



U.S. Department of Agriculture
Office of Inspector General
Southwest Region
Audit Report

NATURAL RESOURCES
CONSERVATION SERVICE
FARMLAND PROTECTION PROGRAM



Report No.
10601-5-Te
AUGUST 2002



UNITED STATES DEPARTMENT OF AGRICULTURE
OFFICE OF INSPECTOR GENERAL
Washington D.C. 20250



DATE: August 5, 2002

REPLY TO
ATTN OF: 10601-5-Te

SUBJECT: NRCS' Farmland Protection Program

TO: Bruce Knight
Chief
Natural Resources Conservation Service

ATTN: Dana York
Director
Operations Management and Oversight Division

This report presents the results of our audit of the Natural Resources Conservation Service's (NRCS) Farmland Protection Program. The NRCS' response to the draft report, dated July 1, 2002, is included as exhibit B and the Office of Inspector General's position incorporated into the relevant sections of the report.

While we generally agree with your position, we need additional information to reach management decisions on all recommendations (Recommendations Nos. 1, 2, 3, and 4). The information needed is set forth in the sections of the report marked "OIG Position."

In accordance with Departmental Regulation 1720-1, please furnish a reply within 60 days describing the corrective action taken or planned and the timeframes for implementation of each audit recommendation. Please note that the regulation requires management decisions to be reached on all findings and recommendations within a maximum of 6 months from report issuance and final actions to be taken within 1 year of the management decisions.

We appreciate the courtesies and cooperation extended to us by members of your staff during the audit.

/s/ R. D. Long
RICHARD D. LONG
Assistant Inspector General
for Audit

EXECUTIVE SUMMARY

NATURAL RESOURCES CONSERVATION SERVICE FARMLAND PROTECTION PROGRAM

AUDIT REPORT NO. 10601-5-Te

RESULTS IN BRIEF

This report presents the results of our review to evaluate the Natural Resources Conservation Service's (NRCS) management controls over the Farmland Protection Program (FPP). We tested the effectiveness of the management controls to identify reportable conditions that had program-wide impact.

The FPP was established to protect farmland from conversion to nonagricultural uses. This is accomplished by funding the acquisition of conservation easements on agricultural lands designated as prime, unique, or otherwise productive. During fiscal years (FY) 1998 through 2000, 19 States received over \$17.5 million to participate in the FPP. We reviewed selected acquisitions in Maryland and California. Acquisitions at both States totaled over \$1.4 million in FY 1998.

At the two NRCS State Offices, we identified that there was no process to monitor program compliance and no controls to ensure that the terms of the cooperative agreements were modified to include the proper requirements that the cooperators must follow in order to be eligible for reimbursement for easement acquisitions. Also, the State offices did not have a review process to ensure that these reimbursement payments to cooperators were based on compliance to the terms of the cooperative agreements. As a result we identified the following conditions relating to cooperative agreements:

- Three cooperators in Maryland used other land appraisal methods, even though the cooperative agreements required cooperators to use valuations of easement acquisitions using Federal land appraisal standards only. The Office of the General Counsel (OGC) ultimately deemed these alternative methods to be acceptable.
- Two easement acquisitions, one in California and one in Maryland, allowed for consideration for termination after 25 years, even though the cooperative agreements required easement acquisitions for a minimum 30-year duration. OGC also determined this to be allowable under FPP.

- One easement acquisition in California already had a prior conservation restriction in place prior to having the easement acquisition funded by FPP. The cooperative agreement did not include terms to certify that the conservation easement appraisal takes into account the reduction in value of the easement caused by the prior restriction.

In all easement acquisitions noted above, the cooperators were paid by the State offices despite the deficiencies to the terms of the cooperative agreements. Our discussions with the NRCS National Office also disclosed that there were no controls in place to monitor the State offices to ensure that they were properly reviewing the easement acquisitions prior to making the payments.

Our survey also noted one instance in California where \$580,000 in FY 1996 funds still remained obligated at the time of our review. We concluded that the State has had ample time to expend the funds and that any funds remaining should be deobligated for use in other acquisitions.

During and after the conclusion of the fieldwork of this review, the NRCS National Office responded to these conditions by taking immediate steps to increase its monitoring of the FPP. NRCS initiated a major revision to the FPP field operations manual and will provide training in these revisions based on what our survey disclosed. NRCS agreed to implement periodic monitoring of the FPP by its Oversight and Evaluation Staff and will create national software, which will allow National and State Managers to track the easement monitoring and conservation plan progress. NRCS also took steps to modify future cooperative agreements to reflect the proper terms and restrictions.

When implemented, we believe that these positive steps will address the conditions that we found during our survey. Based on NRCS' actions on our recommendations, we recommend no additional audit work.

KEY RECOMMENDATIONS

We recommend that NRCS establish controls at State offices to modify cooperative agreements to properly reflect the terms and requirements and to review easement acquisitions prior to making payments. We also recommend that NRCS establish a monitoring system to assess State offices' compliance to program requirements.

AGENCY RESPONSE

NRCS has drafted policy and revised its cooperative agreement template to not only ensure that State offices review and modify cooperative agreements as needed, but also

to make certain that standardized reviews are conducted by NRCS and the cooperating entity. The standardized reviews will be conducted on annual easement monitoring, land appraisals, and title standards as they relate to easement duration and possible title encumbrances. The complete NRCS response is shown in exhibit B.

OIG POSITION

NRCS generally agreed with our recommendations; however, to reach management decision, we need additional information. The information needed is described in the "OIG Position" section for each recommendation.

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INTRODUCTION

BACKGROUND

The 1996 Farm Bill established the FPP to protect farmland from conversion to nonagricultural uses. Section 388 of the Federal Agriculture Improvement and Reform (FAIR) Act authorized up to \$35 million in Commodity Credit Corporation (CCC) funds for the purchase of agricultural conservation easements and other interests in productive farmland but defined no method of easement valuation or minimum duration of an acquisition.

To be eligible to receive matching funds, State, tribal, and local governments must have established FPP's that have pending offers for the acquisition of conservation easements on prime, unique, or other productive soils as defined in the Farmland Protection Policy Act of 1981, as amended.¹ Program criteria stipulate that the farmland to be protected must be threatened by development, yet located near agricultural infrastructure and markets to ensure future viability. Applicants must demonstrate a commitment to farmland protection through the use of incentive-based or regulatory farmland protection techniques, and by proving their capacity to monitor and enforce conservation easements. State, tribal, and local governments are also required to provide at least 50 percent of the estimated fair market value of the interest they are acquiring.

To distribute FPP funds, NRCS publishes a request for proposals (RFP) in the Federal Register. The RFP is also posted online. State or local government entities are eligible to apply² and submit their proposal to the respective NRCS State Conservationist. The State Conservationist and staff compile the proposals, prioritize them using a methodology outlined in 7 CFR 658, and submit them to the NRCS National Office. The National FPP Coordinator uses the same methodology to prioritize the lists from each State and awards those proposals having the greatest impact. When a State or local application for matching funds is approved, NRCS executes a cooperative agreement on behalf of the CCC. The agreement describes the transaction, including information about the parcel, the type of interest to be acquired, the project cost, and an estimate of the Federal share. Enrollment in FPP limits the land to agricultural use for a minimum of 30 years. Preference is given to projects

¹ 7 U.S.C. 4201-4209, July 5, 1984.

² Prior to the FY 2001 funding, only State or local (county or municipality) governments were eligible for participation. Nonprofit entities became eligible with the FY 2001 funding.

that protect farmland in perpetuity. Conservation plans must be implemented on all land enrolled in the FPP. Failure to do so is considered a violation of the agreement. The cooperative agreement describes the role of NRCS in the development and implementation of a conservation plan, which is used as the basis for eligibility and inclusion into FPP. The agreement contains a reversionary clause requiring the State or local government to reimburse the Federal government if the terms of the cooperative agreement are not enforced or if the easement is terminated.

The cooperating entity shall be responsible for:

- Carrying out necessary legal and administrative actions to ensure proper acquisitions and recordation of the conservation easement or other interest instrument.
- Coordinating with NRCS and ensuring legal sufficiency of the conservation easement deed or other interest instrument, including the requirement of a conservation plan and a contingent right in the United States of America.
- Holding title to conservation easements or other protection devices.
- Ensuring that the easement is managed according to the conservation plan developed and approved according to the NRCS standards and specifications.
- Managing, monitoring, and enforcing the conservation easement acquired.
- Submitting status reports to NRCS when requested.

OBJECTIVES

The objectives were to identify and to evaluate material management controls in the FPP and to test compliance with those controls.

SCOPE

We evaluated NRCS' controls over compliance with 7 CFR 3016, "Uniform Administrative Requirements for Grants and Cooperative Agreements to State and Local Governments", eligibility determination, matching costs, easement valuation and duration, oversight and monitoring, and selection of easement acquisitions. We tested compliance with these requirements in Maryland and California.

During FY's 1998 through 2000, 19 States received over \$17.5 million to participate in the FPP. The cooperators within these States completed 151 FPP acquisitions.

NRCS officials suggested that we include Maryland in our review because, in their opinion, Maryland had an effective and efficient program. We also selected California because it had six pending FPP acquisitions and unexpended FPP funds of over \$1.3 million since 1996.

During FY 1998, 3 Maryland cooperators completed 19 acquisitions (12 percent of the National total) for over \$1.1 million (6 percent of the National total) and California completed 2 acquisitions (1 percent of the National total) for over \$250,000 (1 percent of the National total).

We selected for review 3 of 19 FPP acquisitions completed in 1998 in Maryland and 2 of 2 FPP acquisitions completed in 1998 in California. The Maryland acquisitions were also selected because we wanted a sample of State- and county-administered programs.

Fieldwork was performed during the period April through June 2001. Our review was performed in accordance with Generally Accepted Government Auditing Standards.

METHODOLOGY

To accomplish our objectives, we reviewed laws, policies, and guidelines addressing the administration of the program. At the NRCS National Office, we interviewed officials and reviewed the controls over the eligibility, prioritization, management, and cost sharing of the projects.

At the Maryland and California NRCS State Offices, we interviewed officials and reviewed records maintained by these offices.

We interviewed officials of, and reviewed records maintained by, four judgmentally selected cooperators within Maryland and California to accomplish the survey objectives. We selected all participating cooperators that completed acquisitions during our scope period. At the cooperator offices, we reviewed the judgmentally selected acquisitions to determine if the acquisitions met published eligibility requirements, had prior restrictions against nonagricultural use, if more than the appraised fair market value was paid for an acquisition, the duration of the acquired easements was no less than 30 years, and if costs were shared in the prescribed proportion. We also visited selected acquisitions to verify compliance.

FINDINGS AND RECOMMENDATIONS

CHAPTER 1	CONTROLS NEEDED OVER THE PURCHASE OF CONSERVATION EASEMENTS IN FPP
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FINDING NO. 1

NRCS had not established controls at the National office and State offices to review and to monitor the purchase of conservation easements in the FPP. At the time of our review, NRCS had just issued guidelines to the State offices on their program review responsibilities and the State offices had not yet implemented procedures to comply with the guidelines. The lack of controls resulted in the following conditions that we noted during our review of selected cooperative agreements:

- We found the three Maryland acquisitions we reviewed were not valued according to the terms specified in the cooperative agreements. Cooperators did not value the easements by the method prescribed in the Uniform Appraisal Standards for Federal Land Acquisitions (UASFLA), although the cooperative agreements required compliance with these standards. For two of the acquisitions, an appraisal was conducted to estimate the value of the parcels prior to encumbrance by the easement but did not value the parcel after imposition of the easement restrictions as required by the UASFLA. The third acquisition had no appraisal but was instead valued by a method used in other acquisitions by the county.
- We determined that two of the five easements reviewed (one in California and one in Maryland) allowed consideration to terminate the easement after 25 years instead of the minimum 30-year duration prescribed in the eligibility publication. Both the California State Coordinator and the Maryland County Coordinator cited local laws as the reason for the more lenient easement duration.

- We also determined that one of the two California acquisitions we reviewed was restricted from nonagricultural use by a Williamson Act contract³ prior to having an easement purchased as part of the FPP. While reviewing the title search documentation, we found this contract on the parcel. As we researched, we determined that this contract appeared to duplicate the purpose of the FPP. When we questioned the need for the easement when the property was already restricted from nonagricultural use, OGC said that the previous restriction did not guarantee protection in perpetuity, and the value was considered in the appraisal of the property. The OGC attorney concluded that the purchase was proper.

When notified of the above conditions, NRCS officials researched the State statutes and determined that the statutes do not materially compromise the FPP program. NRCS supported their decision by saying the State statutes do not violate the underlying FPP statute and FPP must act in conjunction with State programs. Our discussions with attorneys from OGC disclosed that cooperators should have followed the terms of their cooperative agreements but said that the statute establishing the FPP did not require compliance with these standards, and NRCS could retroactively amend the agreements to remove the requirements.

Even though the conditions we found did not result in noncompliance to FPP standards, we questioned why the State offices did not ensure that the terms of the cooperative agreements were modified accordingly. We also questioned why the State offices approved reimbursement to the cooperators despite the apparent conflict to the terms of their cooperative agreements. There was also a lack of program oversight at the National level to ensure that State offices are properly reviewing agreements prior to making payments.

NRCS Actions To Improve Controls

NRCS agreed that program oversight both at the State and National levels needed to be established and has taken positive actions at the time of our audit. In a letter dated August 27, 2001, NRCS addressed the need to improve controls by citing "several actions" taken by NRCS. These actions included, but were not limited to:

- A major revision of the FPP field operations manual (CPM, Part 519);

³ California Land Conservation (Williamson) Act, Government Code Section 51200-51297.4.

- National training for FPP State Managers to be held in November 2001, based on revision of the field operations manual and issues disclosed during this survey;
- Periodic monitoring of the program by NRCS Oversight and Evaluation Staff; and
- The creation of national software, which will allow State and National Managers to track the easement monitoring and conservation plan progress using digital data layers.

In this same letter, NRCS responded to the following issues:

- For the valuation issue, NRCS told us that they modified the FY 2001 cooperative agreements, after consultation with OGC, to allow for alternative real estate valuation techniques in its easement acquisition process. The alternative methods may be allowed when approved and utilized by State governments when expending State funds for land acquisition.
- Regarding the prior nonagricultural restriction, NRCS stated that they have added a paragraph to the cooperative agreements that stipulates, "For those parcels with Williamson Act contracts for which the [cooperator] seeks FPP funding, the [cooperator] agrees to identify the parcel as having a Williamson Act contract and certify that the conservation easement appraisal takes into account the reduction in value of the easement caused by the contract."
- Regarding the minimum easement duration, NRCS stated that California Public Resources Code, sections 10270-10277, requires the allowance for an easement to be terminated after 25 years. They also cited Maryland law, section 2-514(b), which stipulates that the landowner may request a review to determine if the easement is still a viable agricultural easement after 25 years. Since these State statutes do not violate the underlying FPP statute, and FPP must act in conjunction with State programs, they determined that these State statutes do not materially compromise the FPP.

When implemented, we believe that these steps will address the conditions that we found during our survey. The following recommendations are set forth in this report to track the implementation of NRCS' corrective action.

RECOMMENDATION NO. 1

Develop and establish controls at State offices to review and modify cooperative agreements using the appropriate terms and conditions with emphasis on land appraisal standards, easement duration periods and parcels under a Williamson Act contract.

NRCS Response

NRCS agrees with the Office of Inspector General (OIG). NRCS has drafted policy and revised its cooperative agreement template to not only ensure that State offices review and modify cooperative agreements as needed, but also to make certain that standardized reviews are conducted by NRCS and the cooperating entity. The standardized reviews will be conducted on annual easement monitoring, land appraisals, and title standards as they relate to easement duration and possible title encumbrances.

Specifically, NRCS has drafted new policy and procedures contained within the conservation Programs Manual, Part 519, on title assurance, appraisal review, and annual easement monitoring.

OIG Position

In order to reach management decision, we need a timeframe for the implementation of the policy and revised cooperative agreement template.

RECOMMENDATION NO. 2

Establish controls at the State offices to ensure that easement acquisitions are in compliance with the terms of the cooperative agreements and other requirements before payments are made to cooperators.

NRCS Response

NRCS agrees with OIG and has drafted procedures to ensure that appraisals are conducted, title reviews occur, and conservation-planning requirements are met before issuing payment. NRCS has accomplished this step by revising the procedures contained in the Conservation Programs Manual, Part 519, and through training with the FPP State program managers.

OIG Position

In order to reach management decision, we need a timeframe for the implementation of the procedures and the training for the FPP State program managers.

RECOMMENDATION NO. 3

Implement periodic monitoring of the FPP by the Oversight and Evaluations Staff.

NRCS Response

NRCS agrees with OIG and will have the NRCS Oversight and Evaluation Staff conduct periodic program reviews of the FPP.

OIG Position

In order to reach management decision, we need timeframes for implementation of the periodic program reviews.

CHAPTER 2	CALIFORNIA STATE OFFICE DID NOT TIMELY DEOBLIGATE FY 1996 FUNDS
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FINDING NO. 2

During our review, we noted one instance where the California State Office did not timely deobligate funds. Our review identified that \$580,000 in FY 1996 funds remained

obligated to the State of California due to problems in finalizing the purchase of easements in two locations. The cooperative agreement had been amended to extend the expiration date on three separate occasions, the latest to expire on September 30, 2001. We spoke with both the State and National FPP Coordinators who agreed that the State had ample time in which to expend the funds and that any funds not expended at the end of the current extension should be deobligated.

We explained our concern over the lack of progress in expending the FY 1996 funds to the manager of the California Farmland Conservancy Program (CFCP). We also expressed our intent to recommend deobligation of the FY 1996 funds unless the acquisitions were finalized and reimbursement requested by September 30, 2001, and both the State and National offices concurred with our recommendation. Because of our intended recommendation, the parties involved in the acquisition resolved the points of difference and completed the acquisitions. The CFCP, through the California NRCS State Office, provided the Requests for Reimbursement for the two projects funded with FY 1996 monies. These requests totaled \$575,000, and the State office explained that the remaining \$5,000 would be combined with FY 1998 funds to complete an acquisition by April 2002.

RECOMMENDATION NO. 4

Deobligate all FY 1996 funds provided to the State of California that remain unexpended as of October 1, 2001.

NRCS Response

The NRCS California State Office has disbursed funds to the cooperating entities for the purchase of two easements. The attached CCC statement documents disbursement of the 1996 funds.

OIG Position

The attachment to NRCS' response did not show when the funds were distributed. In order to reach management decision, we need documentation showing the date the funds were disbursed.

EXHIBIT A - SUMMARY OF MONETARY RESULTS

FINDING NUMBER	RECOMMENDATION NUMBER	DESCRIPTION	AMOUNT	CATEGORY
2	4	Untimely Expenditure of FY 1996 Funds	\$580,000	FTBPTBU <u>1/</u> : Management or Operating Improvement/Savings
Total			\$580,000	

1/ - Funds To Be Put To Better Use

EXHIBIT B – NRCS’ RESPONSE TO THE DRAFT REPORT

United States Department of Agriculture



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

SUBJECT: LNU – Farmland Protection Program Audit Report (10601-5-Te) JUL 01 2002

TO: Richard D. Long
Assistant Inspector General for Audit
Office of the Inspector General

The Natural Resources Conservation Service’s (NRCS) response to recommendations from the Office of the Inspector General’s Farmland Protection Program (FPP) Draft Audit Report (Report number 10601-5-Te) follows. Since an exit conference was held on February 6, 2002, and the changes in the second draft report are minor, NRCS does not feel that another exit conference is needed.

Recommendation #1 – Develop and establish controls at State offices to review and modify cooperative agreements using the appropriate terms and conditions, with emphasis on land appraisal standards, easement duration periods, and parcels with prior nonagricultural easements.

NRCS Response – NRCS agrees with the Office of the Inspector General. NRCS has drafted policy and revised its cooperative agreement template to not only ensure that State offices review and modify cooperative agreements as needed, but also to make certain that standardized reviews are conducted by NRCS and the cooperating entity. The standardized reviews will be conducted on annual easement monitoring, land appraisals, and title standards as they relate to easement duration and possible title encumbrances.

Specifically, NRCS has drafted new policy and procedures contained within the Conservation Programs Manual, Part 519, on title assurance, appraisal review, and annual easement monitoring.

Recommendation #2 – Establish controls at the State offices to ensure that easement acquisitions are in compliance with the terms of the cooperative agreements and other requirements before payments are made to cooperators.

NRCS Response – NRCS agrees with the Office of the Inspector General and has drafted procedures to ensure that appraisals are conducted, title reviews occur, and conservation planning requirements are met before issuing payment. NRCS has accomplished this step by revising the procedures contained in the Conservation Programs Manual, Part 519, and through training with the FPP State program managers.

The Natural Resources Conservation Service provides leadership in a partnership effort to help people conserve, maintain, and improve our natural resources and environment.

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Recommendation #3 – Implement periodic monitoring of the FPP by the Oversight and Evaluation Staff.

NRCS Response – NRCS agrees with the Office of the Inspector General and will have the NRCS Oversight and Evaluation Staff conduct periodic program reviews of the FPP.

Recommendation #4 – Deobligate all fiscal year 1996 funds provided to the State of California that remained unused as of October 1, 2001.

NRCS Response – The NRCS California State Office has disbursed funds to the cooperating entities for the purchase of two easements. The attached Commodity Credit Corporation statement documents disbursement of the 1996 funds.

If you have any questions about this response, please do not hesitate to contact me.

A handwritten signature in black ink, appearing to read "Bruce I. Knight", with a large, sweeping flourish at the end.

BRUCE I. KNIGHT
Chief

Attachment