permitted to offer assistance that integrates religion and social services and requires participation in all aspects of their programs. The religious freedom of beneficiaries in an indirect funding program is protected by the guarantee of genuine and independent private choice. A beneficiary has the right to select any eligible provider, and no beneficiary may be required to receive services from a provider to which the beneficiary has a religious objection. In other words, vouchers for services funded by the government must be available to eligible beneficiaries regardless of their religious belief, and

those who object to a religious provider may select an eligible alternative provider.

Finally, HUD notes that this final rule does not modify any statutory nondiscrimination requirements for HUD programs covered by the rule. To the extent that such requirements restrict the activities of indirectly funded organizations, those restrictions remain in effect. Accordingly, the statute that applies to each program should be reviewed for the scope of its applicability.

Comment: Rule should provide for stricter monitoring and enforcement. Several commenters wrote that the rule fails to provide for any oversight mechanisms or "firewalls" to prevent the religious use of government funds. The commenters wrote that the rule should require faith-based organizations to regularly account for the expenditures of funds and to undergo regular audits.

HUD Response. HUD has not revised the rule in response to these comments. HUD has a responsibility to monitor all program participants to ensure that HUD funds are used in accordance with HUD program and any governmentwide requirements. Inappropriate use of HUD funds or failure to comply with HUD requirements is not a possibility that arises only when program participants are faith-based organizations. Failure of any organization receiving Federal funds to ensure that the Federal portion of their funding is not used for prohibited purposes will subject the organization to the imposition of sanctions or penalties. All HUD program participants must carefully manage their various sources of Federal funds and abide by Office of Management and Budget (OMB) cost accounting circulars, where applicable, or other cost accounting methods that may be specified in individual program regulations. These existing procedures, therefore, more than suffice to address the concerns raised by the commenters.

Comment: The regulatory restrictions should not apply to non-financial assistance. One commenter expressed concern about the HUD programs covered by the rule, which included the "full range of HUD programs and activities, including programs that make funds available through contracts, grants, cooperative agreements, or other instruments for eligible goods, services, and activities, and programs that do not make funds available, but involve other forms of benefit or resources" (69 FR 10127, first column). The commenter expressed concern that application of all applicable regulatory requirements

would place non-financial assistance under quite restrictive requirements.

HUD Response. HUD believes that the commenter has misunderstood the rule in part. Certain portions of the rule apply to all who "participate in HUD's programs and activities," while others apply more narrowly to organizations that receive direct HUD funds. For example, religious organizations are eligible, on the same basis as any other organization, to participate in HUD's programs and activities. Therefore, in administering HUD-supported financial and non-financial assistance, neither the Federal government nor a State government, local government, or other entity administering a HUD program or activity can discriminate against an organization on the basis of the organization's religious character or affiliation. In contrast, the restriction on inherently religious activities is limited to programs that receive direct HUD funds. Certain forms of non-financial assistance, such as HUD-supported mortgage insurance, do not fall within the definition of direct HUD funds. HUD, therefore, does not believe that further clarification in the regulatory text is needed.

B. Comments Regarding Employment and Non-Discrimination Provisions

Comment: Comments regarding the Title VII exemption. One commenter expressed support for the regulatory provision regarding the employment nondiscrimination exemption provided in Title VII of the Civil Rights Act of 1964. However, the commenter requested that HUD provide more specific guidance on how faith-based organizations may preserve their employment exemption, notwithstanding program-specific requirements. Other commenters questioned whether a faith-based organization retains its Title VII exemption after receipt of Federal funds. The commenters wrote that the exemption from Title VII was never intended to provide the basis for government-funded discrimination, and expressed concern that the rule will result in illegal employment discrimination.

HUD Response. As noted above in this preamble, this final rule clarifies that a faith-based organization's exemption from the Federal prohibition on employment discrimination on the basis of religion, set forth in section 702(a) of Title VII of the Civil Rights Act of 1964, is not forfeited when the organization participates in a HUD program. HUD believes that faith-based organizations should retain their fundamental civil rights, including their

ability to take faith into account when they make employment decisions without running afoul of Title VII. Title VII recognizes that for a faith-based organization to define or carry out its mission, it must be able to choose its employees based on its vision and beliefs. Some HUD programs, however, contain independent statutory provisions that impose certain nondiscrimination requirements on all grantees. Accordingly, grantees should consult with the appropriate Department program office to determine the scope of any applicable requirements.

Comment: Rule should provide for applicability of State and local nondiscrimination requirements. Several commenters wrote that the proposed rule did not make clear that State and local civil rights laws continue to apply to organizations providing federally funded programs and activities. The commenters urged that the final rule should explicitly preserve the application of state and local nondiscrimination laws, particularly those concerning employment discrimination. However, a commenter writing in support of the Title VII exemption expressed a contrary view. This commenter requested that the final rule explicitly preempt any conflicting State or local restrictions on religious staffing when HUD funds are commingled with State or local funds.

HUD Response. The requirements that govern funding under the HUD programs at issue in these regulations do not directly address preemption of State or local laws. Federal funds, however, carry Federal requirements. No organization is required to apply for funding under these programs, but organizations that apply and are selected for funding must comply with the requirements applicable to the program funds. As noted earlier, if a State or local government voluntarily contributes its own funds to supplement federally funded activities, the State or local government has the option to segregate the Federal funds or commingle them. If the funds are commingled, this regulation applies to all the commingled funds.

Comment: The nondiscrimination provisions should be strengthened by explicitly prohibiting discrimination based on sexual orientation and gender identity. One commenter made this suggestion.

HUD Response. As noted earlier, this final rule does not modify any statutory nondiscrimination requirements for the HUD programs covered by the rule. The purpose of this rule is to ensure the

equal treatment of faith-based organizations participating in HUD programs. The purpose of this rule is not to establish nondiscrimination requirements or to alter existing nondiscrimination requirements. Current requirements of applicable statutes continue to apply to the HUD programs covered by this final rule, but HUD declines to impose additional requirements by regulation.

C. Comments Regarding Inherently Religious Activities

Comment: The restrictions on inherently religious activities require clarification. One commenter requested a more expansive definition of “inherently religious activities.” The commenter wrote that while the rule defines “inherently religious activities” to include “worship, religious instruction, or proselytization,” such guidance is insufficient to ensure that grantees do not run afoul of the constitutional restrictions.

HUD Response. The final rule continues to specify that inherently religious activities include “worship, religious instruction, or proselytization.” It would be difficult to establish an acceptable list of all inherently religious activities. Inevitably, the regulatory definition would fail to include some inherently religious activities or include certain activities that are not inherently religious. Rather than attempt to establish an exhaustive regulatory definition, this final rule retains the language of the proposed rule, which provides examples of the general types of activities that are prohibited by the regulations. This approach is consistent with Supreme Court precedent, which likewise has not comprehensively defined inherently religious activities. For example, prayer and worship are inherently religious, but social services do not become inherently religious merely because they are conducted by individuals who are religiously motivated to undertake them or view the activities as a form of ministry. If HUD determines that additional guidance is needed regarding specific activities that are “inherently religious,” HUD will provide this guidance.

Comment: Clarify the term “separation in time or location.” One commenter requested that HUD clarify the separation “in time or location” restriction. The commenter wrote that the vagueness of the current language would lead to confusion among service providers. The commenter suggested that specifying that religious activities must be separated by both time and location could provide greater clarity.

HUD Response. HUD declines to adopt the suggestion made by the commenter. HUD does not agree that the separation of time or location requirement is ambiguous or necessitates the need for additional regulation for proper adherence. HUD believes that existing regulations and this rule are clear that faith-based organizations using direct Federal funds for certain activities must separate their inherently religious activities from the federally funded activities. HUD believes that a common sense approach to this regulation supported by HUD guidance, not a detailed regulatory approach, is the better one. HUD believes that requiring that inherently religious activities be separated from HUD-funded activities by both time and location is legally unnecessary. Further, such a requirement would impose an unnecessarily harsh burden on small faith-based organizations, which may have access to only one suitable location for the provision of HUD-funded services.

Comment: The requirement regarding “separation in time or location” fails to meet constitutional standards. One commenter wrote that the “time or location” restriction applies solely to inherently religious activities. According to the commenter, this seems to suggest that religious activity that is not inherently religious is permissible during the provision of HUD-funded programs or services. The commenter wrote that this is misleading and fails to meet the current constitutional standard, which requires that no government funds be diverted to religious indoctrination.

HUD Response. HUD has not revised the rule in response to this comment. The final rule, consistent with Supreme Court decisions interpreting the First Amendment to the Constitution, is clear that faith-based organizations using direct Federal funds must separate their inherently religious activities from the federally funded activities. However, prohibiting any and all references to religion or religious belief is legally unnecessary. As to the commenter’s suggestion that the regulation should more clearly prohibit the use of government funds for religious indoctrination, HUD believes that the language of the proposed rule, which HUD has decided to retain, adequately addresses this concern. The rule provides examples of the general types of activities that are prohibited by the regulations: worship, religious instruction, and proselytizing. As to the commenter’s suggestion that all “religious activity” must be separate from HUD-funded services, HUD notes

that some religious organizations view the very provision of social services as a “religious” activity. HUD-funded services, however, do not become impermissibly religious merely because they are conducted by individuals who are religiously motivated to undertake them or view them as a form of “ministry.” HUD believes that its approach is consistent with Supreme Court precedent.

D. Comments Regarding Other Rule Provisions

Comment: The rule should prohibit the display of religious art or iconography. Two commenters made this suggestion. The commenters wrote that the rule fails to recognize that proselytization, religious instruction, and worship can occur through art, icons, and images. Further, the commenters were concerned that the symbols might create a pervasively sectarian atmosphere in which members of a different religion may not feel comfortable or welcome.

HUD Response. HUD declines to impose this restriction on HUD program participants that are faith-based organizations. A number of Federal statutes affirm the principle embodied in this rule (*see e.g.*, 42 U.S.C. 290kk–1(d)(2)(B)). For no other program participants do HUD regulations prescribe the type of artwork, statues, or icons that may be placed within or without the structures in which HUD-funded services are provided. A prohibition on the use of religious icons would make it more difficult for many faith-based organizations to participate in the program than other organizations, and would thus be an inappropriate and excessive restriction.

Comment: The proposed rule allows the misuse of HUD funds to build structures used for religious purposes. Several commenters objected to the use of HUD funds in the acquisition, construction, or rehabilitation of religious structures. The commenters wrote that the provisions are contrary to Supreme Court decisions that prohibit spending government funds on structures that are not exclusively secular in their use. The commenters wrote that the “attribution” requirements are vague and that HUD will need to establish effective safeguards to avoid the perceived constitutional pitfalls.

HUD Response. HUD has not revised the rule in response to these comments. HUD believes that the prorated funding of improvements to a structure that has a mixed use—both religious and nonreligious—is not itself a violation of the Constitution. In a neutral program in

which the government directly funds the capital improvements of institutions that administer Federal social welfare programs, the government need only put in place safeguards to ensure that public money is not used to finance inherently religious activities. Therefore, the final rule's prohibition on the funding of capital improvements for sanctuaries, chapels, or any other rooms that a religious congregation uses as its principal place of worship simply provides extra assurance that HUD-funded capital improvements will not be used to support inherently religious activities, and HUD's rule is well within the bounds of the Constitution.

V. Findings and Certifications

Regulatory Planning and Review

The Office of Management and Budget (OMB) reviewed this rule under Executive Order 12866 (entitled "Regulatory Planning and Review"). OMB determined that this rule is a "significant regulatory action" as defined in section 3(f) of the Order (although not an economically significant action, as provided under section 3(f)(1) of the Order). Any changes made to the rule subsequent to its submission to OMB are identified in the docket file, which is available for public inspection in the Regulations Division, Room 10276, Office of General Counsel, Department of Housing and Urban Development, 451 Seventh Street, SW., Washington, DC 20410-0500.

Regulatory Flexibility Act

The Secretary, in accordance with the Regulatory Flexibility Act (5 U.S.C. 605(b)) has reviewed and approved this final rule and in so doing certifies that this rule will not have a significant economic impact on a substantial number of small entities. The final rule will not impose any new costs, or modify existing costs, applicable to HUD grantees. Rather, the purpose of the final rule is to ensure the equal participation of faith-based organizations (irrespective of size) in HUD's programs.

Environmental Impact

This final rule sets forth nondiscrimination standards. Accordingly, under 24 CFR 50.19(c)(3), this final rule is categorically excluded from environmental review under the National Environmental Policy Act of 1969 (42 U.S.C. 4332).

Unfunded Mandates Reform Act

Title II of the Unfunded Mandates Reform Act of 1995 (UMRA) (2 U.S.C. 1531-1538) establishes requirements for Federal agencies to assess the effects of

their regulatory actions on State, local, and tribal governments and the private sector. This final rule does not impose any Federal mandate on State, local, or tribal government or the private sector within the meaning of UMRA.

Executive Order 13132, Federalism

Executive Order 13132 (entitled "Federalism") prohibits, to the extent practicable and permitted by law, an agency from promulgating a regulation that has Federalism implications and either imposes substantial direct compliance costs on State and local governments and is not required by statute or preempts state law, unless the relevant requirements of section 6 of the Executive Order are met. Consistent with the consultation requirements of the Executive Order, HUD specifically solicited comment from State and local government officials on the March 3, 2004, proposed rule, but received no such comments. This final rule does not impose substantial direct costs on State or local governments and therefore does not have Federalism implications under this Executive Order.

Catalog of Federal Domestic Assistance Numbers

The regulatory amendments contained in this final rule apply to all HUD assistance programs for which faith-based organizations are eligible to participate. The Catalog of Federal Domestic Assistance number for a particular HUD program may be found on the CFDA Web site at: <http://www.cfda.gov>.

List of Subjects

24 CFR Part 5

Administrative practice and procedure, Aged, Claims, Drug abuse, Drug traffic control, Grant programs—housing and community development, Grant programs—Indians, Individuals with disabilities, Loan programs—housing and community development, Low and moderate income housing, Mortgage insurance, Pets, Public housing, Rent subsidies, Reporting and recordkeeping requirements.

24 CFR Part 570

Administrative practice and procedure, American Samoa, Community development block grants, Grant programs—education, Grant programs—housing and community development, Guam, Indians, Loan programs—housing and community development, Low and moderate income housing, Northern Mariana Islands, Pacific Islands Trust Territory, Puerto Rico, Reporting and

recordkeeping requirements, Student aid, Virgin Islands.

■ Accordingly, for the reasons described in the preamble, HUD amends 24 CFR parts 5 and 570 as follows:

PART 5—GENERAL HUD PROGRAM REQUIREMENTS; WAIVERS

■ 1. The authority citation for 24 CFR part 5 continues to read as follows:

Authority: 42 U.S.C. 3535(d), unless otherwise noted.

■ 2. Add § 5.109 to read as follows:

§ 5.109 Equal Participation of Religious Organizations in HUD Programs and Activities.

(a) *Purpose.* Consistent with Executive Order 13279 (issued on December 12, 2002, 67 FR 77141, 3 CFR, 2002 Comp., p. 258), entitled "Equal Protection of the Laws for Faith-Based and Community Organizations," this section describes HUD's policy for the equal participation of religious organizations in HUD's programs and activities. The equal participation policies and requirements contained in this section are generally applicable to religious organizations in all HUD programs and activities. More specific policies and requirements regarding the participation of religious organizations in individual HUD programs may be provided in the regulations for those programs.

(b) *Equal participation of religious organizations in HUD programs and activities.* Religious organizations are eligible, on the same basis as any other organization, to participate in HUD's programs and activities. Neither the Federal government, nor a State or local government, nor any other entity that administers any HUD program or activity shall discriminate against an organization on the basis of the organization's religious character or affiliation.

(c) *Inherently religious activities.* Organizations that receive direct HUD funds under a HUD program or activity may not engage in inherently religious activities, such as worship, religious instruction, or proselytization, as part of the programs or services funded under a HUD program or activity. If an organization conducts such inherently religious activities, the inherently religious activities must be offered separately, in time or location, from the programs, activities, or services supported by direct HUD funds and participation must be voluntary for the beneficiaries of the programs, activities or services provided under the HUD program.

(d) *Independence of religious organizations.* A religious organization that participates in a HUD program or activity will retain its independence from Federal, State, and local governments, and may continue to carry out its mission, including the definition, practice, and expression of its religious beliefs, provided that it does not engage in any inherently religious activities, such as worship, religious instruction, or proselytization as part of the programs or services supported by direct HUD funds. Among other things, religious organizations may use space in their facilities to provide services under a HUD program without removing religious art, icons, scriptures, or other religious symbols. In addition, a religious organization participating in a HUD program retains its authority over its internal governance, and it may retain religious terms in its organization's name, select its board members on a religious basis, and include religious references in its organization's mission statements and other governing documents.

(e) *Exemption from Title VII employment discrimination requirements.* A religious organization's exemption from the Federal prohibition on employment discrimination on the basis of religion, set forth in section 702(a) of the Civil Rights Act of 1964 (42 U.S.C. 2000e-1), is not forfeited when the organization participates in a HUD program. Some HUD programs, however, contain independent statutory provisions that impose certain nondiscrimination requirements on all grantees. Accordingly, grantees should consult with the appropriate HUD

program office to determine the scope of applicable requirements.

(f) *Nondiscrimination requirements.* An organization that receives direct HUD funds shall not, in providing program assistance, discriminate against a program beneficiary or prospective program beneficiary on the basis of religion or religious belief.

(g) *Acquisition, construction, and rehabilitation of structures.* HUD funds may not be used for the acquisition, construction, or rehabilitation of structures to the extent that those structures are used for inherently religious activities. HUD funds may be used for the acquisition, construction, or rehabilitation of structures only to the extent that those structures are used for conducting eligible activities under a HUD program or activity. Where a structure is used for both eligible and inherently religious activities, HUD funds may not exceed the cost of those portions of the acquisition, construction, or rehabilitation that are attributable to eligible activities in accordance with the cost accounting requirements applicable to the HUD program or activity. Sanctuaries, chapels, and other rooms that a HUD-funded religious congregation uses as its principal place of worship, however, are ineligible for HUD-funded improvements. Disposition of real property after use for the authorized purpose, or any change in use of the property from the authorized purpose, is subject to governmentwide regulations governing real property disposition (*see, e.g.,* 24 CFR parts 84 and 85).

(h) *Commingling of Federal and State and local funds.* If a state or local

government voluntarily contributes its own funds to supplement Federally funded activities, the State or local government has the option to segregate the Federal funds or commingle them. However, if the funds are commingled, the requirements of this section apply to all of the commingled funds. Further, if a State or local government is required to contribute matching funds to supplement a Federally funded activity, the matching funds are considered commingled with the Federal assistance and therefore subject to the requirements of this section. Some HUD programs' requirements govern any project or activity assisted under those programs. Accordingly, grantees should consult with the appropriate HUD program office to determine the scope of applicable requirements.

PART 570—COMMUNITY DEVELOPMENT BLOCK GRANTS

■ 3. The authority citation for 24 CFR part 570 continues to read as follows:

Authority: 42 U.S.C. 3535(d) and 5301-5320.

■ 4. Add § 570.480(e) to read as follows:

§ 570.480 General.

* * * * *

(e) Religious organizations are eligible to participate under the State CDBG Program as provided in § 570.200(j).

Dated: July 6, 2004.

Alphonso Jackson,
Secretary.

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