



U.S. Department of Agriculture

Office of Inspector General



**American Recovery and Reinvestment Act -
Emergency Watershed Protection Program
Floodplain Easements
Phase I**

Audit Report 10703-1-KC
September 2010



U.S. Department of Agriculture
Office of Inspector General
Washington, D.C. 20250



DATE: September 8, 2010

REPLY TO
ATTN OF: 10703-1-KC

TO: Dave White
Chief
Natural Resources Conservation Service

ATTN: Lesia Reed
Deputy Chief
Strategic Planning and Accountability

FROM: Gil H. Harden /s/
Assistant Inspector General
for Audit

SUBJECT: American Recovery and Reinvestment Act, Emergency Watershed Protection
Program Floodplain Easements—Phase I

This report presents the results of our audit of the internal controls over Emergency Watershed Protection Program Floodplain Easements funded by the American Recovery and Reinvestment Act of 2009. This report compiles the results of our work that we reported in two Fast Reports: one dated August 19, 2009, and the other dated November 19, 2009. Summaries of your responses, along with the Office of Inspector General's (OIG) position, are incorporated into the Findings and Recommendations sections of this report.

Based on your responses, we have accepted management decision for all recommendations in the report. Please follow your internal agency procedures in forwarding final action correspondence to the Office of the Chief Financial Officer. Please note that Departmental Regulation 1720-1 requires final action to be completed within 1 year of the date of management decision to preclude being listed in the Department's annual Performance and Accountability Report.

We appreciate the courtesy and cooperation extended to us by members of your staff during the review.

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Emergency Watershed Protection Program Floodplain Easements Phase I

Executive Summary

This report presents the results of our first phase of audit work related to floodplain easement acquisitions through the Emergency Watershed Protection Program (EWPP). The American Recovery and Reinvestment Act (ARRA) of 2009 (Recovery Act)¹ was signed into law on February 17, 2009. The purposes of the Recovery Act include preserving and creating jobs, promoting economic recovery, and assisting those most impacted by the recession. The Recovery Act included \$145 million for the U.S. Department of Agriculture (USDA) to acquire floodplain easements.

The Natural Resources Conservation Service (NRCS) works with landowners to help them conserve, maintain, and improve their natural resources. The Secretary of Agriculture is authorized to undertake emergency measures, including the purchase of floodplain easements, for runoff retardation and soil erosion prevention, in cooperation with landowners and land users.² Floodplain easements restore, protect, maintain, and enhance the functions of the floodplain; conserve natural values, including fish and wildlife habitat, water quality, floodwater retention, groundwater recharge, and open space; reduce long-term Federal disaster assistance; and safeguard lives and property from floods, drought, and the products of erosion.

Congress, in enacting the Recovery Act, emphasized the need for accountability and transparency in the expenditure of funds. The Office of Management and Budget (OMB) subsequently issued guidance that required Federal agencies to establish rigorous internal controls, oversight mechanisms, and other approaches to meet the accountability objectives of the Recovery Act.³ According to guidance issued by the Secretary of Agriculture, agencies shall develop transparent merit-based criteria that will guide their discretion in committing, obligating, and expending funds under the Recovery Act.

Our role, as mandated by the Recovery Act, is to oversee agency activities and to ensure agencies expend funds in a manner that minimizes the risk of improper use. We are using a multi-phase approach in performing our review of the Recovery Act-funded EWPP Floodplain Easements (FPE) program. Phase I focused on (1) monitoring the development of program guidance and requirements and (2) evaluating internal control systems utilized to ensure that program objectives are achieved, that program participants fully meet eligibility requirements, and that payments are accurately computed.

During this initial phase, we identified internal control issues where existing controls were not adequate for acquiring permanent easements. We reported these issues to the Chief, NRCS, in two Fast Reports in August and November of 2009. The findings include the following.

- NRCS did not ensure that acquiring floodplain easements on small tracts of land would be a prudent use of Recovery Act funds. We identified that 30 easements were to be

¹ Public Law (P.L.) 111-5, dated February 17, 2009.

² P.L. 81-516, section 216 (as amended).

³ On April 3, 2009, OMB issued *Updated Implementing Guidance for the American Recovery and Reinvestment Act of 2009*.

acquired on small tracts (about 1 acre) located in 3 States. To meet the intent of the program, the land placed under easement is to be restored to its natural floodplain condition, which necessitates the removal of unnatural obstructions including the flood-prone or damaged homes. The average cost to NRCS was about \$150,000 per easement or \$130,000 per acre. Generally, floodplain easements are acquired for a cost of less than \$4,000 per acre.

- Adequate procedures were not established for this unique easement process. Specifically, procedures should have specified the method to assess the value of the flood-prone or damaged homes; how insurance payments received by homeowners may impact the valuation; and situations where the landowner acquired the damaged property below assessed value.
- Easement compensation was not limited to the lowest of: 1) the value based on an area-wide market analysis or survey; 2) a geographical area rate cap determined by the Secretary in regulations; or 3) the producer's offer as required. In these cases, NRCS included the home's assessed value as part of the easement compensation value.
- NRCS did not demonstrate that the legal requirement to use appraisals for valuation of Recovery Act-funded easements was not practicable prior to prohibiting appraisals.
- NRCS adopted the use of a valuation methodology based on its Wetlands Reserve Program (WRP) which eliminated appraisals without determining whether this expansion was permissible and consistent with applicable laws pertaining to floodplain easements using regular funding.

As a result, the absence of critical procedures and the inappropriate expansion of the WRP easement valuation methodology could substantially reduce confidence that the program is implemented properly and applicants are fairly compensated.

Recommendation Summary

We recommended that NRCS:

- (1) revisit the policy of purchasing easements on small tracts of land where the costs of acquiring and demolishing homes are high, and determine whether such purchases constitute a prudent use of Recovery Act funds;
- (2) establish comprehensive EWPP-FPE procedures which address the purchasing of easements on residential home sites;
- (3) follow up with State offices to correct applications and ensure proper accounting of restoration/easement costs;
- (4) identify all approved applications where the cost of purchasing and removing homes constitutes the primary restoration cost, perform a review of each identified application, and make the appropriate corrections;

- (5) stop approving any further Option Agreements to Purchase for floodplain easements using the WRP valuation methodology until NRCS can demonstrate that the currently required appraisal method is not practicable for Recovery Act - funded easements;
- (6) rescind the specific direction provided to State Conservationists authorizing use of the WRP valuation methodology for floodplain easements; and
- (7) consult with USDA's Office of the General Counsel (OGC) to determine appropriate valuation procedures for Recovery Act-funded floodplain easements, implement these procedures, and document the support and rationale for any procedures implemented.

Agency Response

NRCS responded in writing to each of the Fast Reports and provided agreement with, or further explanation regarding, each of the concerns noted. The two Fast Reports and their corresponding NRCS responses can be found at http://www.usda.gov/oig/recovery/recovery_reports.htm. In addition, NRCS provided additional responses, dated June 11, 2010, and August 6, 2010, to the second Fast Report which are included at the end of this report.

OIG Position

Based on NRCS' responses, we accept management decision on all seven of the report's recommendations.

Background & Objectives

Background

NRCS is the primary Federal agency that works with private landowners to help them conserve, maintain, and improve their natural resources. The Secretary of Agriculture is authorized to undertake emergency measures, including the purchase of floodplain easements, for runoff retardation and soil erosion prevention, in cooperation with landowners and land users, as the Secretary deems necessary to safeguard lives and property from floods, drought, and the products of erosion on any watershed whenever fire, flood, or any other natural occurrence is causing or has caused a sudden impairment of that watershed.⁴ Floodplain easements restore, protect, maintain, and enhance the functions of the floodplain; conserve natural values, including fish and wildlife habitat, water quality, floodwater retention, groundwater recharge, and open space; reduce long-term Federal disaster assistance; and safeguard lives and property from floods, drought, and the products of erosion.

The Watershed Protection and Flood Prevention Act of 1954,⁵ as amended, authorized NRCS to cooperate with States and local agencies to carry out works of improvement for soil conservation and for other purposes, including flood prevention, conservation, development, utilization and disposal of water, and proper utilization of land. The Federal Agriculture Improvement and Reform Act of 1996 amended the Emergency Watershed Program to allow NRCS to provide for the purchase of floodplain easements as an emergency measure.⁶

The Recovery Act provided \$145 million to NRCS “for necessary expenses to purchase and restore” such easements.⁷ On February 18, 2009, OMB issued initial guidance requiring Federal agencies to establish rigorous internal controls, oversight mechanisms, and other approaches to meet the accountability objectives of the Recovery Act.

Floodplain Easement Application Process

NRCS accepted applications during a national sign-up period which began on March 9, 2009, and was extended to April 10, 2009. All applications were to be ranked by the NRCS State offices and entered into a database by April 17, 2009. Prior to April 24, 2009, each State office was to send its ranking list, a project showcase⁸ for each application that it expected to fund, and photographs of a selection of showcase projects to NRCS Headquarters. All offers were to be obligated prior to July 3, 2009, and easements closed prior to February 3, 2010. All new floodplain easements were to be formally accepted, in writing, and are to be recorded as part of the warranty easement deed using an OGC-approved acceptance document. Restoration funds are to be obligated upon completion of the restoration plan of operations using a Long-Term Agreement (AD-1154) form, Federal contract, Cooperative/Contribution Agreement, or other appropriate procurement document. Restoration should be fully completed prior to December 30, 2010.

⁴ P.L. 81-516, section 216 (as amended).

⁵ P.L. 83-566.

⁶ P.L. 104-127, section 382.

⁷ P.L. 111-5, 123 Stat. 117.

⁸ Each project showcase briefly describes the current condition of the land offered for easement, the restoration needed to return the land to a natural floodplain condition, and the anticipated environmental benefits to be obtained.

Land Eligibility

To be eligible, at least 65 percent of the acreage proposed for enrollment must be located within an authorized watershed. The land must be privately owned or owned by State or local units of Government and must be: (1) land damaged by flooding at least twice within the previous 10 years or at least once in the last 12 months, and/or (2) land that would be inundated or adversely impacted as a result of a dam breach.

Compensation—Easement Payments

Under the floodplain easement option, a landowner voluntarily offers to sell to NRCS a permanent conservation easement that gives the agency the full authority to restore and enhance the floodplain's functions and values. In exchange, a landowner receives as an easement payment, the lowest of the following three values:

- i. a value based on a market analysis
- ii. a geographical area rate cap determined by the Secretary in regulations, or
- iii. the landowner's offer

Appraisals were not allowed for the floodplain easement enrollment, as NRCS used the WRP valuation methodology (cited above) to determine easement value.

Restoration

For Recovery Act-funded EWPP floodplain easements, NRCS is to pay 100 percent of the actual cost of restoration efforts. NRCS actively restores natural floodplain features and characteristics by re-creating the topographic diversity, increasing the duration of inundation and saturation, and providing for the re-establishment of native vegetation. Restoration on floodplain easements is to include the necessary conservation practices, measures, and activities required to restore the floodplain functions and values to its natural condition to the greatest extent practicable. This could involve such practices as removing dikes, planting native grasses, planting native trees, un-leveling ground that had been leveled, and plugging draining ditches in order to restore the historic hydrology and wildlife habitat. The removal of existing structures, including fences and incidental farm buildings, is to be allowed as a restoration practice if it is necessary to permit the floodplain to function properly during flood events.

Landowner Use

Landowners retain several rights to the property, including:

- quiet enjoyment,
- the right to control public access, and
- the right to undeveloped recreational use, such as hunting and fishing.

At any time, a landowner may obtain authorization from NRCS to engage in other activities, provided that NRCS determines these activities will further the protection and enhancement of the easement's floodplain functions and values. Compatible uses may include managed timber

harvest, periodic haying, or grazing. NRCS determines the amount, method, timing, intensity, and duration of any compatible use that might be authorized.

While a landowner can realize economic returns from an activity permitted on the easement area, a landowner is not assured of any specific level or frequency of such use, and the authorization does not vest any right of any kind to the landowner.

Objectives

The overall objectives of our audit oversight of the Recovery Act monies are to ensure: (1) the Department's Recovery Act-related programs are timely and effectively implemented; (2) proper internal control procedures are established; (3) program participants meet eligibility guidelines; (4) participants properly comply with program requirements; and (5) agencies establish effective compliance operations.

The objectives of this first phase of the audit were: (1) to monitor the development of program guidance and requirements—including eligibility requirements—for distributing Recovery Act funding to program participants, and (2) to evaluate internal control systems utilized to ensure that program objectives are achieved, that program participants fully meet eligibility requirements, and that payments are accurately computed.

Section 1: Floodplain Easement Acquisition and Valuation

Finding 1: Acquisition of Easements on Tracts with Structures

By June 2009, NRCS received 4,252 applications for Recovery Act-funded flood protection easements that would have totaled \$1.4 billion. The agency approved 289 applications totaling \$138 million. Our review questioned the merit of NRCS approving 30 applications to place easements on very small tracts of land that were primarily residential with very high costs per acre. NRCS procedures were not adequate to address the many factors involved in utilizing the program for residential land easements, including using local tax assessment information for the value of the homes that would be removed to restore the land to its natural floodplain condition.

NRCS Purchased Easements on Small Tracts of Land

Many of the applications approved by NRCS were for the purchase of easements on small tracts of land and included the purchase and removal of flood-prone or damaged houses. Of the 30 such approved applications in Alaska, Ohio, and West Virginia, the land associated with these applications ranged from one-tenth of an acre to 4 acres, and averaged about 1.1 acres. The average total cost to be incurred by NRCS for these applications was \$151,052 or about \$132,115 per acre. NRCS agreed to provide funding to the applicant for the value of the home so that any mortgage could be repaid, liens could be released, and the easement placed on the land. The chart shows that Alaska, Ohio, and West Virginia had 23 approved applications that included structures and their average cost per application and acre in each State.

| State | Number of Approved Applications Identified | Average Cost Per Application | Average Cost Per Acre |
|---------------|---|-------------------------------------|------------------------------|
| Alaska | 3 | \$365,486 | \$135,365 |
| Ohio | 9 | \$227,266 | \$227,266 |
| West Virginia | 18 | \$77,206 | \$80,797 |

While NRCS believes that using these funds to purchase small tracts of land is not prohibited, OIG is concerned about the appearance of purchasing small easements on residential land at high costs. Generally, NRCS purchases easements which average less than \$4,000 per acre. Utilizing the funds to purchase much larger pieces of land allows the agency to more significantly affect flood patterns in the area where the program is in operation.

NRCS Determined the Value of the Homes Using the Homes' Tax-Assessed Value

Although NRCS established a procedure for determining the value of land for easements, it did not have procedures for valuation of the homes on these easements.⁹ In lieu of not having such procedures, the agency elected to use the property tax assessment value for determining the valuation of homes.¹⁰ The value of the home was used in determining the total estimated restoration cost, in addition to the purchase price of the easement.

We questioned whether using tax assessment values is appropriate since local jurisdictions can vary widely in how assessments are determined. Assessment values depend on a number of factors, including when the assessment was made, whether accurate information about the property was used, and the differences among specific assessment procedures. In addition, the period between assessments varies by jurisdiction. Some taxing authorities might conduct full assessments every 6 years, for instance, but update their records annually to account for new homes or building improvements. Others might update more frequently.

For example, for one property in Alaska, NRCS has estimated it will pay \$476,190 for the home and \$6,820 for the land easement payment. After this 2.2 acre property was flooded in 2006 and 2007, the house had to be temporarily abandoned and the land was designated as a flood zone. The tax-assessed value of the home and other improvements was \$366,300, but the costs for demolition and removal of the house and restoration of the floodplain were estimated at \$109,890 for a total estimated restoration cost of \$476,190. Given the state of the house and land, and the method used to determine the value of the house, we question whether it is a prudent use of Recovery Act funds to spend 99 percent of the funds for the acquisition and demolition of the home and only 1 percent to purchase the easement.

NRCS Needs to Establish Procedures for Purchasing Homes as Part of Flood Protection Easements

Overall, NRCS was relatively inexperienced in dealing with homes located on these small easements and did not have procedures to anticipate problems that would likely arise.

- NRCS did not consider whether applicants had received insurance payments related to damage to their properties or reimbursement from other sources (Federal Emergency Management Agency or State and local governments). NRCS officials indicated that they had not considered this issue but that they should obtain this information as part of the decision process.

⁹ According to the procedures for EWPP FPE, the landowner is to receive the lowest of the following values: a value based on an area-wide market analysis or survey; the amount corresponding to a geographical area rate cap, as determined by the Secretary; or the offer made by the landowner.

¹⁰ A home's "tax-assessed value" is defined as the worth or value of a piece of property as determined by the taxing authority for the purpose of levying an *ad valorem* (property) tax.

- NRCS did not consider how to deal with a landowner who had acquired the property after it was damaged. If the current property owner purchased the damaged home after the flood, then NRCS should consider whether the amount paid to the homeowner as part of restoration costs should not exceed the home's market value after the damage.

In Ohio, we found that NRCS planned to compensate landowners for the value of their homes using easement payments rather than using restoration payments.¹¹ After we discussed this issue with NRCS officials, they initially agreed that the payments related to the value of existing structures should not be made through an easement payment but rather through restoration funding. They stated that they would instruct the Ohio NRCS State office to correct the nine applications by moving the payment amounts related to the value of existing structures to restoration costs.

However, NRCS subsequently changed its position, stating that it would no longer consider the value of a structure as a restoration cost. NRCS plans to reclassify as an easement cost—rather than as a restoration cost—the amount paid for a structure. The cost of removal will still be considered a restoration cost.

We note that NRCS' procedure allows only three choices for easement compensation—the lowest of: 1) the value based on an area-wide market analysis or survey, 2) a geographical area rate cap determined by the Secretary in regulations, or 3) the producer's offer. It is unclear to us how NRCS can classify the value paid for a structure as an easement cost rather than a restoration cost. NRCS' latest position is that the agency is buying the easement on the land and any structures should be included in the cost of the land.

After our discussion with NRCS Headquarters officials, we issued a Fast Report to NRCS, dated August 19, 2009. In this report, we made four recommendations, as outlined below. The full text of NRCS' response can be found at http://www.usda.gov/oig/recovery/recovery_reports.htm.

Recommendation 1

Revisit the policy of purchasing easements on small parcels of land where there are high costs for the acquisition and demolition of homes and determine whether it is a prudent use of Recovery Act funds.

Agency Response

NRCS' initial response indicated it had reviewed the policies authorizing the purchase of FPEs on land with existing structures and determined that the purpose of EWPP is furthered by these policies for the reasons identified in the preamble of the final rule. NRCS will continue to administer the EWPP-FPE program in conformance with the statute and regulation, and will continue to use the program to reduce future costs to Federal, State, and local units of government, the private sector, and the taxpayer.

¹¹ According to EWPP FPE procedures, the cost to purchase, demolish, and remove any structure on the land with the easement, as well as any costs to restore the land, fall into the category of restoration costs. Under the procedures, easement payments include only the cost to purchase the easement on the land.

In its June 11, 2010, response, NRCS stated that it had placed a temporary hold on lands in residential use for non-Recovery Act funded easements. NRCS has separated the methodology to be used for agricultural and other non-residential lands from the methodology for lands that were in residential use.

OIG Position

We accept management decision for this recommendation.

Recommendation 2

Establish comprehensive EWPP-FPE procedures which address purchasing easements on small parcels of land where the acquisition and demolition of homes are the primary costs.

Agency Response

NRCS concurs that the establishment of comprehensive procedures will further the accountability and transparency principles of ARRA, in general, and EWPP specifically. NRCS will establish standard operating procedures for purchasing easements on small parcels with structures and incorporate these procedures into the EWPP-FPE manual. In addition, NRCS' June 11, 2010, response stated that NRCS has now separated the methodology to be used for agricultural and other non-residential lands from the methodology for lands that were in residential use.

In its August 6, 2010, response, NRCS stated that it has drafted comprehensive procedures that encompass coordination with sponsoring organizations to identify acquisition costs from restoration costs and the use of appraisal procedures when purchasing easements on small parcels with residential structures. NRCS will incorporate these procedures in a final EWPP-FPE manual by September 30, 2010.

OIG Position

We accept management decision for this recommendation.

Recommendation 3

Follow up with NRCS State offices to correct EWPP-FPE applications and to move costs associated with homes and other improvements to restoration costs, not easement payment amounts.

Agency Response

NRCS concurs that the agency should handle the costs associated with the value of structures, their demolition, and removal in a consistent manner. However, there are two costs associated with structures and improvements: the acquisition costs associated with the increased value that land with structures and improvements has, and the restoration costs associated with demolition and removal of the structures and improvements. Under the terms of the EWPP floodplain easement, NRCS acquires rights, title, and interest in the encumbered property, reserving to the landowner only five enumerated rights. The

landowner does not reserve any rights to the structures and improvements. Thus, NRCS acquires the rights to all structures and improvements affixed to the land when it acquires a EWPP floodplain easement, and believes that fair treatment of landowners supports the agency compensating a landowner for the contribution to land value that such structures and improvements provide. NRCS determines the compensation for this contribution to land value through local tax assessments and adjusts the easement compensation level accordingly. Therefore, these costs are acquisitions costs. There is a separate cost associated with the demolition and removal of the structures and improvements from the easement area. These costs are appropriately considered restoration costs.

In its August 6, 2010, response, NRCS stated that, in November 2009, specific revised guidance was sent to three States (West Virginia, Ohio, and Alaska) with pending ARRA - funded transactions involving structures. NRCS clarified that for projects funded under ARRA, the geographic area rate cap (GARC) for projects with structures is determined by combining the GARC for the land and the value of the structure determined by using the local taxing authority assessment.

For non-ARRA funded transactions, NRCS stated that it has drafted comprehensive procedures that encompass coordination with sponsoring organizations to identify acquisition costs from restoration costs and the use of appraisal procedures when purchasing easements on small parcels with residential structures. NRCS will incorporate these procedures in a final EWPP-FPE manual by September 30, 2010.

OIG Position

We accept management decision for this recommendation.

Recommendation 4

Identify all EWPP-FPE approved applications where homes are the primary restoration cost, perform a review of each application, and make the appropriate corrections.

Agency Response

NRCS will continue to administer the EWPP-FPE program in conformance with all appropriate statutes and regulations, and will use its oversight and evaluation process to ensure the validity of all funded EWPP-FPE applications.

In its August 6, 2010, response, NRCS stated that it will review copies of case files associated with any active ARRA-funded transaction where the cost of purchasing and removing a home constitutes the primary restoration cost. NRCS will not include in this review any transaction where either NRCS or the landowner has decided not to pursue the transaction. This review will occur within the next 3 months, and NRCS will make any appropriate corrections as soon as possible, not to exceed 6 months.

OIG Position

We accept management decision for this recommendation.

Finding 2: NRCS Valuation Methodology for Floodplain Easements

OIG initiated this review to assess NRCS' activities and to ensure that the agency expended funds in a manner that minimized the risk of improper use. Specifically, we determined if NRCS had adequate controls for acquiring permanent easements on private land or on certain land owned by units of State and local governments. Since a crucial aspect of purchasing easements involves determining the value of the land in question, Federal regulations require that property should be appraised before an owner can participate in the program.

We found that NRCS stopped using appraisals as its method for determining the value of easements without adequately justifying or documenting its determination for making this change. Because NRCS believed that the appraisal process would be too slow, it eliminated the requirement that land be appraised, and instead substituted the method it uses to determine the value of easements under its Wetlands Reserve Program (WRP).¹² According to this method, NRCS would purchase easements by offering landowners the lowest of the following three amounts: (1) a value based on a market analysis, (2) a geographic value established by the Secretary in regulations, or (3) the landowner's offer.¹³

Once the Recovery Act provided funds for floodplain easements in February 2009, NRCS consulted OGC to confirm NRCS' legal authority to use the WRP valuation methodology for conservation easements under the Recovery Act, instead of the appraisals it would ordinarily perform for floodplain easements. NRCS personnel explained that they believed the WRP methodology would allow them to obligate funds more quickly, which was an important emphasis of the Recovery Act.

In April 2009, OGC informed NRCS that the legal requirement to use appraisals for valuation of the Recovery Act easements under the EWPP "is conditioned by [the phrase] 'to the greatest extent practicable' and that the NRCS Chief might be able to make a finding that using the NRCS normal appraisal process is NOT to the greatest extent practicable, and determine that an alternative that finds a reasonable market value is appropriate. Of course, this doesn't fix the appraisal requirement for regular [floodplain easement] acquisitions by NRCS under [Emergency Watershed Program], and you may still want to seek a legislative fix for that." OGC officials clarified that this legal advice meant that it would be prudent for NRCS to document how it arrived at its decision to stop using appraisals, in case NRCS were asked to justify its decision.

In May 2009, NRCS notified OGC that it would cease using appraisals for both regular *and* Recovery Act easements under the EWPP. NRCS argued that "it can best ... ensure consistent treatment of landowners by using the same compensation methodology for all [floodplain easements] and [WRP] transactions." Subsequently, on June 3, 2009, the NRCS Chief sent a memo to four Midwest State Conservationists authorizing NRCS staff to determine the purchase price of any floodplain easement—for both regular and recovery programs—by using the WRP methodology instead of appraisals. We believe that in taking this step, NRCS did not comply

¹² NRCS also concluded that using the same method for both programs would result in producers being treated more consistently.

¹³ We found that, in practice, compensation was usually equal to the published rate under the geographic area rate cap, unless the landowner offered less.

with OGC's recommendation that the agency document how it arrived at this decision, nor did it seek and receive legislative change.

When it learned of NRCS' decision, OGC met with the NRCS Chief on July 13, 2009, to express its concerns about NRCS' decision to cease using appraisals for valuation of regular floodplain easements. The NRCS Chief agreed with these concerns and stated that he would reconsider his memo.

Although OIG recognizes NRCS' desire to streamline the process for determining the value of easements purchased with Recovery Act funds, we maintain that if NRCS is going to change its procedures for Recovery Act funds, it must follow OGC's legal advice and provide sufficient justification for that decision. When we asked for the basis for NRCS' determination to arrive at this change in policy and procedures, the agency could not provide us with any documentation supporting its determination beyond its letter provided to OGC in May 2009. We maintain that appropriate easement compensation is best determined by an appraiser on a case-by-case basis, reflecting the unique characteristics of the land being appraised, the market conditions in the area, and the rights retained by the landowner. If NRCS believes that this process is too cumbersome for easements purchased with Recovery Act funds, then it must follow OGC's advice and provide sufficient justification for any decision it makes to change the method it has used for the regular program.

After our discussion with NRCS Headquarters officials, we issued a Fast Report to NRCS dated November 19, 2009. In the Fast Report, we made three recommendations as outlined below. The full text of NRCS' response can be found at http://www.usda.gov/oig/recovery/recovery_reports.htm.

Recommendation 5

Stop approving any further Option Agreements to Purchase using the WRP easement valuation method for EWPP floodplain easements until NRCS demonstrates that the currently required appraisal method is not practicable for Recovery Act-funded floodplain easements.

Agency Response

NRCS initially submitted that its decision adopting an alternative easement compensation methodology is justified because the use of the extensive individual appraisal procedures prevents NRCS from meeting the strict timeframes required by the Recovery Act. Additionally, NRCS submits the alternative methodology meets the Recovery Act timeframes and the Uniform Relocation and Real Property Acquisition Policy Act of 1970 (hereinafter the Uniform Act) appraisal policy principles to the extent practicable. The alternative valuation method satisfies the limitation inherent in the ARRA timeline which renders the standard Federal appraisal approach impractical.

NRCS also provided followup information on June 11, 2010, on its prior responses and actions taken since December 1, 2009, including its coordination with OGC related to the use of the WRP valuation procedures for floodplain easement transactions.

OIG Position

We accept management decision for this recommendation.

Recommendation 6

Rescind the specific direction provided to the State Conservationists on June 3, 2009, authorizing the use of the WRP easement valuation method for floodplain easements.

Agency Response

NRCS responded on December 1, 2009, that it placed a temporary hold on the use of the WRP valuation methodology for floodplain easements pending resolution of this issue. NRCS' response (dated June 11, 2010) shows that on January 15, 2010, NRCS sent a memorandum to States placing a temporary hold on the use of the WRP valuation methodology for pending, non-Recovery Act floodplain easement transactions.

OIG Position

We accept management decision for this recommendation.

Recommendation 7

In consultation with USDA's OGC, determine and implement appropriate valuation procedures for the floodplain easement programs. Document the support and rationale for any procedures implemented.

Agency Response

NRCS' December 1, 2009, response stated that it was discussing with OGC the appropriate valuation procedures for the floodplain easement programs. NRCS will provide to OIG, in subsequent correspondence, the documented support and rationale for any procedures implemented. NRCS' followup response, dated June 11, 2010, shows that NRCS presented to OGC additional information regarding the basis for the agency determination that the alternative easement valuation methodology for EWPP-FPE transactions adheres to the policies identified in section 301 of the Uniform Act. NRCS indicated it has consulted with OGC and, in furtherance of OGC's advice, revised its alternative easement valuation methodology for EWPP-FPE transactions for agricultural and other non-residential lands.

NRCS stated that "OGC responded that NRCS did have authority under the Uniform Act to adopt an alternative easement methodology and advised: (1) NRCS should document review by a professional appraiser that the NRCS process conforms to section 301 policies; (2) NRCS should explain more clearly in its guidance how the valuation methodologies are applied to a particular easement transaction, and revise any aspect of its methodology to the extent it was not in conformity with the Uniform Act's section 301 policies; and (3) NRCS should document its easement valuation methodology process through rulemaking."

Pursuant to OGC's advice, NRCS sent for review its draft EWPP-FPE valuation methodology to an independent and certified general appraiser who opined that the

alternative method using an area-wide analysis or survey would be acceptable as an appraisal under the Uniform Act. NRCS revised its draft guidance in response to both OGC's and the independent appraiser's recommendations.

OGC and the independent appraiser identified that section 301 required that the amount offered to the landowner could not be less than the fair market value. Therefore, NRCS revised the method for developing the geographic area rate cap (GARC), requiring that the GARCs be based upon the values derived through the area-wide assessments, and adjusted according to assessment of the impact that the easement has upon fee title value rather than minimizing easement compensation costs. NRCS clarified the requirements for who can conduct such an area-wide market assessment, identifying that the assessment must be conducted by an independent qualified professional. Once the area-wide market assessments have been obtained and corresponding GARCs developed, a landowner is offered easement compensation based upon the application of the site-specific characteristics that correspond to a particular area-wide market assessment value, as adjusted by the corresponding GARC.

NRCS also separated the methodology to be used for agricultural and other non-residential lands from the methodology for lands that are in residential use. In particular, the alternative easement valuation methodology is for easement transactions where the land is in agricultural or non-residential use. NRCS is currently developing different easement methodology procedures for transactions where the land is in residential use. NRCS also stated that transactions involving lands in residential use are still under temporary hold.

NRCS has distributed its revised guidance to Kentucky and Iowa, the two States with pending EWPP-FPE agricultural and other non-residential land transactions that were placed on temporary hold.

In its August 6, 2010, response, NRCS stated that it has drafted the comprehensive procedures for easement transactions where the land is in agricultural use or residential use. These procedures encompass coordination with sponsoring organizations, identification of acquisition costs from restoration costs, and utilization of appraisal procedures when purchasing easements on small parcels with residential structures. NRCS will incorporate these procedures in a final EWPP-FPE manual by September 30, 2010.

On May 6, 2010, the temporary hold for easement transactions on agricultural or non-residential land was lifted for those pending transactions affected. Additionally, NRCS has provided this guidance to State offices that are purchasing floodplain easements under the Great Lakes Restoration initiative.

The temporary hold for pending easement transactions on residential parcels will be lifted by the time the EWPP-FPE manual is issued.

OIG Position

We accept management decision for this recommendation

Scope and Methodology

We conducted our audit of EWPP-FPE at the NRCS National Headquarters office in Washington, D.C., and at the Kansas NRCS State Office in Salina, Kansas. To meet our timeframes, we judgmentally selected the Kansas NRCS State Office because of its proximity to our office in Kansas City, Missouri. We also accompanied the Kansas NRCS floodplain easement program coordinator to visit two sites that were approved and one site that was not initially funded.

Our audit covered EWPP-FPE applications for Recovery Act funding in fiscal year 2009. On March 10, 2009, NRCS was provided guidance and authorization to begin implementation of the program. After the application and selection process was completed, NRCS was authorized to begin distributing Recovery Act funds. As of October 5, 2009, NRCS had obligated about \$105 million to approximately 254 selected applications.

To accomplish our overall objectives, we reviewed the program's policies and procedures and the design of its internal controls. During this initial phase, we specifically reviewed management controls that ensure NRCS State offices can properly process EWPP-FPE applications with the additional funding provided by the Recovery Act. We interviewed NRCS Headquarters officials, Headquarters program directors, and program coordinators in the Kansas NRCS State Office to obtain their comments on the current resources for EWPP-FPE.

In order to monitor NRCS' performance goals established to measure the EWPP-FPE program's effectiveness in meeting the purposes of the Recovery Act, we discussed performance measures in our interviews with NRCS Headquarters and State office officials. We also reviewed performance measures included in NRCS' Recovery Act Plan specifically for EWPP-FPE.

To evaluate NRCS' compliance activities in relation to overseeing Recovery Act funding requirements, we interviewed NRCS Headquarters and State office officials about the controls and procedures for the approval of applications using Recovery Act funds. We also discussed EWPP compliance activities with those officials.

To accomplish our objective, we also:

- Identified and reviewed NRCS' published guidance, instructions, handbooks, and regulations that detail the controls and procedures over EWPP-FPE;
- Reviewed NRCS' Recovery Act Plan for EWPP-FPE; and
- Obtained and reviewed documents, such as OMB guidance, to gain an understanding of the provisions and requirements related to NRCS' EWPP-FPE.

We performed our audit fieldwork from April through November 2009. We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions

based on our audit objectives. During this initial phase, we did not review, analyze, or verify information in the agency's database, and we make no representation of the adequacy of the system or the information generated. We plan to perform needed testing during the second phase of our audit.

Abbreviations

| | |
|-------------------|---|
| ARRA | American Recovery and Reinvestment Act (Recovery Act) |
| EWPP | Emergency Watershed Protection Program |
| FPE..... | Floodplain Easements |
| GARC | Geographic Area Rate Cap |
| NRCS | Natural Resources Conservation Service |
| OGC | Office of the General Counsel |
| OIG | Office of Inspector General |
| OMB | Office of Management and Budget |
| P.L. | Public Law |
| Uniform Act | Uniform Relocation and Real Property Acquisition Policy Act of 1970 |
| USDA..... | United States Department of Agriculture |
| WRP | Wetlands Reserve Program |

Agency's Response

USDA'S

**NATURAL RESOURCES CONSERVATION
SERVICE**

RESPONSE TO AUDIT REPORT

United States Department of Agriculture



Natural Resources Conservation Service
P.O. Box 2890
Washington, D.C. 20013

June 11, 2010

SUBJECT: OIG – Followup Response to the Office of the Inspector General Report 10703-1-KC (2)—American Recovery and Reinvestment Act (ARRA)—Emergency Watershed Protection and Floodplain Easements

TO: Gil H. Harden
 Assistant Inspector General for Audit
 Office of the Inspector General

This memorandum is to followup on two of the Natural Resources Conservation Service's (NRCS) responses to the Office of the Inspector General (OIG) recommendations in OIG Report 10703-1-KC(2) in our December 1, 2009, memorandum. The two responses related to the use of the Wetlands Reserve Program (WRP) valuation procedures for floodplain easement transactions that were not funded under ARRA.

First, OIG recommended that NRCS rescind specific direction provided to the State Conservationists on June 3, 2009, expanding the use of the WRP's easement valuation method for floodplain easements funded with non-ARRA funds. NRCS responded on December 1, 2009, that it placed a temporary hold on the use of the WRP valuation methodology for such transactions pending resolution of the issue.

Second, OIG recommended NRCS determine and implement appropriate valuation procedures for the floodplain easement programs in consultation with the Office of the General Counsel. NRCS responded on December 1, 2009, that it was currently discussing the appropriate valuation procedures for the floodplain easement programs and that NRCS will provide to OIG, in subsequent correspondence, the documented support and rationale for any procedures implemented.

Attached are the actions NRCS has taken since December 1, 2009, in furtherance of its responses.

If you require additional information, please contact Tony Kramer, Deputy Chief for Easements and Landscape Planning, at (202) 205-7704

/s/

Dave White
Chief

Attachment

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Response to OIG Report 10703-1-KC(2)—Followup

The Natural Resources Conservation Service (NRCS) purchases floodplain easements as an emergency measure authorized under the Emergency Watersheds Protection Program (EWPP), 16 USC 2203; 7 CFR part 624. NRCS uses the Wetlands Reserve Program (WRP) easement valuation method for the EWPP floodplain easements (EWPP-FPE) purchased with funds made available by the American Recovery and Reinvestment Act of 2009 (ARRA). On June 3, 2009, a memorandum from Chief White expanded the use of the WRP easement valuation methodology to non-ARRA funded EWPP-FPE transactions.

Pursuant to the Office of Inspector General (OIG) and NRCS discussions, on January 15, 2010, NRCS sent a memorandum to States placing a temporary hold on the use of the WRP valuation methodology for pending, non-ARRA EWPP-FPE transactions.

Subsequent to placing its temporary hold on pending EWPP-FPE transactions, NRCS presented to the Office of the General Counsel (OGC) additional information regarding the basis for the agency determination that its alternative easement valuation methodology for EWPP-FPE transactions adheres to the policies identified in section 301 of the Uniform Relocation Assistance and Real Property Policy Act of 1970 (the Uniform Act). NRCS elaborated about how the valuation's procedural requirements meet the Uniform Act's statutory definition for an appraisal. OGC responded that NRCS did have authority under the Uniform Act to adopt an alternative easement methodology and advised:

- (1) NRCS should document review by professional appraiser that the NRCS process conforms to section 301 policies;
- (2) NRCS should explain more clearly in its guidance how the valuation methodologies are applied to particular easement transactions, and revise any aspect of its methodology to the extent it was not in conformity with the Uniform Act's section 301 policies; and
- (3) NRCS should document its easement valuation methodology process through rulemaking.

Pursuant to OGC's advice, NRCS sent for review its draft EWPP-FPE valuation methodology to Andrew Parsley, an independent and certified general appraiser. Mr. Parsley opined that the alternative method using an area-wide analysis or survey would be acceptable as an appraisal under the Uniform Act. NRCS revised its draft guidance in response to both OGC's and the independent appraiser's recommendations.

OGC and the independent appraiser identified that section 301 required that the amount offered to the landowner could not be less than the fair market value. Therefore, NRCS revised the method for developing the geographic area rate cap (GARC), requiring that GARCs be based upon the values derived through the area-wide assessments, and adjusted according to assessment of the impact that the easement has upon fee title value rather than minimizing easement compensation costs. NRCS also clarified the requirements for who can conduct such an area-wide market assessment (AWMA),

identifying that the AWMA must be conducted by an independent qualified professional. The guidance now specifies that a qualified professional means:

- (1) A certified, licensed appraiser;
- (2) A college-level professor or researcher of agricultural economics or similar discipline who has specialized expertise in agricultural and rural land values in the area to be encompassed by the area-wide assessment;
- (3) An individual who is employed by a national, State, or local agricultural or rural land statistics service and whose job responsibilities require expertise and familiarity with agricultural and rural land values in the area to be encompassed by the area-wide assessment;
or
- (4) An individual who has comparable knowledge, expertise, and familiarity of agricultural and rural land values in the area to be encompassed by an area wide assessment as an individual identified in (1)-(3) herein.

The revised guidance also provides greater explanation regarding how the valuation methodology is applied to particular easement transaction. Once the AWMA's have been obtained and corresponding GARC's developed, a landowner is offered easement compensation based upon the application of the site-specific characteristics that correspond to a particular AWMA value(s), as adjusted by the corresponding GARC. The guidance provides several examples.

NRCS also separated the methodology to be used for agricultural and other non-residential lands and lands that were in residential use. In particular, the alternative easement valuation methodology is for easement transactions where the land is in agricultural or non-residential use. NRCS is currently developing different easement methodology procedures for transactions where the land is in residential use. While the valuation methodologies are within the current statutory and regulatory framework, NRCS will review the EWPP-FPE regulatory provisions to determine what additional level of detail, if any, would help clarify the valuation policy for the public and initiate rulemaking accordingly.

In the December 1, 2009, response to OIG, NRCS identified that it would provide documented support and rationale for any procedures implemented. NRCS, having consulted with OGC and in furtherance of OGC advice, revised its alternative easement valuation methodology for EWPP-FPE transactions for agricultural and other non-residential lands. NRCS distributed this revised guidance to Kentucky and Iowa, the two States with pending EWPP-FPE transactions that were placed on temporary hold. Transactions involving lands in residential use are still under temporary hold.

The documented support and rationale for the procedures adopted for agricultural and other non-residential lands under EWPP-FPE are shown below.

DOCUMENTED SUPPORT:

Section 1119(o) of the Safe, Accountable, Flexible, Efficient Transportation Equity Act (SAFE-TEA) states: "The requirements of the January 4, 2005, Federal Highway Administration, a final rule on the implementation of the Uniform Relocation Assistance and Real Property Acquisition

Policy Act of 1970 (42 U.S.C. 4601 et seq.) will not apply to the voluntary conservation easement activities of the Department of Agriculture or the Department of the Interior.” The Federal Highway Administration is the lead Federal agency for policy guidance in implementing the Uniform Act and promulgated regulations for all other Federal agencies to use. Thus, NRCS is exempt from the current government-wide regulations implementing the Uniform Act. However, NRCS will amend its EWPP-FPE regulation to incorporate the new alternative easement valuation methodology.

Under the WRP easement valuation methodology, NRCS pays the lowest of the following as easement compensation: (i) The fair market value of the land using the Uniform Standards for Professional Appraisal Practices; or (ii) based on an area-wide market analysis or survey (hereafter “market assessment”), a geographic area rate cap determined by the State Conservationist, with input from the State Technical Committee, using the best information readily available in the State (hereafter “GARC”); or (iii) the landowner offer. 7 CFR 1467.8(a)(3).

OGC has noted that the SAFE-TEA exemption does not exempt NRCS from the Uniform Act itself. Therefore, NRCS reviewed the Uniform Act to ascertain the extent to which its provisions apply to its voluntary conservation easement transactions. In particular, NRCS examined the Uniform Act’s compensation requirements found in section 301 of the Uniform Act to ensure that the agency’s easement acquisition policies and procedures conform to legal requirements, including its easement valuation methodology for all EWPP floodplain easement transactions. NRCS believes that the alternative easement valuation methodology and procedures meet section 301 policy guidelines, including the statutory requirements for appraisals. Section 301 requires that the head of an agency, to the greatest extent practicable, be guided by 10 enumerated policies. Only the appraisal policies, as set forth in section 301(2) and (3), are in question. The other policies outlined in section 301 are not applicable to EWPP-FPE transactions since they relate to involuntary condemnation actions.

Section 301(2) provides that the property should be appraised prior to initiation of negotiations and the representative given an opportunity to accompany the appraiser during the inspection of the property. Section 301(3) provides: (1) the amount believed to be just compensation (also known as fair market value) be determined prior to initiation of negotiations; (2) the amount will not be less than the agency's approved appraisal of the fair market value of such property; (3) any impact to value created by the project be disregarded; and (4) the owner be provided with a written statement of, and summary of the basis for, the amount established.

In essence, the alternative easement valuation methodology inverses the procedural order in which individual appraisals are conducted. In the regular order, individual appraisals start first with documenting the attributes of a particular property, and then property value is determined through seeking and applying comparable values in the market place to the attributes of that parcel. Under the alternative easement valuation process, the comparable values are identified through market assessments of different land types and then those values applied to the attributes of the particular property. By ascertaining up front comparable values through market assessments, NRCS has simply minimized the administrative delay created by each individual appraiser researching the comparable value of attributes separately for each parcel.

NRCS believes the alternative easement compensation methodology meets the appraisal policies found in section 301(2) for the following reasons:

- NRCS conducts a site assessment of an easement area to determine the extent of each land use category and the landowner is given the opportunity to accompany NRCS during that assessment.
- The site assessment occurs prior to the presentation of the offer to the landowner, and is thus prior to initiation of negotiations regarding purchase price.
- The Uniform Act defines an appraisal as a “written statement independently and impartially prepared by a qualified appraiser setting forth an opinion of defined value of an adequately described property as of a specific date, supported by the presentation and analysis of relevant market information.” The NRCS site assessment and application of the market assessment to determine easement compensation value, as capped by the geographic area rate cap, meets the Uniform Act’s definition of appraisal as follows—

| Section 301 appraisal definition | Alternative Easement Compensation Valuation Methodology | Additional Comment |
|--|--|---|
| “written statement” | A “written statement of value” is developed for each easement area based upon the market assessment | |
| “independently and impartially prepared” | The market assessment is developed by individuals independent of the NRCS staff involved in the transaction, and thus, are “independently and impartially prepared.” Additionally, the identification of particular land characteristics of the easement area can be independently and impartially verified. | |
| “by a qualified appraiser” | NRCS identified in its alternative easement valuation methodology that | The Uniform Act does not specify the appraisal methodology or identify who is a qualified appraiser. These details are identified in the DOT regulation to which NRCS is exempt. Section 301 was written prior to the passage of the Title XI |

| | | |
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| | | <p>“Financial Institutions Reform, Recovery, and Enforcement Act of 1989.” Subsequent to this law, the Appraisal Foundation published USPAP which created the standards for appraisal practice by licensed and certified appraisers. Therefore, the section 301 definition did not include these requirements.</p> |
| <p>“setting forth an opinion of defined value”</p> | <p>Once AWMA’s have been obtained and corresponding GARC’s developed (see below), a landowner will be offered easement compensation based upon the application of the site-specific characteristics (per acre per land type) that correspond to a particular AWMA value(s), as adjusted by the corresponding GARC.</p> | |
| <p>“of an adequately described property”</p> | <p>The easement area is specifically identified and acreage of land type circumscribed by GPS, loaded into Customer Service Toolkit and a map generated. The market assessment values are applied based upon the acreages determined through Toolkit. Ultimately, the map of the easement area attached to the option agreement to purchase as the proposed easement area upon which the identified compensation will be paid.</p> | |
| <p>“as of a specific date”</p> | <p>The market assessments are dated and are valid for one year only.</p> | <p>USPAP and Yellow Book appraisals, under program policies, are determined valid</p> |

| | | |
|---|---|--------------|
| | | for one year |
| “supported by a presentation and analysis of relevant market information” | The market assessments are based on value of comparable sales in the local area. In order for the values derived to be accepted as valid and reasonable, the area assessed must be as homogeneous as possible. The determination of the assessment area is based on several considerations, including: the types of land use are similar, the size of land units is similar, the types and amounts of improvements are similar, the potential influence of other factors such as development pressure are similar, the potential highest and best use of the area would be similar, the general topography and natural features of the area would be similar, the locations are similar, and there are similar irrigation water rights. | |

Therefore, the alternative easement valuation methodology conforms to the definition of appraisal within the meaning of the Uniform Act and the policy identified in section 301(2). In summary, floodplain easement compensation rates, utilizing this methodology, are based upon a written statement prepared by an independent qualified professional (often a licensed appraiser) familiar with land values, and the compensation amount is dependent upon site-specific attributes of the land being offered for an easement. The landowner accompanies the NRCS field personnel who inspects the easement area and identifies the respective land categories upon which the market assessment is applied. The landowner can correct any discrepancies during the visit or when the landowner receives the written summary and statement of value (described more fully below).

NRCS believes the alternative easement compensation methodology meets the appraisal policies found in section 301(3) for the following reasons:

- The floodplain easement compensation value determined through the alternative easement valuation methodology is based upon an amount believed to be just compensation (also

known as fair market value) and such value is determined prior to initiation of negotiations. The area-wide assessment and the corresponding GARC is a determination of fair market value of the easement. The easement compensation value for any particular transaction is determined prior to the presentation of an option agreement to purchase to a landowner, i.e. the initiation of negotiations. In fact, the GARCs upon which easement compensation values will be based are made publicly available prior to NRCS accepting applications. Thus, any prospective landowner may ascertain for themselves whether they desire to apply for the program.

- The easement compensation amount is not less than the agency's approved determination of the fair market value of the easement.
- The easement compensation amount is not influenced by any impact to value created by the project itself.
- The landowner is provided with a “written statement of and summary of the basis for the amount established.” In particular, NRCS prepares a transmittal letter with the option agreement to purchase that identifies the method through which the easement compensation amount identified in the option agreement to purchase was developed.

RATIONALE:

NRCS prefers to use the alternative easement compensation methodology to individual appraisals for EWPP-FPE transactions for several reasons, including but not limited to:

- The alternative easement valuation methodology meets the Uniform Act’s statutory definition of appraisal.
- The acquisition procedures meet all other aspects of section 301 policies.
- The valuation methodology meets both EWPP-FPE statutory purposes and the Uniform Act’s statutory purposes. In particular, NRCS encourages and expedites acquisition of real property by agreement through identifying that NRCS will only acquire an easement on a voluntary basis (7 CFR 624.10(a)); using an expedited method for determining easement value; implementing a transparent process through which values are determined thus promoting public confidence; and assuring consistent treatment of owners in other Federal programs by adopting an easement compensation methodology used in an analogous program in similar landscapes.
- The EWPP regulation at 7 CFR § 624.9 places a self-imposed fund obligation on agency officials of 220 days. While this deadline does not have the same status as the statutory time limits of ARRA, the deadline furthers EWPP purposes by encouraging agency officials to provide disaster relief in a time-sensitive manner to landowners impacted by natural disasters. NRCS documented the time frame associated with acquiring an individual appraisal, and NRCS cannot consistently and reliably meet 7 CFR § 624.9 220-day obligation and completion deadline, especially when current year flooding events may delay access to properties for the purpose of conducting a site-specific appraisal.
- For individual appraisals, access to the site is the first step in the process and essential before any other of the steps in the appraisal process can occur. Conversely, under the alternative easement compensation methodology, the site assessment can occur any time prior to sending the offer to the landowner, and thus contributes to the ability to act on an emergency

basis. Based upon NRCS current experience with the ARRA-funded transactions, the time table for the overall acquisition process has been substantially reduced by nearly 6 to 8 months.

- Similar easement valuation policy between WRP, ARRA-funded floodplain easement transactions, and non-ARRA funded EWPP floodplain easement transactions ensures that NRCS offers the same compensation whether a participant applies to sell a floodplain easement or a WRP easement, and thus provides consistent treatment between participants in these programs, no matter the source of funding.
- Since floodplain easement land eligibility overlaps with WRP land eligibility, and the easement deeds for the two programs are virtually identical, the consistent compensation methodology eliminates NRCS from competing with itself for enrollment of lands under its respective programs. This shared policy thus furthers the policy goals of section 301.

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*Projects that did not have a current project plan, with a recent review date, updated environmental documentation, and that were not ready for immediate funding.

United States Department of Agriculture



Natural Resources Conservation Service
P.O. Box 2890
Washington, D.C. 20013

August 6, 2010

SUBJECT: American Recovery and Reinvestment Act (ARRA) of 2009—Watershed Operations and Flood Protection Funding of Floodplain Easements Audit Report 10703-1-KC Phase (1)

TO: Gil H. Harden
Acting Assistant Inspector General for Audit
Office of the Inspector General

This memorandum is in response to Office of Inspector General (OIG) Audit Report 10703-1-KC Phase (1), dated July 2010.

For three of the four findings, OIG indicated that it could not accept the management decision until the Natural Resources Conservation Service (NRCS) identified the timeline for its adoption of comprehensive procedures. NRCS provides this timeline in this memorandum.

For the fourth finding where OIG could not accept the management decision, OIG indicated that NRCS should identify current easement applications where homes are the primary restoration cost, describe how the agency will complete the review, and provide the timeframes for planned or implemented corrective action. NRCS has provided additional information indicating that it will review at the national office level all active ARRA-funded transactions where homes are the primary acquisition and restoration cost.

If you require additional information, please contact Lesia A. Reed, Deputy Chief, Strategic Planning and Accountability, at (202) 720-6297.

/s/

Dave White
Chief

Attachment

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Mr. Gil Harden
Page 2

cc:

Virginia (Ginger) L. Murphy, Associate Chief, NRCS, Washington, D.C.

Anthony J. Kramer, Deputy Chief for Easements and Landscape Planning, NRCS,
Washington, D.C.

Melissa Hammond, ARRA Coordinator, Strategic Natural Resources Initiatives,
NRCS, Washington, D.C.

Leroy Hall, Acting External Function Lead, Compliance Division, SPA, NRCS,
Washington, D.C.

**Agency Additional Information in Response to the Office of the Inspector General (OIG)
Report 10703-1-KC—Phase (1)**

OIG Recommendation 2: Establish comprehensive EWPP-FPE procedures which address the purchasing of easements on residential home sites.

Summary NRCS Initial Response: NRCS will establish standard operating procedures for purchasing easements on small parcels with structures and will incorporate these procedures into the Emergency Watershed Protection Program Floodplain Easements (EWPP-FPE) Manual.

OIG Position: In order to accept the management decision, NRCS needs to provide the date the comprehensive procedures will be incorporated.

NRCS Additional Information: The Natural Resources Conservation Service (NRCS) has drafted the comprehensive procedures that encompass coordination with sponsoring organizations, identification of acquisition costs versus restoration costs, and utilization of appraisal procedures when purchasing easements on small parcels with residential structures. This draft manual was distributed to a review board of NRCS State staff and comments are being received and reviewed. NRCS will incorporate the comments and clarifications received, and distribute the standard operating procedures in a final EWPP-FPE manual to be posted by September 30, 2010.

OIG Recommendation 3: Follow up with State offices to correct applications and ensure proper accounting of restoration/acquisition costs.

Summary NRCS Initial Response: NRCS concurs that the agency should handle the costs associated with the value of structures, their demolition, and removal in a consistent manner. There are two costs associated with structures and improvements: the acquisition costs associated with the increased value that land with structures and improvements have, and the restoration costs associated with demolition and removal of the structures and improvements. Under the terms of the EWPP floodplain easement, NRCS acquires rights, title, and interest in the encumbered property, reserving to the landowner only five enumerated rights. The landowner does not reserve any rights to the structures and improvements. Thus, NRCS acquires the rights to all structures and improvements affixed to the land when it acquires an EWPP floodplain easement, and believes that fair treatment of landowners supports the agency compensating a landowner for the contribution to land value that such structures and improvements provide. There is a separate cost associated with the demolition and removal of the structures and improvements from the easement area. These costs are appropriately considered restoration costs.

OIG Position: In order to accept the management decision, NRCS needs to address the issues noted in the comprehensive drafted procedures and provide the date these procedures will be implemented.

NRCS Additional Information: In November 2009, NRCS sent specific revised guidance to the three States (West Virginia, Ohio, and Alaska) with pending American Recovery and Reinvestment Act (ARRA)-funded transactions involving structures. In particular, NRCS clarified that for projects funded under ARRA, the geographic area rate cap for land with structures is

determined by combining the geographic area rate cap for the land with the value of the structures as determined by the local taxing authority.

For non-ARRA funded transactions, NRCS has drafted comprehensive procedures that encompass coordination with sponsoring organizations, identification of acquisition costs versus restoration costs, and utilization of appraisal procedures when purchasing easements on small parcels with residential structures. This draft manual was distributed to a review board of NRCS State staff and comments are being received and reviewed. NRCS will incorporate the comments and clarifications received, and distribute the standard operating procedures in a final EWPP-FPE manual to be posted by September 30, 2010.

OIG Recommendation 4: Identify all approved applications where the cost of purchasing and removing homes constitutes the primary restoration cost, perform a review of each identified application, and make the appropriate corrections.

Summary NRCS Initial Response: NRCS will continue to administer the EWPP-FPE program in conformance with all appropriate statutes and regulations, and will use our oversight and evaluation process to ensure the validity of all EWPP-FPE applications.

OIG Position: OIG is unable to accept the management decision for this recommendation based on the information provided. NRCS should identify current easement applications where homes are the primary restoration cost, describe how the agency will complete the review, and provide the timeframes for planned or implemented corrective action.

NRCS Additional Information: NRCS will review at the national office copies of the case files associated with any active ARRA-funded transaction where the cost of purchasing and removing a home constitutes the primary restoration cost. For the purposes of this review, NRCS will consider a transaction active if the easement acquisition remains pending or where an easement has been acquired. NRCS will not include in this review any transaction where either NRCS or the landowner has decided not to pursue the transaction. This review will occur within the next 3 months, and NRCS will make any appropriate corrections as soon as possible, not to exceed 6 months.

OIG Recommendation 7: In consultation with USDA's Office of the General Counsel (OGC), determine and implement appropriate valuation procedures for the floodplain easement programs. Document the support and rationale for any procedures implemented.

Summary NRCS Initial Response: NRCS consulted with OIG and developed revised guidance. NRCS has distributed its revised guidance to Kentucky and Iowa, the two States with pending EWPP-FPE agricultural and other non-residential land transactions that were placed on temporary hold, and authorized these two States to proceed with the pending transactions. Additionally, NRCS is incorporating the revised guidance into the EWPP manual.

OIG Position: OIG is unable to accept the management decision for this recommendation. NRCS needs to provide the timeframe for implementing the alternative easement compensation methodology for easement transactions where the land is in agricultural or non-residential use and

the timeframes for implementing the separate easement procedures where the land is in residential use and the timeframe for removing the temporary hold.

NRCS Additional Information: NRCS has drafted the comprehensive procedures for easement transactions where the land is in agricultural or non-residential use. NRCS has also drafted the comprehensive procedures for where the land is in residential use. These procedures encompass coordination with sponsoring organizations, identification of acquisition costs versus restoration costs, and utilization of appraisal procedures when purchasing easements on small parcels with residential structures. The draft manual encompassing both procedures was distributed to a review board of NRCS State staff and comments are being received and reviewed. NRCS will incorporate the comments and clarifications received, and distribute the standard operating procedures in a final EWPP-FPE manual to be posted by September 30, 2010.

On May 6, 2010, the temporary hold for easement transactions on agricultural or non-residential land was lifted for those pending transactions affected. Additionally, NRCS has provided this guidance to State offices that are purchasing floodplain easements under the Great Lakes Restoration Initiative.

The temporary hold for pending easement transactions on residential parcels will be lifted by the time the EWPP-FPE manual is issued.