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DOCUMENT RESUME

00550 - [A1051859]

[Department of Housing and Urban Development's Review of Basic Homes Program]. CED-77-52; B-114860. April 1, 1977. Released April 4, 1977. 2 pp. + enclosure (14 pp.).

Report to Sen. Lee Metcalf; by Elmer B. Staats, Comptroller General.

Issue Area: Domestic Housing and Community Development: Housing for Low and Moderate Income Families (2101).

Contact: Community and Economic Development Div.

Budget Function: Community and Regional Development: Community Development (451).

Organization Concerned: Department of Housing and Urban Development; Department of Agriculture; Battelle Memorial Inst.; Columbus Labs., OH.

Congressional Relevance: Sen. Lee Metcalf.

The Department of Housing and Urban Development's (HUD) Basic Homes Program was intended to determine whether low cost basic homes can be built which are acceptable to the rural poor. Battelle Columbus Laboratories was selected as the prime contractor for the program. Findings/Conclusions: Program funds have not been used to construct demonstration housing units as originally planned. Program emphasis has changed in terms of designs and types of homes to be built, and the program might ultimately benefit people with higher incomes than originally planned. The Advisory Committee, composed of various interest groups, has been critical of the program and its administration. An organization such as Battelle was needed to manage the day-to-day operations of the program. Battelle itself felt it necessary to subcontract with several consultants to do specific analyses. The future of the program is uncertain, and after additional analyses, a decision on whether to continue or kill the program will be made. (Author/DJM)

COMPTROLLER GENERAL OF THE UNITED STATES
WASHINGTON, D.C. 20548

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APR 1 1977

The Honorable Lee Metcalf
United States Senate

Dear Senator Metcalf:

Your letter of May 28, 1976, asked us to study the Department of Housing and Urban Development's Basic Homes Program. Our study was directed to the issues raised in your letter, primarily the (1) use of program funds, (2) changing program emphasis, (3) use of the Advisory Committee, and (4) need for Battelle Columbus Laboratories and several other consultants to be involved in the program.

We examined records and talked to officials at Department headquarters in Washington, D.C., who are responsible for the program. We also talked to the program manager for Battelle Columbus Laboratories because Battelle is the grantee responsible for providing the day-to-day management and technical support services in implementation of the program.

The results of our review are contained in the enclosure to this letter. To summarize, we found that:

- Program funds have not been used to construct demonstration housing units as originally planned.
- Emphasis of the program has changed in terms of designs and types of houses to be built. Also, concern has been expressed that the program might ultimately benefit a population with higher incomes than originally anticipated.
- The Advisory Committee, composed of various interest groups, has been critical of the program and its administration. While the Department has not always taken action to satisfy this criticism, there is evidence which shows the Department's concern and regard for the criticism. The Department recently met with several committee members and told them of the status of the program. Concerns about the program were shared,

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and the Department agreed to provide the members with prototype drawings for their evaluation.

--According to Department officials, an organization such as Battelle was needed by the Office of Economic Opportunity, and later by the Department, to manage the day-to-day operations of the program. Because of its own staffing or technical limitations, Battelle has subcontracted with several consultants during the program to accomplish specific tasks.

--The future of the program is uncertain. Department officials told us that a decision to continue or terminate the program will be made within the next several months after additional analyses.

As your office requested, we did not submit this report to the Department for formal review and comment. Its contents, however, were reviewed and discussed with key agency officials who are responsible for administering the program, and their comments were incorporated where appropriate. Its contents were also reviewed by the Battelle program manager who furnished his comments to the Department.

Sincerely yours



Comptroller General
of the United States

Enclosure

DEPARTMENT OF HOUSING AND URBAN DEVELOPMENTBASIC HOMES PROGRAMBACKGROUND

The Basic Homes Program was begun by the Office of Economic Opportunity in early 1972. It was transferred to the Department of Housing and Urban Development as a result of the Office's demise in May 1973. Although the program concerns rural housing, it was not transferred to the Farmers Home Administration of the Department of Agriculture because Farmers Home lacked the research capability necessary for the program.

The primary purpose of the program was to determine whether low-cost basic homes can be built which are affordable and acceptable to the rural poor. A basic home has been defined within the program as falling between the Census Bureau definition of standard (i.e., a structurally sound house with interior plumbing, hot and cold running water, and electricity) and Minimum Property Standards accepted by the Department of Housing and Urban Development and the Farmers Home Administration. It was anticipated that in building a basic home, certain standards and local zoning and building codes may be modified and perhaps waived.

An acceptable home is one which low-income rural families will buy and occupy. An affordable home, as defined initially, was one for which the Office of Economic Opportunity target population (e.g., a family of four with an income of \$4,000 annually) could afford to pay 20 percent of their income.

Battelle Columbus Laboratories of Columbus, Ohio, was selected by the Office of Economic Opportunity in June 1972 as the prime contractor for the program. The Battelle organization was selected over three others because, among other things, it is large and has had experience in managing complex research and demonstration programs. An initial grant of \$4.7 million was awarded by the Office of Economic Opportunity to Battelle for their management and technical support of the program and for the development and construction of prototype and demonstration housing units.

The program, as originally conceived, was divided into three phases. Phase I was to be a research, planning, and design effort. Battelle's responsibilities were to include participating with the Office of Economic Opportunity in the selection of eight planning subcontractors for this phase who were each to develop a survey of housing needs and preferences of rural families; a local housing market

analysis; a minimum of four design concepts; and drawings, specifications, and cost estimates for each design concept.

Battelle was to evaluate the submissions of the planning subcontractors in terms of program goals and with the Office of Economic Opportunity, select four construction subcontractors to participate in Phase II. Phase II was to include screening families who wanted to participate in the program, land acquisition, preparation of site plans, purchase of materials, and construction of both prototype and demonstration housing units. The demonstration units were to be sold to rural home buyers. They were to be built to order based on the home buyer's selection from the prototypes constructed in his or her particular geographical area. Battelle was to provide construction supervision, including payment of the construction subcontractors and material suppliers. Battelle also was to provide postoccupancy family counseling.

During the planning and construction phases, Battelle was to monitor the performance of the subcontractors and provide technical assistance to them. Also, its job was to evaluate the acceptance by rural home buyers of the prototype units and to determine how well the subcontractors had met cost goals.

In Phase III, the results of the program were to be implemented. Battelle's role was to provide technical advisory assistance and to help in disseminating the results of the program. It was anticipated that the final product of the program would be plans and specifications for acceptable basic homes which were to be endorsed and made available by the Department of Housing and Urban Development to builders and prospective homeowners in rural areas throughout the United States.

In addition to awarding the grant to Battelle, early in the program, the Office of Economic Opportunity also created an Advisory Committee consisting of various organizations which were concerned directly or indirectly with the housing needs of the rural poor. Although the committee's role and responsibilities were not specified, the original grant document between the Office of Economic Opportunity and Battelle stated that it would participate in the selection of the Phase I subcontractors "and other funding decisions."

Upon transfer of the program from the Office of Economic Opportunity to the Department of Housing and Urban Development in 1973, one of the Department's first acts was to perform a budget and work evaluation of the program. The Department determined that in addition to the design and construction of

low-cost housing, the program needed to develop, demonstrate, and evaluate methods of delivering (including marketing and financing) the houses to rural families. Actually, the development of a delivery system had been one of the program's stated goals from the start. Department officials told us that when the Department assumed the program, this particular goal was more clearly defined and given much more emphasis. The Department's evaluation also showed that certain costs relating to the construction of prototype units and costs for construction inspection and warranty enforcement had not been considered. To cover these unanticipated costs, the Department increased the grant to Battelle in June 1974 by \$200,000, increasing its total to \$4.9 million. In January 1977, this total remained unchanged.

USE OF PROGRAM FUNDS

The \$4.9 million in program funds have not been used in accordance with the original plan. The Department's determination that there was a need in the program to develop, demonstrate, and evaluate methods of delivering basic homes to rural families, and the changes which ensued, have rendered the program incapable of producing the up to 400 demonstration units which were initially planned. The only units produced as of November 1, 1976, were 39 prototype units which, as planned, were to be used as "model homes" during the demonstration phase of the program.

In Battelle's request for proposal dated September 1, 1972, which was furnished to prospective Phase I subcontractors, the goals of the Basic Homes Program were listed as follows:

- To develop basic homes acceptable and affordable to low-income rural families.
- To encourage the linking of public and private organizations capable of providing a complete housing delivery system to low-income rural families on a large scale.
- To assess the acceptance of proposed design concepts in a relatively large-scale experimental effort.
- To disseminate information and encourage utilization of the results of the program.

The request for proposal also stated that:

"The program will involve the design and construction of up to 100 experimental housing units in each of four geographic areas of the United States. To determine the variable needs and preferences and to determine the acceptability of the proposed design concepts relative to low-income rural families, two of the four program sites will be located in the South, one in the Southwest, and one in the North. The design of the experimental housing units will be based on a pre-design market assessment of the needs and preferences of low-income rural families and their evaluation of full-scale prototype units. Cost reductions will be sought through the development of design amenities more appropriate to the needs and payment ability of the rural poor than [are] now permitted by existing local codes or by * * * minimum property standards. In addition, cost reductions will be sought through (a) the use of technological innovations, and (b) the use of optimum value engineering such as the reduction of overbuilt construction components."

There were 90 responses to the request for proposal. Of the prospective subcontractors responding, eight were chosen to participate in Phase I of the program although one was later dropped by the Office of Economic Opportunity after an audit disclosed major management weaknesses. Of the seven subcontractors who are participating, three are State housing agencies in Minnesota, South Carolina, and West Virginia. The other four are nonprofit organizations representing California, Oklahoma, Alabama, and New England (Maine, Vermont, and New Hampshire). Final selection of the subcontractors took place on June 28, 1973, after the Department of Housing and Urban Development had assumed responsibility for the program.

Our review disclosed only limited information regarding plans for spending the \$4.7 million initial grant. The grant document between the Office of Economic Opportunity and Battelle did, however, show the following funding breakdown:

<u>Funding activity</u>	<u>Planned time frame</u>	<u>Amount of funds</u>
Funding of grantee to signing of planning subcontracts	6/72-1/73	\$ 200,000
Planning subcontracts to selection of four construction subcontractors	1/73-10/73	600,000
Selection of construction subcontractors through prototype construction	10/73-1/74	500,000
Construction of demonstration units	1/74-6/74	<u>3,400,000</u>
Total initial grant		<u>\$4,700,000</u>

When the department took over the program in 1973, a detailed budget and work evaluation was performed. An internal Department memorandum stated that:

"Adequate funds for Battelle's role and performing tasks such as the user need study, walk-thru evaluation of the prototypes, technical support, and program evaluation were not provided for. Then Phase II was detailed out to place emphasis on the rural housing delivery systems and such things as budgeting for site and unit inspection, counseling and marketing staff, prototype land and construction, etc.

"HUD added \$200K to the grant and based on selecting four subs in Phase II estimated a Phase II subcontract amount of \$750,000 each. The seven subs in Phase I were told to develop a low-cost delivery system that would be replicable and to develop house designs. They were told to develop a delivery system including construction of prototypes that would make effective use of the \$750,000."

Apparently, at this juncture, the plan to construct up to 400 demonstration units with a portion of the \$4.9 million was abandoned.

The Phase I effort was completed by all subcontractors in September 1974. The designs and delivery systems submitted by

the subcontractors were evaluated, and the Department concluded that some of the designs were disappointing, and not one of the delivery systems and accompanying financing plans could justify full use of the \$750,000. It was the Department's opinion that the subcontractors had budgeted most of the money for financing mechanisms which were not fiscally sound and could not be used by other organizations and locations without an up-front grant. In addition, two Advisory Committee members expressed concern that the financing mechanisms which were being developed involved interest rates ranging from 7 percent to 9 percent and that families within the Office of Economic Opportunity established income guidelines could not afford to finance houses at these rates.

Because of the Department's disappointment and the fact that none of the plans justified full use of the \$750,000, it decided to fund all seven Phase I subcontractors during Phase II, rather than only four as originally planned. The Department thought that by funding all seven subcontractors, the marketability and cost of all designs could be tested, and the delivery systems could be demonstrated and evaluated on a smaller scale, in a shorter time frame, and for less money.

The decision to increase the participation in Phase II to seven subcontractors required a reduction in individual subcontract amounts from \$750,000 to an estimated \$420,000. This division of funds among seven rather than four subcontractors has been questioned by the Advisory Committee, the subcontractors, and by a Department review team on the basis that it will not permit any of the subcontractors to demonstrate their proposed financing mechanisms.

Although funds from the \$4.9 million are no longer planned for the construction of demonstration units, the decision to go with seven subcontractors increased the number of demonstration units envisioned from up to 400 units to as many as 700 (up to 100 units for each of the seven subcontractors). How these units are to be financed remains to be determined.

As of July 1976, \$3.3 million of the \$4.9 million grant money had been spent. Of this amount, the seven subcontractors had received about \$400,000 for Phase I and \$1.6 million thus far during Phase II. The cost of Battelle, including a number of consultants they have used to date, has totaled \$1.3 million. It is anticipated that the remaining \$1.6 million will be spent in such areas as the marketing and sale of the demonstration units, family counseling of the home buyers, and evaluation of the program.

As of November 1976, six of the seven subcontractors had completed 39 prototype units (these are all that they plan to build). These units are furnished and landscaped and are being evaluated by the Department in terms of the significance of departures from Minimum Property Standards. The following table represents the 39 units in terms of type and number of bedrooms.

<u>Type of unit</u>	<u>Number of bedrooms</u>	<u>Number of units</u>
Single-family	0 and 1	9
	2	10
	3	9
	4	7
	5	1
		<u>36</u>
Condominium	0, 1, and 3	<u>3</u>
Total		<u>39</u>

Prototype construction by the seventh subcontractor (West Virginia) has been delayed because of (1) land acquisition and title problems, (2) refusal by the Department to approve architectural and engineering planning proposals, and (3) a decision by the Department to prohibit further construction of 0- and 1-bedroom units which required redesign of some of the homes and the subdivision plan. As of November 1976, the West Virginia subcontractor had developed designs for five prototype units which were under review by the Department. Construction of the units is being held in abeyance until the Department completes its design review and also makes a decision regarding future direction of the program.

CHANGING PROGRAM EMPHASIS

Emphasis of the program has changed since its inception in 1972 in terms of designs and types of houses to be built. Designs of the homes developed thus far have been criticized for lacking innovativeness and cost-saving technologies. The idea of designing and building 0- and 1-bedroom homes under the program for singles; couples; or small, young families has, at the moment, been abandoned. Concern also has been expressed that the program will ultimately benefit a population with higher incomes than was originally anticipated partly because of the program's failure to produce a financing mechanism which would effectively serve the lower income rural family.

As stated previously, the purpose of the Basic Homes Program was to investigate the feasibility of developing low-cost basic homes that are affordable and acceptable by low-income rural families. These homes were to meet all requirements for health and safety but were to be free of architectural and construction overdesign. Innovation and imagination were to be used to keep the homes affordable by rural families which have adjusted gross incomes equal to or below poverty guidelines. The homes were to be basic in terms of amenities and size, and some 0- and 1-bedroom homes were contemplated.

Designs of the homes developed thus far in the program have been criticized as lacking innovativeness and, in some instances, as inferior to existing housing plans. A former Department program manager expressed disappointment in the designs, and a Department review team, assembled to evaluate the program and assess various criticisms levied against it, reported the following on January 24, 1975:

"None of the designs appear to be patently unworkable. On the other hand, none of them present striking design innovations, nor do they employ cost-saving technologies to any appreciable advantage. The cost per square foot of the Basic Homes it should be noted, does not appear to be much lower than conventional housing, economies achieved are realized mainly by reducing dwelling size."

The review team also stated that:

"* * * colleagues here at HUD and experts at Farmers Home predict that the cost of the Basic Homes will be higher than the DDC's [subcontractors] have estimated--perhaps not much lower, finally, than the standard, three bedroom Farmers Home unit. If this is true, the program will have failed to accomplish one of its major objectives."

The review team concluded, in part, that "* * * the goal of producing designs with substantial cost-saving variances from the MPS [Minimum Property Standards] seems to have been deemphasized during the program implementation."

One of the overriding concerns facing the program throughout its existence has been the problem of financing the basic homes once they are constructed. In planning the Basic Homes Program, the Office of Economic Opportunity assumed that the Farmers Home Administration's section 502 interest credit program, which reduces interest on home

purchases to as low as 1 percent, would be the main stay financing mechanism. Battelle wrote in its request for proposal of September 1, 1972, that "FmHA in Washington has given OEO a tentative commitment to assume the mortgages on the homes developed within this program--it is anticipated the majority of homes will be covered under the FmHA section 502 program * * *." The Department review team's report, mentioned earlier, indicated that Farmers Home has since denied any such commitment.

Battelle also committed itself in the request for proposal to investigate other forms of subsidies and financing techniques in the Basic Homes Program. As stated earlier, the scope of this effort was later expanded when the Department assumed responsibility for the program. The effort failed, however, which led the Department review team to conclude that:

"Battelle and its subcontractors have been unsuccessful in developing acceptable financing mechanisms for delivery of Basic Homes to the low income rural population which would improve upon FmHA 502 interest credit financing. The original target population will be served to a limited extent where 502 is utilized; other available financing plans will serve a higher income group."

To date, the Department has not enticed the Farmers Home Administration to participate in the program. Farmers Home has objected to the fact that the basic homes, in many instances, do not meet Minimum Property Standards and that 0- and 1-bedroom homes will not sustain consumer appeal. Farmers Home also claims, through its Office of General Counsel, that section 502 rural housing loans cannot be used to finance homes built under the Basic Homes Program because of the experimental nature of the program. Because of Farmers Home's opposition to 0- and 1-bedroom units, the Department does not expect to offer such units during the demonstration phase of the program. We were informed, however, that should Farmers Home later agree to provide financing for the other size units, the Department may try to persuade them to finance the smaller units at a later date.

The financing issue remains one of the program's most pivotal issues. The affordability to the rural poor of the homes developed during the program depends in great measure on the financing scheme that is ultimately used. Department officials told us that in addition to Farmers Home's section 502 program, they are also looking at several of their own

programs which they hope might offer at least a partial solution to the financing problem they now face.

ADVISORY COMMITTEE

As stated earlier, an Advisory Committee was established early in the program by the Office of Economic Opportunity. Its members include the

- National Association of Home Builders Research Foundation,
- National Association of Building Manufacturers,
- Housing Assistance Council,
- Rural Housing Alliance,
- Building Research Advisory Board,
- National Association for the Advancement of Colored People,
- American Institute of Architects,
- National Housing and Economic Development Law Project,
- National Sharecroppers Fund Incorporated, and
- National Spanish Speaking Housing Development Corporation.

Although the committee's formal role and responsibilities have never been specified, the original grant document between the Office of Economic Opportunity and Battelle did state that it would participate in the selection of the Phase I subcontractors and other funding decisions and that the Office would seek advice from the various committee members informally as needed.

Evidence obtained during our review showed that the committee had met only three or four times since its formation, and we were told by both the Battelle and Department program managers that it had last met in January 1975. Not all of the committee members have been active. Those showing the most interest have been the Housing Assistance Council, the Rural Housing Alliance, and the National Association of Home Builders Research Foundation.

Although the committee has met infrequently, Department files contained considerable correspondence between certain committee members and the Department. The Department, while not satisfying all criticisms levied against the Basic Homes Program by committee members, has responded to such criticism in its correspondence and has shown some concern and regard for the things that have been said. As an example, the Department review team referred to earlier was established in November 1974 as a result of criticism received from several members of the committee concerning Battelle's handling of the program and whether or not the original objectives of the program would be met. In a January 1975 report, the review team concluded that although there have been major problems in meeting the goals of the program, Battelle was not solely responsible for the difficulties and that replacing Battelle at that point would serve no useful purpose. The review team indicated that major program decisions affecting the overall structure and direction of the program were made jointly by the Office of Economic Opportunity, Department of Housing and Urban Development and Battelle. The team recommended that the Department assume a more aggressive role in managing and supervising the program.

In recent months there has been a continued interchange of correspondence between several committee members and the Department. The correspondence suggest that the committee may convene in the near future. The Department's program manager said that the Department had met in August 1976 with representatives of the Housing Assistance Council and the Rural Housing Alliance. During this meeting, the status of and concerns about the program were discussed. Also, the Department agreed to submit prototype drawings to the National Association of Home Builders Research Foundation for review. Representatives of the Housing Assistance Council and Rural Housing Alliance indicated that they would look to the National Association of Home Builders for an opinion on the homes.

NEED FOR BATTELLE AND
SEVERAL OTHER CONSULTANTS'
INVOLVEMENT IN PROGRAM

Battelle Columbus Laboratories was chosen early in the program by the Office of Economic Opportunity to

--undertake research and provide technical advisory support for construction of the experimental housing units,

--develop specific survey analyses and evaluations,

- work cooperatively with selected subcontractors in different parts of the country, and
- disseminate the results of the program.

Battelle was selected because of its size and experience in managing complex research and demonstration programs; its technical competence and facilities to evaluate construction design, materials, and methods; and its experience in the area of rural housing.

The Department's program manager said that involvement by an organization such as Battelle was necessary because the Office of Economic Opportunity lacked staff expertise in the housing area and was not equipped to manage the program on a day-to-day basis.

The Department, in effect, inherited Battelle at the time it assumed overall responsibility for the program. Although the Department does possess experts in the housing field, the program manager expressed doubt that the Department would have assumed day-to-day management responsibility of the program had they initiated it because of the limited full-time staff available for such a project and also because of the large amount of travel involved. The program manager also expressed his belief that the Department was committed to the contract with Battelle at the time it assumed the program.

The program manager told us that in those instances where Battelle has needed help in performing specific tasks, due to either staffing or technical limitations, it has contracted with a number of consulting firms. One of the larger efforts involved the user needs and preference survey conducted in the early stages of the program which was to determine the type of house that low-income families need, want, and will buy. Battelle subcontracted with a firm named National Analysts to help with the survey. Of the \$324,310 spent for the survey, National Analysts received \$108,781.

Social Perspectives, another consulting firm, has been involved in four subcontracts valued at about \$112,000 for work performed during both Phases I and II of the program. The work has included reviewing Phase I final reports and evaluating prototype units.

Battelle additionally subcontracted with Homer Hoyt Institute at a cost of \$45,453, to perform an independent cost analysis of the basic home prototypes. The purpose of the analysis was to determine whether homes could be built by independent builders at the same cost as the prototype

subcontractors. Homer Hoyt submitted the final results of the analysis to the Department on August 31, 1976. Battelle, in turn, submitted its interpretation of the results to the Department on November 4, 1976. Battelle concluded, in part, that basic homes

--have been designed that are significantly lower in construction costs, purchase price, and cost of ownership than owner-occupied homes being financed by Farmers Home for comparable size families in rural areas and

--are affordable by lower income rural families.

Department officials told us, however, that they are questioning Battelle's interpretation of the analysis because the comparability of houses used in the analysis is questionable and cost differences have not been adequately explained. A meeting between officials of the Department and Battelle is anticipated to discuss this situation.

As of July 1976, the cost of Battelle and the various consultants which have participated in the program was \$1.3 million. Of this amount, about \$300,000 was paid by Battelle to the consultants.

FUTURE OF THE PROGRAM

The future of the Basic Homes Program has been uncertain for some time. Those in the Department responsible for the program agreed that a decision regarding the future of the program is needed and pointed out certain ongoing functions that must be finalized before such a decision can be made. The program manager told us, for example, that a decision to go forward with or terminate the program would be based on the results of their current review of prototype drawings as well as the review of drawings performed by the National Association of Home Builders Research Foundation. We were told that the results of Homer Hoyt's cost analysis and other studies will be considered in reaching a decision and that the Advisory Committee and Farmers Home will be consulted before a final decision is made. The decision reached will also be dependent upon the Department's ability to resolve the financing issue which it continues to face. Department officials expect to make their decision concerning the future of the program within the next several months.

CONCLUSIONS

Although the Basic Homes Program is over 4 years old, the Department has not yet been successful in determining whether low-cost basic homes can be built which are affordable and acceptable to the rural poor. Designs of some homes in the program have been criticized as lacking innovation and cost-saving features other than reduced size. The conclusions reached from a study of the affordability of the homes developed in the program are being challenged by the Department on the basis that comparable housing was not used in the study and sufficient explanation of cost differences was not made. The affordability of basic homes to the rural poor is largely dependent on how they are to be financed and, yet, the financing issue remains as one of the program's major obstacles.

The acceptability of basic homes was to be determined during the demonstration phase of the program. Initially, up to 400 demonstration units were to be built to order for low-income families using designs of prototype units earlier developed. This figure was later changed to up to 700 units; however, to date, no demonstration units have been built.

The ultimate goal of the program was to produce plans and specifications for basic homes which would have been affordable and acceptable to the rural poor. These plans and specifications were to be endorsed and made available by the Department to anyone interested. In view of the fact that neither the affordability nor acceptability issue has been resolved, the program's ultimate goal seems to be in the distant future.

Department officials have told us that a decision either to go forward with or terminate the Basic Homes Program will be forthcoming within the next several months after additional analyses have been made and some current problems have been resolved.