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REPORT TO THE CONGRESS

Need For Improved Consumer Protection In Interstate Land Sales B-118754

Office of Interstate Land Sales Registration
Department of Housing and
Urban Development

**BY THE COMPTROLLER GENERAL
OF THE UNITED STATES**

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COMPTROLLER GENERAL OF THE UNITED STATES

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To the President of the Senate and the
Speaker of the House of Representatives

Our report concerns the need for improved consumer protection in interstate land sales under the interstate land sales registration program. The Department of Housing and Urban Development administers the program.

We made our review pursuant to the Budget and Accounting Act, 1921 (31 U.S.C. 53), and the Accounting and Auditing Act of 1950 (31 U.S.C. 67).

We are sending copies of this report to the Director, Office of Management and Budget, the Secretary of Housing and Urban Development, and the Governors and U.S. Senators and Representatives of the States discussed in detail in the report.

Comptroller General
of the United States

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ABBREVIATIONS

GAO General Accounting Office

HUD Department of Housing and Urban Development

D I G E S T

WHY THE REVIEW WAS MADE

To help protect the public in interstate land transactions, the Congress, in August 1968, enacted the Interstate Land Sales Full Disclosure Act, to be administered by the Department of Housing and Urban Development (HUD)

Because HUD received complaints of abuses in such transactions, GAO reviewed how HUD's Office of Interstate Land Sales Registration was carrying out its regulatory responsibilities

Background

Before selling undeveloped land to the public, developers generally must file statements of record with HUD which supply specific physical, financial, and legal facts on the land, supporting documentation, and certain certifications

Before or at the time of sale, developers must give buyers property reports disclosing all pertinent facts about the land. These reports place buyers in a better position to decide whether to buy the land and therefore must be accurate and reliable (See p 5)

In March 1972, the Secretary of HUD directed that the Office provide

"tough, meaningful regulation and effective consumer protection" in interstate land transactions. Since that time, the Office has

- Stepped up its campaign against unscrupulous land developers
- Held public hearings in 17 cities to investigate consumer complaints about abuses in land sales and to inform the public of its rights under Federal law
- Issued numerous press releases to increase public awareness of its program
- Increased its enforcement efforts against violators of the act, including initiating administrative proceedings and issuing orders suspending developers' rights to sell land (See p 9)

FINDINGS AND CONCLUSIONS

The Office had 55 full-time staff members and no field support. Therefore, it could not

- identify all land developers offering unregistered land for sale to the public (see p 11),
- effectively coordinate consumer protection activities with the States, particularly those having

regulatory programs accepted by HUD for Federal registration purposes (see p 12),

- adequately verify land developers' registration information (see p 14),
- investigate alleged significant violations of the act indicated by consumer complaints nor follow up on complaints referred to the developers (see p 21),
- take prompt enforcement action against registered developers who did not amend their statements of record and property reports (see pp 25 and 26),
- promptly investigate subdivisions which, according to GAO, may have been offering unregistered land for sale to the public (see p 26)

RECOMMENDATIONS

GAO recommends that the Secretary of HUD, to the extent practicable, decentralize the Office's regulatory activities--assigning responsibility to HUD field office personnel (See p 20)

GAO also recommends that the Secretary have the Office

- Selectively inspect subdivisions before and after registration to verify the accuracy and reliability of land developers' disclosures and to help determine the adequacy of State regulatory programs (See p 20)
- Establish working agreements with the States for exchanging information on land subdivisions and developers The agreements should

encourage joint efforts to improve the States' regulatory programs and to promote uniformity (See p 20)

- Improve followup procedures to insure that land developers respond promptly to consumer complaints referred by the Office
- Investigate alleged significant violations of the act indicated by consumer complaints
- Promptly act against developers who, contrary to law, fail to amend statements of record and property reports and who may be offering unregistered land for sale (See p 27)

AGENCY ACTIONS AND UNRESOLVED ISSUES

In commenting on GAO's draft report, HUD said that

- The Office is evaluating GAO's recommendation to establish a field staff Coordination among States and between the States and the Federal Government should provide "a regulatory presence in the field " (See p 18)
- The Office's permanent staff is budgeted to increase from 55 to 74 employees in fiscal year 1974 This projected staffing is realistic both in terms of the current restrictions on levels of Federal employment and the Office's ability to recruit, train, and effectively use more staff (See p 18)
- It disagreed with GAO's recommendation that the Office inspect subdivisions before registration, because the States can better make such inspections However,

reliance on the States requires uniform State regulations and procedures for making such inspections. Developing such uniformity will be a prime objective of the Office's attempt to coordinate State activity. (See p 19)

--Eliminating the complaint backlog is a high-priority item on the Office's agenda, as is following up complaints referred by the Office to land developers. The Office is determined to strictly and vigorously implement the existing law to educate the public in protecting itself. The Office is also going to discipline the land sales industry, when required, to reduce the number of defrauded consumers. (See p 27)

--Since March 1972, the Office has effectively used administrative sanctions against land developers who failed to comply with the law. Despite problems with staff limitations and competing priorities, this effort is expected to be even more effective in the future. When more staff members become available, they will concentrate

on improving enforcement actions. (See p 27)

GAO believes that, until HUD is reasonably satisfied that the States' inspection programs are adequate, the Federal Government must take the initiative to inspect subdivisions before as well as after registration.

GAO believes that inspections of subdivisions before registration, made on a sample basis, would assist the Office in determining whether certain data reported by land developers was accurate and would place the Office in a better position during subsequent inspections to evaluate progress or improvements made by the developer. (See p 19)

MATTERS FOR CONSIDERATION
BY THE CONGRESS

This report contains data on weaknesses in agency administration and suggestions for correction or improvement by the agency.

This information should help committees and Members of the Congress with their legislative responsibilities for the interstate land sales registration program.

CHAPTER 1

INTRODUCTION

To help protect the public, the Congress, in August 1968, enacted the Interstate Land Sales Full Disclosure Act, which was included as title XIV of the Housing and Urban Development Act of 1968 (15 U S C 1701). The act, effective April 28, 1969, provides for Federal regulation of the sale of undeveloped land to the public. Developers generally sell such land for vacation, retirement, or investment purposes. The American Land Developers Association, a trade organization representing land developers, estimated that industry sales for 1971 were \$5.5 billion.

The act, administered by the Office of Interstate Land Sales Registration, Department of Housing and Urban Development (HUD), requires land developers to give prospective buyers property reports disclosing all pertinent facts about the properties for sale. Such disclosure places the public in a better position to decide whether to buy the land. Because of the large number of subdivisions (tracts of land divided into smaller parcels) for sale in the United States and the complaints HUD was receiving on abuses in interstate land transactions, GAO reviewed how the Office was carrying out its regulatory responsibilities to protect the public.

THE INTERSTATE LAND SALES FULL DISCLOSURE ACT

Under the Interstate Land Sales Full Disclosure Act, a developer proposing to sell land to persons in States other than that in which the land is located or to sell land located in a foreign country generally must file a statement of record with HUD for each subdivision. The statement must contain specified facts concerning the physical, financial, and legal aspects of the land, supporting documentation, including maps and contract documents, and certifications on such matters as the availability of utility services and easements or other restrictions.

A land developer may not use any kind of interstate transportation or communication to sell land unless HUD has accepted his statement of record. If HUD accepts the statement, the land is registered. A statement becomes effective 30 days after filing unless the Office finds it

incomplete or inaccurate in any material respect and so notifies the developer

Developers do not always have to file statements of record with HUD. Developers can be exempted from filing, for example, when they furnish sufficient evidence to HUD that (1) the land consists of less than 50 lots, (2) lots are 5 acres or larger, or (3) there is a residential, commercial, or industrial building on the lots to be sold or the seller has contracted to erect such a building within 2 years. Certain other exemptions are permitted after a partial statement of record has been filed with and approved by HUD.

The act encourages Federal-State cooperation. In lieu of a statement of record, HUD may accept comparable information filed with and accepted by State authorities. However, developers must file with HUD certified duplicates of the information approved by the State and must pay filing fees. HUD considers information filed pursuant to the regulations of California, Florida, Hawaii, and New York to be adequate for Federal registration purposes. At the inception of the program, HUD found that these States

- required developers to give property reports to prospective land buyers,
- had laws similar in scope and effect to the Federal act, and
- had sufficient, adequately trained staffs to administer the act

A property report must be included in the statement of record. The report, in question and answer form, covers important facts buyers should know about the land, including the name and location of the developer and the subdivision, the effective date of the report, road distances to nearby communities, financial terms and refund policies, if any, mortgages and liens on the subdivision, protection, if any, afforded the buyer in case of financial default of the developer, leasing arrangements, taxes and special assessments to be paid by the buyer, escrow and title arrangements, plus any restrictions, easements, or covenants and their effect on the buyer, recreational facilities available and dates

proposed facilities are expected to be completed, availability or lack of utilities and services such as trash collection, sewers, or water supply, any need for drainage and fill before the land can be used for building, schools, medical facilities, shopping, and transportation or proposed dates when such services will be available, the number of homes occupied, and access roads

HUD regulations require that each property report display the following notice of disclaimer

"This report is not a recommendation or endorsement of the offering herein by the Office of Interstate Land Sales Registration, nor has that office made an inspection of the property nor passed upon the accuracy or adequacy of this report or any promotional or advertising materials used by the seller

"It is in the interest of the buyer * * * to inspect the property and carefully read all sale * * * documents."

The developer must give the property report to each prospective purchaser in advance or at the time of the land transaction. Failure to do so entitles a purchaser to void his contract. A purchaser may also void his contract within 48 hours after entering into a land transaction if he received the report less than 48 hours before he signed the contract. The purchaser, however, may waive the right of revocation

By law, a purchase contract may stipulate that the purchaser acknowledges and certifies by his signature that his revocation right is not applicable to the contract by virtue of the fact that, before signing the contract, he has received, read, and understood the property report and has inspected the lot HUD sponsored an amendment to the law to preclude developers from inducing buyers to waive their right of revocation and to prohibit such stipulations in sales contracts The amendment was included in the Housing and Urban Development Act of 1972, which did not pass the 92d Congress

The 1968 act authorizes HUD to bring an action in any U.S. district court to enjoin practices which violate the act, such as (1) sale of unregistered land, (2) improper disclosure in a property report, or (3) deceptive sales practices. HUD is also authorized to transmit to the Attorney General evidence concerning illegal acts or practices, so that he may initiate criminal proceedings. Willful violations of the act are punishable by a fine up to \$5,000 or imprisonment up to 5 years, or both. By law, HUD can also institute formal administrative proceedings which can lead to suspension of a developer's right to sell land covered under the act.

THE OFFICE OF INTERSTATE LAND SALES REGISTRATION

The Secretary of HUD has delegated substantially all of his authority under the act to the Interstate Land Sales Administrator, who heads the Office. The Office consists of the Examination Division and the Administrative Proceedings Division.

The Examination Division examines land developers' statements of record and property reports to determine the adequacy of their disclosures. The Division receives requests from developers for opinions on whether the Administrator will grant exemptions from filing. When the Administrator does grant an exemption, he refers his decision to HUD's Office of General Counsel to ascertain whether there are legal objections to it.

The Administrative Proceedings Division examines complaints alleging failure of developers to comply with the act. This Division determines whether violations have occurred or illegal activities are in process and develops the legal basis for initiating administrative proceedings or criminal actions against land developers.

As of December 1972, 55 full-time professional and clerical employees, augmented by 19 temporary employees and 12 consultants, were centrally administering the Office's activities from HUD headquarters in Washington, D C. HUD has not provided the Office with regional office staff.

As of November 1, 1972, about 4,400 subdivisions, located throughout the United States and in several foreign

countries, were registered with HUD HUD is authorized to charge a land developer a fee up to \$1,000 when he files a statement of record

The Office's operations are financed through a combination of appropriated funds and fees collected from developers During fiscal year 1971, about \$600,000 was appropriated to finance its activities, in fiscal year 1972, its activities were funded entirely from about \$700,000 in fees collected from land developers HUD estimates that, for fiscal year 1973 activities, the Office will need about \$1 1 million, of which about \$0 9 million will be provided from fees

In March 1972 the Secretary of HUD directed that the Office provide "tough, meaningful regulation and effective consumer protection" in interstate land transactions Since that time, the Office has

- stepped up its campaign against unscrupulous land developers,
- held public hearings in 17 cities to investigate consumer complaints and to inform the public about abuses in land sales and of its rights under Federal law, and
- issued numerous press releases to increase public awareness of the program

CHAPTER 2

NEED TO DECENTRALIZE AND EXPAND THE OFFICE'S

REGULATORY ACTIVITIES

Because of its small staff and lack of field support, the Office was not able to

- identify all land developers offering unregistered land for sale to the public,
- effectively coordinate consumer protection activities with the States, particularly those having regulatory programs accepted by HUD for Federal registration purposes, and
- adequately verify registration information filed by land developers

We visited 123 subdivisions in Arizona, California, Delaware, Florida, Maryland, North Carolina, Tennessee, and Virginia to determine their Federal registration status (We had identified these subdivisions from local newspaper advertisements, from discussions with land developers, and from records kept by State land sales authorities) We also reviewed the adequacy of property report disclosures for 102 of these subdivisions in Arizona, California, and Florida. Twenty-two, or about 18 percent, of the 123 subdivisions were not registered with or exempted from registration by HUD. Lots in these subdivisions may have been illegally offered for sale to the public.

Property reports for 5 of the 102 subdivisions visited and for 1 not visited, involving about 7,400 lots, were misleading and did not disclose pertinent information on matters such as pending litigation against a land developer, the availability of necessary utility services, and the lack of access roads to subdivision lots.

We believe the Office needs to decentralize and expand its activities to the extent practicable so it can administer the act more effectively and improve consumer protection

NEED TO IDENTIFY LAND DEVELOPERS
WHO FAIL TO REGISTER WITH HUD

The Administrator stated in June 1972 that

"there may be thousands of subdivisions throughout the Nation that are not registered with HUD and are therefore being operated in violation of the law--either intentionally or through ignorance "

Twenty-two, or about 18 percent, of the 123 subdivisions we visited were not registered or exempted from registration by HUD. Lots in these subdivisions may have been illegally offered for sale to the public. We referred these cases to the Office for investigation, and their findings are discussed on page 26

Effective regulation of land developers requires that subdivisions subject to registration requirements be identified. Unless the Office obtains the required registrations, consumers may not receive the protection intended by the property report requirement.

Our review showed that consumers who purchased land in a State other than their own generally did not inspect the land before buying. Of the approximately 650 land purchasers who responded to our questionnaire (see p 29), 469 purchased land in a State other than their own and 284, or 61 percent, indicated that they did not inspect the subdivisions before signing their contracts.

Purchasers of subdivision land who received property reports before signing their contracts had fewer problems with their purchases than those who did not receive reports. For example, 188 purchasers who responded to our questionnaire bought land after April 28, 1969, when the Interstate Land Sales Full Disclosure Act went into effect. Of these purchasers, 97 indicated that they had received property reports. Of this group, 16 percent expressed dissatisfaction with their purchases. On the other hand, of the 91 purchasers who indicated that they did not receive property reports, 54 percent expressed dissatisfaction with their purchases. This may indicate that those persons who had the benefit of the property reports were in a better position to make a prudent purchase decision.

About 47 percent of the subdivisions registered with HUD are in the popular resort States of Arizona, California, and Florida. In view of the concentration of subdivisions in States distant from Washington, D C , we believe that the Office should have field representatives close to where land is being sold to facilitate more effective regulation. Office personnel in Washington, D C , were not able to keep abreast of land developers' activities in distant States because Office personnel did not generally make onsite inspections of subdivisions (see p 16) and, as discussed below, there was little coordination with State regulatory authorities.

A HUD official told us that there were no working agreements between HUD and the States to help coordinate regulatory activities. Arizona and California officials told us that there is a need for better program coordination with HUD. California and Florida officials advised us that they notified HUD when a land developer registered land in their States. As discussed on page 6, however, a land developer registered with a State must still register with HUD and pay a Federal filing fee. Of the 22 subdivisions which were not registered with or exempted from registration by HUD, 10 were registered with California and Florida.

To identify land developers who might have been subject to registration requirements but who were not registered with HUD, the Office requested in May 1972 that HUD personnel in Washington, D C , and in HUD regional, area, and insuring offices, monitor local newspapers and submit land advertisements to the agency periodically. Office officials informed us that, although HUD personnel furnished numerous advertisements, relatively few unregistered subdivisions were identified because the advertisements were generally for subdivisions already registered.

Office officials advised us, however, that the public hearings held between May and December 1972 resulted in the identification of 40 unregistered subdivisions. The officials also said that inquiries from such sources as State regulatory agencies and professional associations had resulted in the identification of about 20 more unregistered subdivisions.

The investigative hearings held by the Office and contacts with State authorities and professional associations have been useful in identifying subdivisions which should be registered. Identifying unregistered subdivisions should not, however, depend entirely on the voluntary assistance of outside parties, such as disgruntled consumers, HUD personnel assigned responsibility in other HUD program areas, and State authorities.

If Office personnel were assigned to field locations close to where subdivisions are concentrated, they could better (1) coordinate and exchange information with State and local officials, (2) obtain local advertising and promotional material, (3) contact local financing institutions and land developers, and (4) acquire a general familiarity with local land sales activity. In our opinion, Office personnel who may be assigned to field locations and who use such techniques could identify unregistered subdivisions more easily and could better administer the Office's regulatory responsibilities.

NEED FOR VERIFICATION OF REGISTRATION
INFORMATION FILED BY LAND DEVELOPERS

Because of insufficient staff, the Office generally was not able to verify the data submitted by land developers.

Data in a developer's statement of record serves as the basis for preparing the property report. It is therefore essential that this data be accurate and reliable. A statement of record, or an amendment thereto, becomes effective 30 days after filing unless the Office finds the statement or amendment incomplete or inaccurate in any material respect and so notifies the developer.

Our visits to 102 subdivisions in Arizona, Florida, and California revealed 5 instances where disclosures in property reports were inadequate. We also noted one instance where disclosure was inadequate for a subdivision in Arizona which we did not visit.

Our findings on the adequacy of property report disclosures for subdivisions in these States follow.

Arizona

We visited 27 subdivisions in Arizona. Property reports for two of these subdivisions and for one which we did not visit, but met with the land developer, did not disclose essential data.

- A report did not disclose that the developer was a defendant in a civil action suit initiated by the local water district which charged him with illegally diverting water from the district to serve the subdivision.
- A report did not disclose that the water supply to the subdivision had been halted because of problems relating to the ownership of the water company.
- Although a report stated that there were graded roads to all lots in the subdivision, we found none. In addition, the report stated that the site's water supply would not be sufficient without the assistance of a water company to provide additional quantities

after the ground wells were exhausted. It did not indicate when this additional supply would be needed or whether the necessary arrangements had been made with a water company.

Officials of the Arizona State Real Estate Department agreed that these property reports did not fully disclose information for consumers. In the case concerning access roads, the officials stated that, after our inspection, the roads had been adequately graded. Although land developers may improve subdivisions, property reports should describe the conditions existing at subdivisions at the time such reports are made available to prospective buyers.

Florida

We visited 48 subdivisions in Florida. Property reports for two of them did not disclose essential facts which, in our opinion, could affect a potential land buyer's decision.

--A report for one subdivision stated that individual septic tanks would dispose of sewage. An official of the county in which the subdivision was located told us that the county would not consider issuing septic tank permits for lots in the subdivision until the developer submitted adequate drainage plans. At the time the property report was approved, the developer had not submitted plans which the county considered adequate. In addition, the property report failed to disclose that part of the land remained under water much of the year.

Officials of the Division of Florida Land Sales stated that, because a registered engineer had prepared the developer's drainage plans and because the facilities were to be installed by an authorized drainage district, they had assumed, when approving the property report, that the work would meet county requirements.

--A report for another subdivision indicated that individual septic tanks would dispose of sewage. A county health official stated that septic tank permits could not be issued for most of the lots because of the high water table in the area.

State officials advised us that they would contact the health department to obtain a justification for its position. The officials stated that, in this type of situation, the developer might be required to revise his property report or to stop offering the lots for sale as homesites.

California

We visited 27 subdivisions in California. We noted that a property report for one of the subdivisions did not provide essential facts. The subdivision was in an area adjacent to a large inland sea which was publicized as a prime source of recreation. According to State and Federal Government officials, however, the salt content of the sea was increasing to a degree which would eliminate marine life by 1975.

Officials of the California Department of Real Estate advised us that State property reports did not always disclose this type of information. They added, however, that, if fishing was a prime source of recreation, this matter should have been disclosed. A representative of the developer told us that many purchasers had canceled their contracts because their property values had decreased due to the increasing salinity of the sea.

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Generally the Office does not inspect subdivisions. Regulatory authorities in Arizona, California, and Florida generally require onsite inspections of subdivisions upon registration and periodically thereafter.

Office officials informed us that, short of a massive expansion of the staff, the Office could not inspect all registered subdivisions. They advised us, however, that from March to December 1972, about 100 inspections of registered subdivisions had been made--principally in States near HUD headquarters.

These inspections disclosed several violations of the law, including land offered for sale to the public illegally. The officials contended that onsite inspections were not necessarily essential before registration because subdivisions often consist of undeveloped parcels of land and any improvements to be made by land developers were still in the planning stages.

We believe that onsite inspections should be made on a sample basis, which would not require a massive expansion of the Office's staff. As each case arose, the Office could decide about visiting the subdivision, depending on the adequacy of information filed by a land developer and the adequacy of the applicable State's onsite inspection program.

By visiting a subdivision at the time of a developer's initial filing, the Office could determine whether data reported was accurate with respect to such matters as distances to nearby communities, schools, medical facilities, shopping, transportation, and the availability of roads. Such visits would enable Office representatives to meet with county officials to discuss and obtain documentation on such matters as utility services, easements, and taxes. During later inspections, the Office would be in a better position to evaluate progress or improvements made by the developer.

Inspections made after registration would permit the Office to determine whether developers are implementing their subdivision plans as provided in their property reports and would help determine the continuing effectiveness of States' programs. If the Office discovers improper disclosures after registration, the Office can initiate formal administrative proceedings which could result in the suspension of the developer's registration until the report is corrected.

In June 1972, the Examination Division requested authorization for 62 positions--an increase of 44 positions--to perform what it considered the quality of work needed to fulfill the intent of the Congress. However, the Deputy Administrator reduced this request to eight additional positions because of manpower limits established by HUD and the Office of Management and Budget. HUD approved five of these positions for fiscal year 1973.

AGENCY COMMENTS AND OUR EVALUATION

In commenting on our draft report (see app. II), HUD advised us that

- Under the present budget, it is unrealistic to expect staff increases large enough to police the industry to be forthcoming soon. For this reason and because the Interstate Land Sales Full Disclosure Act is a disclosure rather than a substantive regulatory statute, HUD is determined to strictly and vigorously implement the law to educate the public in protecting itself with the help of the Federal act and a strong State regulatory role.
- The Office is evaluating our proposal on field staff. Field personnel from other parts of HUD could possibly be used selectively in interstate land sales, and the Office is studying this option. Coordination among the States and between the States and the Federal Government should provide "a regulatory presence in the field," but HUD is evaluating whether an Office field staff will maximize such efforts.
- For fiscal year 1974, the Office's permanent staff is budgeted to increase from 55 to 74 employees. This projected staffing is realistic both in terms of the current restrictions on levels of Federal employment and the Office's ability to recruit, train, and effectively use additional staff.
- It is important to coordinate Federal and State efforts in regulating land sales. A strong State regulatory role is preferred, but dual standards and conflicting and confusing requirements at the State level are unacceptable. The Office is planning to hold formal conferences with State officials where it can stress the need for uniform regulations and practices and has made available to all State regulatory bodies a list of all subdivisions registered with HUD. The Office has day-to-day contact with State officials on matters of mutual concern.

--It is aware of the problems pointed out in our draft report concerning the acceptance, without verification, of registration material from the four States whose registrations were accepted by HUD. The Office does not have sufficient grounds to revoke this acceptance but is presently monitoring the situation in one of the four States. It would prefer the States to accept Federal registration in satisfaction of their requirements, as 10 States do, such acceptance would increase uniformity and would free State resources for better regulatory activities.

--It disagreed with our proposal that the Office conduct onsite inspections before registration. State officials who know about local conditions and laws can better make the inspections than can Office officials. However, relying on the States for these inspections requires uniform State regulations and procedures for conducting such inspections, and developing such uniformity will be a prime objective of the Office's attempt to coordinate State activity. The Office has conducted spot onsite inspections of registered subdivisions and will continue to do so. This is an area where strong State action is required if the Federal role is not to increase.

We agree with HUD that (1) the States and the Federal Government must work together and must do the jobs best suited to their respective abilities and statutory responsibilities, (2) the Federal role in consumer protection in interstate land sales should not be unnecessarily expanded, and (3) the States need to adopt uniform consumer protection statutes to provide more adequate consumer protection.

We believe, however, that the degree of Federal regulation must depend on whether the States do their part and implement more effective regulatory programs. Until HUD is reasonably satisfied that the regulatory programs are adequate, the Federal Government must take the initiative to provide the degree of protection for consumers which the Congress intended.

RECOMMENDATIONS

We recommend that the Secretary of HUD, to the extent practicable, decentralize the Office's regulatory activities-- assigning responsibility to HUD field office personnel. Decentralization would facilitate (1) the identification of unregistered subdivisions, (2) Federal-State cooperation in consumer protection activities, and (3) more effective verification of land developers' registration information. At a minimum, field representatives should be available in those States having major interstate land sales activity.

We also recommend that the Secretary have the Office

- Selectively inspect subdivisions before and after registration to verify the accuracy and reliability of land developers' disclosures and to help determine the adequacy of State regulatory programs. The selection of subdivisions and developers for inspection and the number of such inspections could be based on the degree of reliability of State regulatory programs and the completeness and adequacy of the developers' information.
- Establish working agreements with the States for exchanging information on land subdivisions and developers and encourage joint efforts to improve the States' regulatory programs and to promote uniformity in such programs.

CHAPTER 3

NEED TO STRENGTHEN ENFORCEMENT ACTIONS

From April 1969 (program inception) through March 1972, the Office's efforts to initiate enforcement actions against violators of the act were limited. From March to November 1972, the Office increased its enforcement activities. Because of staff limitations, however, the Office could not

- investigate alleged significant violations of the act indicated by consumer complaints nor follow up on consumer complaints referred to land developers and
- promptly enforce the legal requirement that all registered developers amend their statements of record and property reports to provide more detailed information on property owners' associations, the availability of water, nuisances, and safety factors concerning subdivisions

Although we found that some subdivisions were neither registered nor exempt, the Office did not promptly investigate them

NEED TO FOLLOW UP AND INVESTIGATE POSSIBLE VIOLATIONS OF THE ACT INDICATED BY CONSUMER COMPLAINTS

The Office needs to improve its procedures for handling consumer complaints to insure that developers are responsive and resolve the complaints. It also needs to investigate significant complaints to determine whether illegal activities have occurred, so it can act to protect the public and prevent recurrence of the illegal activities

The Director, Administrative Proceedings Division, told us that the Office referred consumer complaints to land developers against whom the complaints were made and asked that the developers advise the Office as to the action taken to resolve the complaints. The Office, as of December 1972, had received up to 200 complaints a week concerning land subdivision transactions.

The Deputy Administrator advised us that, although followup procedures existed, lack of staff limited followup

when developers did not respond to the Office's referral. An official of the Administrative Proceedings Division estimated that about 75 percent of the complaints received were resolved to the consumers' satisfaction as a result of the Office's referral to developers.

The Office, however, could not support this estimate. Therefore, we could not evaluate the effects of the Office's assistance to complainants.

In response to an inquiry from a Member of the Congress, HUD reported in July 1971 that the Office

"* * * lacks sufficient staff to do any independent investigation or testing of complaints, except in the case of the more flagrant violations of the act."

HUD said that, since April 1969, the Office's field investigations "have not numbered more than several dozen." As noted on page 16, since March 1972 the Office has made about 100 onsite inspections of subdivisions registered with HUD.

We believe that consumers need help in resolving problems with land developers. Consumers generally are not aware, however, of the assistance available from the Office. For example, about 500 people--about 81 percent of those responding to our questionnaire--reported that they had not heard of the Office.

The Deputy Administrator stated that, since March 1972, the Office's efforts to increase the public awareness of the Federal regulatory program--through public hearings and contacts with the news media--have been quite successful. Before then, the Office received only about 50 complaints concerning land subdivisions each week, as of December 1972, it was receiving about 150 to 200 complaints each week. In addition, numerous public inquiries were being received as a result of news coverage late in 1972. The Deputy Administrator told us that the Office received about 1,000 inquiries because of 1 article in a news magazine.

About 180 people--about 28 percent of those responding to our questionnaire--said they were dissatisfied with their

purchases. Their complaints indicated that the problems most frequently experienced included alleged

- failure of developers to provide promised improvements to property,
- deceptive sales practices,
- poor investment potential of property,
- failure of developers to provide adequate utility services,
- financing irregularities,
- property use restrictions, and
- excessive real property taxes

Examples of these problems are in appendix I. The nature of these complaints indicates that land developers might not have fully disclosed pertinent facts at the time of the sales transactions. Neither we nor HUD investigated the propriety of the complaints and whether the requirements of the act were met. We primarily intended to ascertain the types of problems most frequently confronting purchasers in land transactions.

In June 1972, the Administrative Proceedings Division requested authorization for 50 positions--an increase of 27 positions--to properly serve the public in processing, reviewing, and investigating consumer complaints. The Deputy Administrator reduced this request to five additional positions because of manpower limits established by HUD and the Office of Management and Budget. HUD approved three of these positions for fiscal year 1973.

NEED FOR MORE PROMPT ENFORCEMENT ACTIONS

Although the Office's enforcement activities improved during 1972 and 1973, we noted delays in (1) its enforcement of the requirement that registered developers amend their statements of records and property reports to disclose more complete information to consumers and (2) its actions against

land developers we identified as offering unregistered land for sale to the public

The Secretary of HUD is authorized to bring an action in a U.S. district court to obtain an injunction whenever any person appears to be engaged or about to engage in any illegal practice involving interstate land transactions. The Secretary is also authorized to transmit evidence to the Attorney General who may, at his discretion, institute appropriate criminal proceedings.

Under HUD's procedures for obtaining civil injunctions, the Administrative Proceedings Division develops a preliminary case for court action and submits the case to HUD's General Counsel for review. The General Counsel, if he concurs, submits the case to the Department of Justice for court action. In initiating criminal cases, HUD is authorized by the Department of Justice to work directly with the U.S. attorney in the jurisdiction where an indictment will be sought.

In January 1972 the Secretary adopted rules and regulations specifying administrative procedures whereby the Secretary can, for varying periods, suspend the right of a developer to engage in the interstate sale of registered subdivisions.

From April 1969 to March 1972, the Office took 20 enforcement actions against violators of the act. From March 1972 to March 1973, however, it took 432 enforcement actions--primarily initiating administrative proceedings and issuing orders suspending developers' rights to sell land.

In addition, the Deputy Administrator advised us that about 6,000 letters were sent to land purchasers informing them of their rights to receive refunds because they purchased land offered for sale illegally. He reported that, as of November 1, 1972, about \$830,000 had been refunded as a direct or indirect effect of this effort. He further reported that, because the Office had intervened with developers on behalf of consumers registering complaints with HUD, about \$330,000 more had been refunded.

As indicated above, the Office's enforcement activities have improved. The Office did not, however, promptly act

against (1) registered land developers who did not amend their statements of record and property reports, contrary to HUD regulations and (2) land developers we identified who were offering unregistered land for sale

Pursuant to a January 1972 amendment to HUD regulations, developers registered with HUD were required by March 31, 1972, to amend their statements of record and property reports to provide fuller disclosure to consumers. The regulations required developers to provide more detailed information on the organization and operation of property owners' associations, the availability of water, nuisances, and safety factors concerning subdivisions.

In April 1972 the Office notified all registered developers who had not amended their statements of record that they must do so to comply with the revised regulations. Of approximately 1,200 registered developers notified, about 450 had not responded to the notice as of July 31, 1972.

About 750 developers had amended their statements of record. According to an Examination Division official, however, the Division, because of its small staff, was unable to adequately review such amendments and many of them became effective automatically--without any review--after the prescribed 30-day period. The Deputy Administrator advised us that, as of November 1972, these amendments had been examined and any deficiencies noted had been corrected.

With respect to the 450 developers who did not respond to the Office's April 1972 notice, the Office, as of December 8, 1972, had sent notices of administrative proceedings to about 200 developers advising them that they had 15 days to answer charges concerning noncompliance with the regulations and to request a formal hearing. If they failed to respond to this notice, the Office could order the developers to suspend sales in the subdivisions.

The Deputy Administrator advised us in December 1972 that the Office would send notices of administrative proceedings to the remaining 250 developers who had not responded to the April 1972 notice. He stated that, because of the Office's small staff, it could send only about 25 notices a week to developers.

In a March 19, 1973, news release, HUD announced that notices of administrative proceedings had been sent to 280 of the 450 developers who had failed to comply with the revised regulations. The Deputy Administrator told us that the other 170 developers had complied.

As a result of the administrative proceedings for the 280 cases, HUD suspended the rights of 107 developers to sell land and 30 developers voluntarily agreed to suspend sales.

Of the remaining 143 developers, 63 had responded satisfactorily to the notices, 42 had just been sent notices, 6 had requested hearings, 30 were no longer in business at their known addresses, and 2 had formally entered into bankruptcy proceedings.

From August 4, 1971, to June 5, 1972, we referred to the Office the names of 38 subdivisions which were not included in HUD's control listing of developers registered or exempted from registration. We requested the Office to determine whether these subdivisions were subject to the act. We visited 33 of these subdivisions during our review and identified the other five primarily from land developers' advertisements.

A subsequent examination of HUD files and of an updated control listing showed that 11 of the 33 subdivisions visited and 2 of the 5 subdivisions not visited had been registered or exempted from registration.

We examined HUD records in April 1973 to determine the current status of these cases. On the basis of information available, we found that, of the 25 developers not registered or exempted, 9 had become registered and 1 had a pending registration. HUD determined that 1 was not subject to the act. Of the remaining 14, 7 had not responded to HUD's letters of inquiry following our referrals, and HUD had only recently sent letters of inquiry to 7.

Delays in investigating land developers who may be offering unregistered land for sale may deny prospective land purchasers the benefits of full and proper disclosures. In our opinion, the Office should act promptly when it identifies subdivisions which are neither registered nor exempt from registration.

RECOMMENDATIONS

We recommend that the Secretary of HUD have the Office

- Improve followup procedures to insure that land developers respond promptly to consumer complaints referred by the Office
- Investigate alleged significant violations of the act indicated by consumer complaints.
- Promptly act against land developers who, contrary to law, fail to amend their statements of record and property reports and who may be offering unregistered land for sale

AGENCY COMMENTS

In commenting on our draft report, HUD stated that

- Because the Office receives so many complaints from land purchasers, decisions on the manner of followup and whether to investigate a particular complaint become matters of choosing among competing priorities. The Office limits investigation to cases involving unusually serious alleged violations of the act or when illegal activity seems to be forming a pattern.
- Eliminating the backlog of complaints is a high-priority item on the Office's agenda, as is following up complaints referred by the Office to land developers. The Office is determined to strictly and vigorously implement the existing law to educate the public in protecting itself. The Office will also discipline the land sales industry, when required, to reduce the number of defrauded consumers and thus the number of complaints
- Since March 1972 the Office has used a considerable proportion of its resources to take effective action--especially in the area of administrative sanctions--against land developers who failed to comply with the act. This effort has been extremely productive, and the Office expects it to be even more effective in the future, despite problems with staff limitations

and competing priorities. When more staff members became available, they will concentrate on improving enforcement actions.

CHAPTER 4

SCOPE OF REVIEW

We reviewed the legislative history of the Interstate Land Sales Full Disclosure Act and HUD's policies, procedures, and practices for administering the law, examined HUD files, and held discussions with Office officials at HUD headquarters in Washington, D.C.

We met with officials of State regulatory authorities in Arizona, California, and Florida. We inspected 123 subdivisions located in these States and in Delaware, Maryland, North Carolina, Tennessee, and Virginia and held discussions with land developers or their representatives.

In addition, we sent a questionnaire to about 2,000 purchasers of subdivision lots in Arizona, California, and Florida. We had obtained the names and addresses of these people from land developers willing to furnish this information. The information furnished by these purchasers may not, therefore, be representative of all land purchasers. About 650 purchasers, or about 32 percent, responded to the questionnaire. We made our review from July 1971 to September 1972, we mailed the questionnaires during the period March to May 1972 and analyzed the responses received through June 1972.

EXAMPLES OF COMPLAINTS REPORTED TO GAO BY CONSUMERS
IN INTERSTATE LAND SALES TRANSACTIONS

PROMISED IMPROVEMENTS

- A purchaser of a lakefront lot in Texas in 1969 reported that there had never been any water in the manmade lake areas
- A purchaser of two canalfront lots in Florida who was promised access to the Gulf of Mexico reported that canals had not been dug within the time promised
- A purchaser of a lot in North Carolina reported that, because roads had been incomplete for almost 2 years, his lot was inaccessible during rainy periods
- A purchaser of a lot in California reported that promised security arrangements for property owners--protective gates manned by guards--had not been provided

SALES PRACTICES

- A purchaser of a lot in North Carolina reported that, before he signed the contract, the developer did not inform him of a mandatory charge for road maintenance, security, and fire protection
- A purchaser of a lot in Arizona reported that he did not receive the gift--a television set--which he had been promised for being among the first 100 purchasers in the subdivision. The developer later informed him that the televisions were given only to purchasers who prepaid 1 year's principal and interest charges

PROPERTY'S INVESTMENT POTENTIAL

- A purchaser of a lot in Florida reported that, at the time of purchase, the developer said he would resell the land when the purchaser so desired. The developer later refused to assist the purchaser in selling land. Four independent brokers later told the purchaser that the land was worth less than one-half of the purchase price and that there was little or no market for the property.

APPENDIX I

- A purchaser of a lot in Arizona reported that the promised 10-percent annual appreciation of property had never materialized.
- Another purchaser of a lot in Arizona attempted to resell his property but was told by the developer that he could not sell the lot until the subdivision was completely developed. He was not informed of this restriction when he purchased the lot.

UTILITY SERVICES

- A purchaser of a lot in California reported that, at the time of purchase in 1971, the developer told him that utility services--sewage, water, electricity, gas, and telephone--would be completed in 1971. As of March 1972, none of the necessary services had been provided.
- A purchaser of a lot in Arizona who intended to install a mobile home reported that the developer had not told him that he would have to pay several hundred dollars for the installation of a septic tank, which he had understood would be provided at no additional charge

FINANCING

- A purchaser of a lot in Florida reported that he was advised that monthly interest charges would be on the unpaid balance of the contract. He later learned that monthly interest was computed on the original balance due, without considering payments made.
- A purchaser of a lot in Virginia reported that the developer would not provide him with a breakdown of the amount of interest paid on the contract, which he needed to compute his Federal income tax deduction.

PROPERTY USAGE

- A purchaser of a lot in California reported that the developer had refused to allow him to install a mobile home because it was 2 feet less than the minimum width allowed and that he was not aware of such a restriction at the time of purchase

--A purchaser of a lot in California reported that a drainage easement on his property had rendered the land useless.

PROPERTY TAXES

--A purchaser of a lot in California reported that he was informed at the time of purchase that real property taxes averaged about \$30 a year. During the first 2 years of ownership, taxes totaled about \$300.

--A purchaser of a lot in California reported that, at the time of purchase in 1971, the developer told him that annual property taxes would be \$40. Property taxes for 1972 were \$127.

--Another lot purchaser in California reported that the developer's sales agent had told him that annual taxes payable would be \$8. Annual taxes payable were \$50.



DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT
OFFICE OF INTERSTATE LAND SALES REGISTRATION
WASHINGTON, D C 20410

IN REPLY REFER TO

JAN 26 1973

Mr B E Birkle
Associate Director
United States General
Accounting Office
Washington, D C 20548

Dear Mr Birkle

The Secretary has requested that I respond to your memorandum of December 21, 1972. We have reviewed the proposed report to the Congress on your review of this Office. The following are our comments on the action planned with respect to your recommendations.

Broadly speaking, there are two possible extremes with respect to the role of the Federal government in the area of interstate land sales. One envisions the job of the government to be that of a passive repository of whatever information is filed by developers. We reject this out of hand. The other believes the Federal government must actively regulate and police the activities of land developers in all areas of the industry on a prior approval basis. Although our experience has demonstrated, and your report has confirmed, that fraud is too prevalent in the industry and the average consumer too uninformed and credulous to allow this Office to simply file the information it receives. However, given the realities of the present budgetary situation, we feel it is unrealistic to expect that staff increases of the magnitude necessary to police the industry through a system of pre-registration examination and review of subdivisions and developers will be forthcoming soon. Obviously, such a goal must assume its proper perspective in our national priorities.

In view of the above and the fact that the Interstate Land Sales Full Disclosure Act is a disclosure rather than a substantive regulatory statute, we have, as I pointed out in a recent speech at the Convention of the National Association of Real Estate License Law Officials, determined to "seek by strict and vigorous implementation of the existing law to educate the public to the point where it could protect itself, utilizing the assistance of the Federal Act and a strong State Regulatory role." This course of action requires a complex balancing of roles and priorities not required by the other philosophies. While I do not rule

Mr B E Birkle
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out some additional regulatory teeth in the Act, nevertheless, I feel strongly that the course we are on is the proper one for this Office to follow. It is in light of this enforcement philosophy that I would respond to your specific recommendations as follows:

- (1) I appreciate the recognition your report gives to the intensified efforts this Office has made since March of 1972 to increase the protection afforded consumers under the Act. Also, as your report documents, the sheer magnitude of the task of adequate enforcement has severely tested the manpower made available to this Office. Your report recommends the assignment of staff to the field in order to identify developers who have not registered their subdivision with HUD. We are considering whether the adoption of this recommendation is consistent with the most effective utilization of our resources. (It is possible that field personnel from other parts of HUD can be used selectively in this area and we are presently studying this option. However, such personnel already have other duties and may lack the necessary expertise.) As indicated, we believe a regulatory presence in the field should be provided by coordinated efforts among the states and between the states and Federal government but we are evaluating whether an OILSR field staff would maximize these efforts.
- (2) As your report indicates, our present staff consists of 55 permanent employees augmented by 19 temporary employees and 10 consultants. For Fiscal 1974, we are presently budgeted to increase our permanent staff to 74 employees. I believe that the staffing projected for 1974 is realistic both in terms of the current climate on levels of Federal employment and OILSR's capability to recruit, train and make effective use of additional staff.
- (3) I believe that my speech to the state regulatory officials referred to above signalled our awareness of the importance of coordinating the Federal and state effort in this industry and indicated the way we feel this effort should proceed. A strong State regulatory role is preferred. However, dual standards and conflicting and confusing requirements at the state level will not do.

In any case, the Federal role should not be expanded beyond that which is absolutely necessary. As a part of our continuing effort to provide the necessary coordination for this

Mr B E Birkle

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regulatory effort, we are planning formal conferences with state officials where the need for uniformity of regulations and practices can be stressed. We have already seen some movement by NARELLO following my November address. Also, we have made available to all state regulatory bodies copies of a list of all developments registered with this Office. An updated list will soon be distributed. Finally, as your report indicates, members of my staff are in virtual day-to-day contact with state officials on matters of mutual concern.

- (4) As indicated in your report, the Act requires OILSR to cooperate with State Officials and allows this Office to accept state filings in satisfaction of the Federal statutory requirements where satisfied the state law and enforcement effort is sufficient. OILSR has only accepted the filings of four states under this provision. While we do not, as yet, have sufficient grounds to revoke the acceptance for any of the four states, we are aware of many of the problems indicated in your report and are monitoring the situation in one of them. In terms of priorities, we have not been able to give this review the emphasis it will receive. In fact, as I have indicated, we feel that it would be preferable if the states accepted Federal filings in satisfaction of their local registration requirements, as ten states do now. This would increase uniformity and free state resources for substantive regulatory activities.
- (5) As your report indicates, I am not in favor of OILSR conducting on-site inspections before registration. Again, OILSR's position is that such inspections can better be performed by state officials who have the knowledge of local conditions and laws necessary to do the job adequately. Of course, this will require the development of uniform state regulations and procedures for conducting such inspections. Such uniformity will be, as indicated earlier, a prime objective of OILSR's attempt to coordinate state activity. Within the limitations imposed by the availability of personnel, OILSR has conducted spot, on-site inspections of developers registered with this Office and this program will continue to be an important aspect of our total effort. Obviously, this is also an area where strong state action is required if the Federal role is not to increase.
- (6) The volume of complaints received by this Office is so large that decisions as to the manner of follow-up--all complaints are looked into--and whether or not a particular complaint

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should be investigated, as opposed to being followed up, or how to conduct an investigation once it is initiated become matters of choosing among competing priorities. As a matter of investigative strategy, this Office limits investigation to cases where the complaint involves unusually serious violations of the Act or where a pattern of illegal activity seems to be present. Many complaints, because they involve matters outside our jurisdiction or comparatively isolated behavior do not, in our opinion, require full scale investigations. Even though, as your report recognizes, we have made substantial efforts since March to improve our performance in this area, there is no doubt that we can improve our performance. Indeed, elimination of the backlog of complaints received by our Administrative Proceedings Division is a high priority item in our agenda. So is improving our follow-up of complaints referred by OILSR to developers. Our primary long-range goal, however, is to educate the public and discipline the industry where required so as to cut down on the number of defrauded consumers and thus the number of complaints.

- (7) As your report recognized, this Office since March 1972 has devoted a considerable proportion of its resources to the effort to take effective action--especially in the area of administrative sanctions--against developers who fail to comply with the requirements of the Act. This effort has been extremely productive and we expect it to move even more quickly and effectively in the future despite problems with staff limitations and competing priorities. Improvement in this area is a prime target for the utilization of such additional manpower as becomes available.

Sincerely,



George K. Bernstein
Interstate Land Sales Administrator

APPENDIX III

PRINCIPAL OFFICIALS OF THE
DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT
RESPONSIBLE FOR THE ADMINISTRATION OF ACTIVITIES
DISCUSSED IN THIS REPORT

	<u>Tenure of office</u>	
	<u>From</u>	<u>To</u>
SECRETARY OF HOUSING AND URBAN DEVELOPMENT		
George W Romney	Jan 1969	Jan 1973
James T Lynn	Feb. 1973	Present
ASSISTANT SECRETARY FOR HOUSING PRODUCTION AND MORTGAGE CREDIT AND FEDERAL HOUSING COMMISSIONER (note a)		
William B Ross (acting)	Feb. 1969	Sept 1969
Eugene A Gulledge	Oct 1969	Mar 1972
INTERSTATE LAND SALES ADMINISTRATOR		
Alfred J Lehtonen	Apr 1969	Feb 1971
George K C Ellsworth (acting)	Feb 1971	June 1971
Roy P Cookston	June 1971	Nov. 1971
Fred A Mann (acting)	Nov 1971	Feb 1972
George K Bernstein	Mar 1972	Present

*

^a Responsibility for the Office's activities were transferred in March 1972 from the Assistant Secretary for Housing Production and Mortgage Credit and Federal Housing Commissioner to the Interstate Land Sales Administrator, who reports directly to the Secretary of Housing and Urban Development.

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